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Texas State Securities Board

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IN THE MATTER OF THE
DEALER REGISTRATION OF
SMH CAPITAL INC.

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Order No. IC08-CAF-20

TO: John T. Unger, Senior Vice President and General Counsel
SMH Capital Inc. (CRD No. 20580)
600 Travis, Suite 5800
Houston, TX 77002-3003

DISCIPLINARY ORDER

Be it remembered that SMH Capital Inc. ("Respondent"), by and through John T. Unger, its Senior Vice President and General Counsel, appeared before the Securities Commissioner of the State of Texas ("Securities Commissioner") and consented to the entry of this Order and the Findings of Fact and Conclusions of Law contained herein.

FINDINGS OF FACT

1. Respondent has waived (a) Respondent's right to notice and hearing in this matter; (b) Respondent's right to appear and present evidence in this matter; (c) Respondent's right to appeal this Order; and (d) all other procedural rights granted to the Respondent by The Securities Act, TEX. REV. CIV. STAT. ANN. art. 581-1 et seq. (Vernon 1964 & Supp. 2008) ("Texas Securities Act"), and the Administrative Procedure Act, TEX. GOVT CODE ANN. §2001.001 et seq. (Vernon 2000 & Supp. 2008) ("Administrative Procedure Act").
2. On or about September 30, 1987, Respondent registered with the Securities Commissioner as a securities dealer, which is currently effective.
3. On or about March 30, 2006, Respondent, a federal covered investment adviser, notice filed with the Securities Commissioner, which is currently effective.

Kevin Calandro

4. On or about October 31, 2002, Kevin Calandro ("Calandro") registered with the Securities Commissioner as an agent of Respondent, which is currently effective.

5. On or about April 14, 2004, Calandro registered with the Securities Commissioner as an investment adviser representative of SMH Capital Advisors, Inc. ("SMH Advisors"), a federal covered investment adviser notice-filed with the Securities Commissioner, which was terminated on February 14, 2007.
6. On or about June 23, 2006, Calandro applied for registration with the Securities Commissioner as an investment adviser representative of Respondent, which is currently pending.
7. During the registration process, the Staff of the Texas State Securities Board, ("Staff"), discovered that from on or about January 1, 2003 to on or about March 30, 2004, without first being registered as an investment adviser representative, Calandro provided investment advisory services on behalf of SMH Advisors.
8. During the registration process, Staff also discovered that from on or about January 1, 2003 to on or about March 30, 2004, Calandro failed to comply with written procedures of Respondent related to unregistered activity and Respondent failed to enforce such written procedures, as follows:
 - A. "All individuals engaged in activities...subject to registration requirements of SROs or other regulators must complete the necessary registration and licensing prior to engaging in such activities. Employees may not conduct business with public customers until required registrations or licenses are effective."
 - B. "No employee may engage in activities that require registration...unless registered in the appropriate capacities."

Calandro provided investment advisory services to customers of SMH Advisors without first being registered as an investment adviser representative. Respondent knew of Calandro's activity and failed to require Respondent Calandro obtain the required registration prior to providing investment advisory services to customers.

Kenneth Derek Thomson

9. On or about January 2, 2002, Kenneth Derek Thomson ("Thomson") registered with the Securities Commissioner as an agent of Respondent, which is currently effective.
10. On or about September 25, 2007, Thomson registered with the Securities Commissioner as an investment adviser representative of Respondent, which is currently effective.
11. On or about September 28, 2007, Thomson registered with the Securities Commissioner as an investment adviser representative of Calandro Advisory Services, Inc. ("CAS"), which is currently effective.

12. The Staff performed an inspection of CAS on or about November 6, 2007 and November 7, 2007 ("Inspection").
13. During the course of the Inspection, Staff discovered that from on or about April 8, 2003 to on or about September 28, 2007, without first being registered as an investment adviser representative, Thomson provided investment advisory services on behalf of CAS, with a percentage of the management fees he received being retained by Respondent.
14. During the course of the Inspection, Staff also discovered that from on or about April 8, 2003 to on or about September 28, 2007, Thomson failed to comply with written procedures of Respondent related to outside business activity, receipt of fees, and unregistered activity, and Respondent failed to enforce such written procedures.
 - A. The written procedures of Respondent related to outside business activity provided as follows:
 - 1) "Employees requesting approval to engage in outside business activities must complete the Outside Business Activity Request form and submit it to Compliance prior to engaging in the activity. Compliance will approve or disapprove the outside business activity in writing and notify the employee and the employee's supervisor."
 - 2) "RRs are prohibited from engaging in investment advisory services unless they are offering adviser services specifically authorized by the firm. If the RR has received permission from the firm to register as an investment adviser independent of the firm, the designated supervisor will ensure that the RR has disclosed this as an outside business activity. The designated supervisor will also be responsible for developing procedures to document the supervision of the RRs investment advisory business."
 - 3) "Independent Contractors." may be independently registered as investment advisers, however, the investment adviser activities are subject to the supervision of SMH."
 - 4) "It is the RR's responsibility to include accurate information and promptly notify SMH of any updates that may require amendment to Form U4". SMH will submit amendments to Form U4 when an RR advises of updates that require amendment."

