

# **MELLON SECURITIES FAIR FUND** **STATEMENT TO ELIGIBLE INVESTORS**

## **INTRODUCTION**

This statement is applicable if you have received a payment from the BNY Mellon Securities Distribution Fund (hereinafter, "Mellon Securities Fair Fund" or "Fair Fund"), a Fair Fund established by the United States Securities and Exchange Commission ("SEC") as a result of the settlement of proceedings brought by the SEC in *In the Matter of BNY Mellon Securities LLC*, SEC Admin. Proc. File No. 3-14191, and *In the Matter of Mark Shaw*, SEC Admin. Proc. File No. 3-14192 (hereinafter, "BNY Mellon" and "Shaw, respectively; or "Respondents," collectively).

Your payment has been calculated based on information contained in the records of Respondents and third-party intermediaries. This payment is intended to compensate you for harm to your investment(s) due to Respondents' failure to meet the duty of best execution in certain cross trades ("Identified Conduct") during the period spanning from approximately November 1999 through March 31, 2008 (the "Relevant Period").

This Statement to Eligible Investors ("Statement") provides information to help you determine the U.S. federal income tax consequences of the distribution payment if you are a citizen or resident of the U.S. for U.S. federal income tax purposes.

**YOU SHOULD NOT RELY ON THIS STATEMENT AS TAX ADVICE.  
CONSULT YOUR TAX ADVISOR WITH RESPECT TO THE SPECIFIC TAX  
CONSEQUENCES OF THE DISTRIBUTION PAYMENT, INCLUDING THE  
EFFECTS OF U.S. FEDERAL, STATE, LOCAL AND NON-U.S. TAX RULES  
AND THE EFFECT OF POSSIBLE CHANGES IN LAWS.**

On January 14, 2011, the SEC issued orders instituting and simultaneously settling administrative and cease-and-desist proceedings against Respondents ("Orders"). Pursuant to the Orders, Mellon Securities was required to pay disgorgement of \$19,297,016, prejudgment interest of \$3,748,431 and a civil money penalty of \$1,000,000 for a total of \$24,045,447, while Shaw was required to pay disgorgement of \$195,300, prejudgment interest of \$23,291 and a civil money penalty of \$150,000, for a total of \$368,591. In total, the Orders require Respondents to pay disgorgement of \$19,492,316, prejudgment interest of \$3,771,722 and civil money penalties of \$1,150,000.

The Orders required BNY Mellon to retain an Independent Distribution Consultant ("IDC") not unacceptable to the SEC's Division of Enforcement to develop a distribution plan ("Distribution Plan") for the distribution of monies

ordered to be paid by Respondents. BNY Mellon retained Alan Friedman, Vice President of Charles River Associates, Inc. to serve as the IDC.

On February 28, 2014 the SEC approved a Distribution Plan, which provides for distribution of the disgorgement, penalties and interest paid by Respondents, plus accumulated interest. This amount, less taxes paid by the Qualified Settlement Fund described below, is available for distribution proportionately to Plan Customers whose investments were harmed by the Identified Conduct (“Eligible Investors”).

The Fair Fund is a Qualified Settlement Fund (“QSF”) under the Internal Revenue Code. Damasco & Associates LLP (“Damasco”) was appointed by the SEC as the Tax Administrator for the Fair Fund. Damasco has participated in the preparation of this Statement, but is not providing services or advice to you or any other Eligible Investor receiving a distribution payment.

Some Eligible Investors may be subject to special tax rules, such as, without limitation, non-U.S. investors, investors who hold or held shares in a tax-qualified retirement plan or an individual retirement account (“IRA”) (except as specifically discussed below), or investors that are tax-qualified retirement plans. This Statement does not address the tax consequences under any state, local or non-U.S. tax laws, or the alternative minimum tax provisions of the Internal Revenue Code.

### **COMPONENTS OF THE DISTRIBUTION PAYMENT**

The Order provides that the Distribution Plan shall be distributed “in a manner that compensates fairly and proportionately the Plan Customers [Eligible Investors] for losses attributable to cross trades conducted on their behalf by the Respondent” during the Relevant Period. Accordingly, your distribution payment is comprised of a “losses” component and an “interest” component. The losses component is attributable to the disgorgement and civil money penalties that Respondents were required to pay pursuant to the Orders. This component is intended to compensate you for the losses you sustained as a result of the Identified Conduct with respect to shares of the various investments<sup>1</sup> you held during the Relevant Period. The interest component is attributable to prejudgment interest that Respondents were required to pay pursuant to the Orders. The distribution payment calculations were performed under the direction of the IDC.

