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INVESTMENT ADVISER AND ITS PRESIDENT SETTLE SEC FRAUD CHARGES RELATING TO MISSTATED VALUATIONS OF FUND PORTFOLIO SECURITIES

[17948] September 3, 2004 TO: CHIEF COMPLIANCE OFFICER COMMITTEE No. 4-04 COMPLIANCE ADVISORY COMMITTEE No. 86-04 SEC RULES MEMBERS No. 124-04 SMALL FUNDS MEMBERS No. 96-04 RE: INVESTMENT ADVISER AND ITS PRESIDENT SETTLE SEC FRAUD CHARGES RELATING TO MISSTATED VALUATIONS OF FUND PORTFOLIO SECURITIES The Securities and Exchange Commission has issued an order making findings and imposing sanctions in an enforcement proceeding against a registered investment adviser to a group of mutual funds ("Funds") and the adviser's president (collectively, "Respondents").1 The Respondents consented to the entry of the SEC Order without admitting or denying the SEC's findings. The action, which is summarized below, involved allegations that the Respondents: (i) misled Fund shareholders about the nature and value of the Funds' investments in illiquid securities; and (ii) failed to oversee effectively personal trading at the firm. I. Findings The SEC Order finds that from 1999 through 2001, the Funds' Statements of Additional Information stated that the Funds would not acquire illiquid securities if such purchases would cause more than 15 percent of any Fund to be invested in illiquid securities. During this period, according to the SEC Order, the president categorized as liquid various securities that were subject to "lock-up" agreements that committed the Funds to hold the securities for six months. The SEC Order finds that these mischaracterizations caused the Funds to understate significantly their investments in illiquid securities and to exceed the 15 percent limit. The SEC Order further finds that the president repeatedly caused the Funds to purchase new illiquid securities when their illiquid portfolios already exceeded the 15 percent limit. In addition, the SEC Order finds that from December 2000 through Fall 2001, the Respondents knowingly or 1 See In the Matter of Garrett Van Wagoner and Van Wagoner Capital Management, Inc., SEC Release Nos. IA-2281 and IC- 26579, Admin. Proc. File No. 3-11611 (Aug. 26, 2004) ("SEC Order"). Copies of the SEC Order and accompanying press release are available at http://www.sec.gov/litigation/admin/ia-2281.htm and http://www.sec.gov/news/press/2004-122.htm, respectively. 2 recklessly lowered the Funds' valuations for several illiquid securities – in some cases to zero – in an attempt to meet the 15 percent limit, thereby causing the Funds to understate their net asset values. The SEC Order also finds that the president, who also served as the adviser's compliance officer, failed to administer the firm's Code of Ethics. Specifically, it finds that the president did not review the quarterly transaction reports submitted by the firm's employees and, as a result, he failed to detect that an employee traded in the same public equity securities as the

Funds and omitted those trades from her reports for more than one year.2 It further finds that the president, when alerted to the prohibited trading based on new reports submitted by the employee, did not cause the trading to be halted or discipline the employee. In addition, the SEC Order finds that the president was aware that a director of the Funds was investing in private equity securities in which the Funds were simultaneously investing, without having received prior approval from the SEC.3 As a result of the conduct generally described above, the SEC Order finds that the adviser willfully violated, and the president willfully aided and abetted and caused the adviser's violations of: (i) Section 17(j) of the Investment Company Act of 1940 and Rule 17j-1(c)(2) under that Act; and (ii) the antifraud provisions of Sections 206(1) and (2) of the Investment Advisers Act of 1940.4 The SEC Order also finds that the Respondents willfully aided and abetted and caused the Funds' violations of Rule 22c-1 under the Investment Company Act. II. Sanctions and Undertakings The SEC Order censures the Respondents, imposes a cease and desist order, and requires the Respondents to pay a civil money penalty of $800,000. It also requires the Respondents to comply with the undertakings summarized below. The president, who has submitted his resignation from the Funds' Board effective December 31, 2004, undertakes the following: • to resign as an officer of the Funds effective December 31, 2004, and not to transact any Fund business without a second signatory until his resignation is effective; • not to serve as an officer or director for any registered investment company for a period of seven years beginning December 31, 2004; 2 The employee settled SEC charges that her conduct violated Section 17(j) of the Investment Company Act of 1940 and Rule 17j-1(d) thereunder. See In the Matter of Audrey L. Buchner, SEC Release Nos. IA-2282 and IC-26580, Admin. Proc. File No. 3-11612 (Aug. 26, 2004), which is available at http://www.sec.gov/litigation/admin/ia-2282.htm. 3 The director, who resigned from the Funds' board in July 2000, settled SEC charges that his conduct violated Rule 17d-1(a) under the Investment Company Act. See In the Matter of Robert S. Colman, SEC Release No. IC-26581 (Aug. 26, 2004), which is available at http://www.sec.gov/litigation/admin/ic-26581.htm. 4 Rule 17j-1(c)(2) under the Investment Company Act requires funds and investment advisers to use reasonable diligence and institute procedures reasonably necessary to prevent violations of the fund's or the adviser's code of ethics. 3 • not to serve on the Funds' Pricing Committee, effective immediately; • for a period of seven years, to abstain from making recommendations on the adviser's behalf to: (1) the Funds' Pricing Committee about any valuation changes to private equities; and (2) the Funds' Board about which securities are liquid or illiquid; and • to recommend to the Funds' Board that it add two independent directors acceptable to the SEC staff. The adviser undertakes the following: • to submit to the Funds' Pricing Committee, in advance, all future pricing changes regarding private equities and all future determinations regarding the liquidity of any security; • to hire an independent consultant acceptable to the SEC staff to review the pricing and liquidity determinations for the four quarters following the date of the SEC Order and to make recommendations concerning the adviser's policies, procedures, and practices for pricing and liquidity determinations for private equity securities; and • to implement the independent consultant's recommendations, although the adviser may suggest alternative procedures to achieve the goals of those recommendations. Finally, the Respondents each undertake to abstain from making, on behalf of the Funds, any new private equity investments or any valuation changes to private equity investments until after the new investments or valuation changes have been approved by the Funds' Pricing Committee. Rachel H. Graham Assistant Counsel

should not be considered a substitute for, legal advice.