Thomson failed to complete an outside business activity request form, engaged in investment advisory services independent of Respondent without authorization, and failed to properly notify Respondent of the need to update his Form U4. Since Respondent accepted a portion of the management fees received by Thomson, they knew or should have known of Thomson's activity and failed to approve such activity as provided in their procedures, failed to develop procedures to document the supervision of Thomson's investment advisory business, and failed to update his Form U4.

B. The written procedures of Respondent related to receipt of fees provided as follows:

- 1). "With few exceptions, regulators generally prohibit the sharing of commissions or compensation with non-registered persons. Any payment or sharing arrangement to a non-registered person must be referred to Compliance for review."
- 2) "SMH will not share in the profits of accounts under investment management except as permitted by rule. Any compensation arrangement with an investment adviser will be included in a written agreement between SMH and the adviser."

Thomson received management fees without referring his payment arrangement to compliance for review. Respondent shared in the receipt of Thomson's management fees without a written agreement in place and without requiring Respondent Thomson's payment arrangement be referred to compliance.

C. The written procedures of Respondent related to unregistered activity provided as follows:

- 1) "All individuals engaged in activities...subject to registration requirements of SROs or other regulators must complete the necessary registration and licensing prior to engaging in such activities. Employees may not conduct business with public customers until required registrations or licenses are effective."
- 2) "No employee may engage in activities that require registration...unless registered in the appropriate capacities."

Thomson provided investment advisory services to customers of CAS without first being registered as an investment advisor representative or having passed the appropriate licensing exam. Since Respondent accepted a portion of the management fees received by Thomson, they knew or should have known of Thomson's activity and failed to require Thomson obtain the required registration and take the appropriate licensing exam prior to providing investment advisory services to customers.

15. Pursuant to § 115.9(a)(6) of the Board Rules, each dealer registered with the Securities Commissioner must report to the Securities Commissioner any change in information previously disclosed to the Securities Commissioner within thirty (30) days of such change.

16. Pursuant to § 115.10(b)(1) of the Board Rules, a dealer is required to establish, maintain, and enforce written procedures to supervise the activities of its agents that are reasonably designed to achieve compliance with the Texas Securities Act and Board Rules.

17. Pursuant to Section 14.A(6) of the Texas Securities Act, the Securities Commissioner may reprimand a person registered under the Texas Securities Act if the person has violated any of the provisions of the Texas Securities Act or Board Rules.

18. Pursuant to Section 23-1 of the Texas Securities Act, the Securities Commissioner may assess an administrative fine against any person found to have engaged in an act or practice that violates the Texas Securities Act or Board Rules.

CONCLUSIONS OF LAW

1. Respondent's failure to enforce a system reasonably designed to achieve compliance with the Texas Securities Act and Board Rules constitutes a violation of § 115.10(b)(1) of the Board Rules.
2. Respondent's failure to disclose Thomson's outside business activity to the Securities Commissioner on the Form U-4 constitutes a violation of § 115.9(a)(6) of the Board Rules.
3. Pursuant to Section 14.A(6) of the Texas Securities Act, the foregoing violations constitute bases for the issuance of an order reprimanding a dealer.
4. Pursuant to Section 23-1 of the Texas Securities Act, the foregoing violations of the Board Rules constitute bases for the issuance of an order assessing an administrative fine against a dealer.

ORDER

1. It is ORDERED that SMH Capital Inc. is hereby REPRIMANDED.
2. It is further ORDERED that SMH Capital Inc. is ASSESSED AN ADMINISTRATIVE FINE in the amount of Thirty Thousand Dollars (\$30,000). Payment shall be made by delivery of a cashier's check to the Securities Commissioner in the amount of Thirty Thousand Dollars (\$30,000), payable to the State of Texas, contemporaneously with the delivery of this Order.
3. It is further ORDERED that SMH Capital Inc. COMPLY with the terms of the Undertaking incorporated by reference herein.

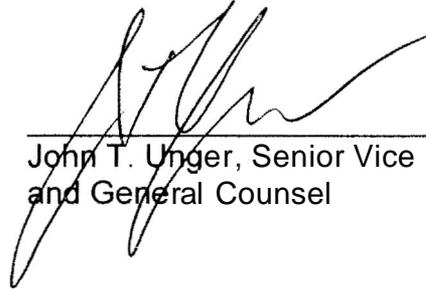
SIGNED, AND ENTERED by the Securities Commissioner this 20th day of November, 2008.



DENISE VOIGT CRAWFORD
Securities Commissioner

Respondent:

SMH Capital Inc.



John T. Unger, Senior Vice President
and General Counsel

Approved as to Form:



Benette L. Zivley
Director
Inspections and Compliance Division

ACKNOWLEDGMENT

On the 12th day of November, 2008, SMH Capital Inc. ("Respondent"), by and through John T. Unger, its Senior Vice President and General Counsel, appeared before me, executed the foregoing Order and acknowledged that:

1. John T. Unger is duly authorized to enter into the foregoing Order on behalf of Respondent;
2. John T. Unger has read the foregoing Order;
3. Respondent has been fully advised of its rights under the Texas Securities Act and the Administrative Procedure Act;
4. Respondent knowingly and voluntarily consents to the entry of the foregoing Order and the Findings of Fact and Conclusions of Law contained therein; and,
5. Respondent, by consenting to the entry of the foregoing Order, has knowingly and voluntarily waived its rights as set forth therein.



 Notary Public in and for
 the State of Texas

[affix notary seal here]

My Commission Expires: 11/4/12