Each of these components has different tax consequences (discussed below).

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<sup>1</sup> References to “investments” throughout this Statement means shares of certain securities that were traded (purchases and/or sales) for your account(s) through the Respondent during the Relevant Period to which your distribution payment relates.

## A. Losses Component

The losses component comprises 84.55% of your distribution payment. The losses component of your distribution payment is intended to compensate you for harm to your investment(s) caused by the Identified Conduct. In order to determine the tax consequences of the losses component, you should first allocate the losses component among the various investment(s) you held during the Relevant Period in a reasonable manner according to your holdings.

*Example 1:* You held 50 shares of Security A with a tax basis of \$50 and 100 shares of Security B with a tax basis of \$100 in each year of the Relevant Period. You receive a distribution payment containing a \$150 losses component. It would be reasonable to allocate \$50 of the losses component to Security A and \$100 of the losses component to Security B.

The losses that you have allocated to a particular investment is not income to you to the extent it does not exceed your basis in the shares of that investment; however, you must adjust your basis downward by the amount you have allocated to those shares (generally, your basis is the amount you paid for your shares). If the amount of the losses component that you have allocated to a particular investment exceeds your tax basis in that investment, then the excess is includable in your income as capital gain. Any such capital gain is long-term capital gain, unless you disposed of your investment before holding it for longer than one year.

*Example 2:* You have a basis of \$100 in your investment. You have allocated \$10 of the losses component of your distribution to that investment. You do not have gross income as a result of the losses component of your distribution allocated to that investment *BUT* your basis is reduced to \$90 for purposes of determining gain or loss in the future (\$100 basis less \$10 losses component = \$90).<sup>2</sup>

*Example 3:* You have a basis of \$400 in your investment. You have allocated \$1,000 to the losses component of your distribution to that investment. You apply \$400 of the losses component to reduce your basis to zero for purposes of determining gain or loss in the future *AND* you include the remaining \$600 in income as taxable gain on your investment.

*Example 4:* You have sold all of your shares in an investment to which the distribution relates and the losses component of the

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<sup>2</sup> If you use the specific identification method of determining basis when shares are sold (as opposed to the dollar cost averaging method), your basis must be allocated among the shares in a reasonable manner.

distribution allocated to that investment is \$1,000. Generally, you will include the \$1,000 in income as additional taxable gain from your shares. If you have sold only a portion of your shares in that investment, you should make a reasonable allocation of the distribution between the shares you have sold and the shares you retain. The portion allocated to the sold shares is treated as described in this Example 4 and the portion allocated to the retained shares is treated as described in Examples 2 and 3.

If you do not have reasonable access to records indicating the tax basis of your investment, then you may assume that your tax basis is zero and that the entire losses component of your distribution allocated to a particular investment is includable in your income as capital gain. Any such capital gain is long-term capital gain, unless you disposed of your investment before holding it for longer than one year.

**The Fair Fund will not issue a Form 1099 to you for the losses component of your distribution payment. The Fair Fund is not required to report the losses component of the distribution.<sup>3</sup> Nevertheless, you should consult with your tax advisor as to how to report any portion of the losses component that is taxable to you as described in Examples 3 and 4.**

B. Interest Component

The interest component comprises 15.45% of your distribution payment. The interest component constitutes taxable interest income to you.

**Pursuant to the Internal Revenue Code and Treasury regulations, the Fair Fund will issue a Form 1099-INT to you reporting this interest only if the interest component of your distribution payment equals or exceeds \$600.**

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<sup>3</sup> This conclusion is consistent with guidance from the Internal Revenue Service (“IRS”) with respect to payments to injured investors from Fair Funds established by the SEC in other proceedings involving market timing. For example, see the following IRS Private Letter Rulings (“PLRs”) obtained by the Tax Administrator in other proceedings: 200645008, 200645017, 200646010, 200701001, 200702006, 200702008, 200702009, 200702010, 200702011, 200702012, 200702048, 200703008, 200703009, 200703010, 200703034, 200712004, 200712005, 200722004 and 200722025. You may obtain copies of these PLRs from the IRS’ web site, [www.irs.gov](http://www.irs.gov). Although the Fair Fund does not have a Form 1099 reporting obligation, such determination does not affect nor imply the tax consequence of a distribution payment *in the hands of an Eligible Investor*. The payments may, in whole or in part, constitute income, as discussed in Examples 3 and 4, even though no 1099s will be issued to Eligible Investors. Please note: there may be some circumstances in which the Fair Fund will issue information returns and will report payments to the IRS; however, these circumstances are beyond the scope of this Statement.

