

**MEMO# 15734**

March 7, 2003

## **SEC SANCTIONS INDIRECT SHAREHOLDER AND PRESIDENT OF INVESTMENT ADVISER FOR SALE AND REDEMPTION OF FUND SHARES AT INFLATED NET ASSET VALUE**

[15734] March 7, 2003 TO: COMPLIANCE ADVISORY COMMITTEE No. 19-03 INVESTMENT ADVISER ASSOCIATE MEMBERS No. 5-03 INVESTMENT ADVISER MEMBERS No. 10-03 SEC RULES MEMBERS No. 27-03 RE: SEC SANCTIONS INDIRECT SHAREHOLDER AND PRESIDENT OF INVESTMENT ADVISER FOR SALE AND REDEMPTION OF FUND SHARES AT INFLATED NET ASSET VALUE The Securities and Exchange Commission recently accepted an offer of settlement and imposed sanctions in an administrative proceeding against an indirect shareholder and the president of an investment adviser.<sup>1</sup> The indirect shareholder also served as a director of the adviser and president and chief executive officer of the adviser's parent company. The president also served as a director of the adviser, vice president and chief operations officer of the adviser's parent, and vice president of the fund advised by the adviser. Each of these parties consented to the entry of the order, which is summarized below, without admitting or denying the Commission's findings. According to the order, the parent company of the investment adviser agreed to pay to a registered investment company advised by the adviser expenses that exceeded a certain amount. The fund recorded a receivable from the parent company for these expenses. From at least January 1999 through June 2000, this receivable was included as an asset in the fund's calculation of its net asset value. Although the parent company was insolvent during this time period, the fund, through its adviser, recorded the receivable on its books at full value, thereby inflating the fund's net asset value and causing the fund to sell and redeem shares at artificially high prices. As a result, one of the fund's portfolios experienced liquidity problems and improperly suspended redemptions. The order also states that the adviser did not advise the fund's shareholders or its private advisory clients who were invested in the fund about the doubtful collectability of the receivable. <sup>1</sup> In the Matter of Judy M. Rupay and Dixon R. Holman, SEC Release Nos. 33-8199, IA-2113 and IC-25960 (March 4, 2003). A copy of the order is available on the Commission's website at [www.sec.gov/litigation/admin/33-8199.htm](http://www.sec.gov/litigation/admin/33-8199.htm). <sup>2</sup> During this period, the fund also sold shares using an outdated prospectus and failed to file fiscal year-end annual reports. The order further notes that the fund failed to provide its shareholders with a semi-annual report for the year ended December 31, 1999.<sup>2</sup> Based upon this conduct, the Commission found that:

- the adviser engaged in transactions, practices or courses of business that violated Section

206(2) of the Investment Advisers Act of 1940 and Section 34(b) of the Investment Company Act of 1940 and the indirect shareholder and president willfully aided and abetted and caused the adviser's violations; and • the indirect shareholder and president of the investment adviser willfully aided and abetted and caused the fund's violations of Sections 21(b), 22(e), 30(a) and 30(e) of the Investment Company Act and Rules 22c-1, 30a-1 and 30d-1 thereunder, and Section 5(b) of the Securities Act of 1933. Based upon these findings, the respondents were ordered to cease and desist from committing or causing any violation and any future violation of the provisions of law they were found to have violated. In addition, they were prohibited from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter for a period of six months, and each ordered to pay a civil penalty of \$10,000. Anu Dubey Assistant Counsel 2 The order indicates that, in a related civil injunctive action, the adviser and its parent company, without admitting or denying the Commission's allegations, consented to permanent injunctions enjoining each entity from future violations of the federal securities laws. A court-appointed special master liquidated the fund's assets and distributed the proceeds to the fund's shareholders. During the liquidation of the fund, the parent company fully paid the receivable. See SEC v. Rupay-Barrington Capital Management, Inc., et al., Civ. No. 3:00-CV-1482-D (N.D. Tex.) (SEC Litigation Release No. 17345) (January 29, 2000). A copy of the release is available on the Commission's website at [www.sec.gov/litigation/litreleases/lr17345.htm](http://www.sec.gov/litigation/litreleases/lr17345.htm).

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