## **SPECIAL ISSUES FOR INVESTMENTS HELD IN IRAS OR TAX-QUALIFIED RETIREMENT PLANS**

### A. Distributions to IRA Accounts

**Please follow the applicable instructions below if you received a check that is associated with an IRA.<sup>4</sup>**

#### 1. For Checks Payable to the Custodian but Mailed to the Investor

a. If you held some or all of your investment through an IRA, in most cases the distribution check will have been made payable to your IRA custodian but mailed directly to you. You may choose to forward the check to your custodian with a letter of instruction or, to review your options, contact the Administrator of the Fair Fund (“Fair Fund Administrator”) at 1-888-213-9043.<sup>5</sup> You should deposit the check in your IRA account. Caution: If the check is cashed or deposited in any account other than an account eligible to receive the check, it may be subject to a 10% penalty and taxed as ordinary income in the year of receipt.

b. If your IRA custodian has changed, you may be able to transfer the payment to another custodian, or roll the payment over to another IRA or eligible account. Please contact the Fair Fund Administrator at 1-888-213-9043 to review your options. Caution: Please consult with your tax advisor because the rules related to transfers and rollovers are complicated and failure to comply with those rules could subject the payment to income tax and a 10% penalty.

c. If you no longer hold your IRA, please contact the Fair Fund Administrator at 1-888-213-9043 to review your options.

#### 2. For Checks Payable to the Investor and Mailed to the Investor

If the distribution check was made payable to you (as opposed to the custodian of your IRA) because of the way your account was registered in the records obtained for the distribution, please contact the Fair Fund Administrator immediately at 1-888-213-9043 to receive instructions to get a replacement distribution check made payable to the custodian of your IRA. Caution: If you cash the check, or deposit it in any account other than an account eligible to receive the check, it

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<sup>4</sup> As a general rule, distribution payments from the Fair Fund received as a result of the investment held by your IRA do not constitute a “contribution” to your IRA for purposes of determining your maximum yearly contribution to your IRA.

<sup>5</sup> The IDC retained Boston Financial Data Services to serve as the Administrator of the Fair Fund.

may be subject to a 10% penalty and be taxed as ordinary income in the year of receipt.

Additional information on this topic is available on the IRS web site, [www.irs.gov](http://www.irs.gov), Tax Topic 451 and Publication Number 590.

B. Distributions to Tax-Qualified Retirement Plans

1. Checks Mailed to Your Retirement Plan

If you held some or all of your investment(s) through a tax-qualified retirement plan, in most cases the distribution check was made payable and mailed to your tax-qualified retirement plan.<sup>6</sup> Plan fiduciaries are responsible for allocating these funds. Please contact your plan fiduciary if you have questions.

2. Checks Mailed to You

**Please follow the applicable instructions below if you received a check that is associated with a tax-qualified retirement plan.**

In limited instances, the distribution check was mailed to you and made payable to either: (i) your retirement plan; or (ii) you because of the way your account was registered in the records obtained for the distribution.

a. For A Check Payable to Your Retirement Plan but Mailed to You

In some instances the check payable to your tax-qualified retirement plan was mailed to you because your address was the address of record. If *you* received a check made payable to your tax-qualified retirement plan, please follow the directions in i. or ii., below.

i. If you are still a participant in the tax-qualified retirement plan, contact your retirement plan trustee/administrator to coordinate the deposit of the check to your retirement plan.

ii. If you are no longer a participant in the tax-qualified retirement plan to which the distribution is directed, please contact the trustee/administrator of your former tax-qualified retirement plan to determine the appropriate course of action. If you have difficulty making contact with your former

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<sup>6</sup> As a general rule, distribution payments from the Fair Fund received as a result of an investment held in or by your tax-qualified retirement plan do not constitute a "contribution" to your plan for purposes of determining your maximum yearly contribution to your plan or for purposes of determining your employer's contributions to your plan.

plan trustee/administrator, consult your tax advisor or contact the Fair Fund Administrator at 1-888-213-9043.

b. For a Check Payable to You and Mailed to You

Distributions with respect to investments held by a tax-qualified plan should not be payable to individual investors. If you received such a check, this is an error likely due to the data available for the distribution. If you received a distribution check made payable to you in connection with an investment held by your tax-qualified retirement plan, please contact the Fair Fund Administrator immediately at 1-888-213-9043.

Additional information on this topic is available on the IRS web site, [www.irs.gov](http://www.irs.gov), Tax Topic 558.