

MEMO# 5257

October 25, 1993

SEC SANCTIONS MUTUAL FUND ADVISER FOR VIOLATIONS OF THE 1940 ACT

October 25, 1993 TO: COMPLIANCE COMMITTEE NO. 26-93 INVESTMENT ADVISERS
COMMITTEE NO. 29-93 SEC RULES COMMITTEE NO. 93-93 RE: SEC SANCTIONS MUTUAL
FUND ADVISER FOR VIOLATIONS OF THE 1940 ACT

The Securities and Exchange Commission instituted proceedings against an investment adviser to two mutual funds ("Adviser") to determine whether the Adviser (1) caused violations of Sections 17(a)(1) and (2) and 17(d) of the Investment Company Act of 1940 and Rule 17d-1 thereunder (which generally prohibit joint and affiliated transactions), and (2) failed reasonably to supervise one of its portfolio managers with a view to preventing violations of these provisions and of Section 31(a) of the Investment Company Act and Rule 31a-1(b)(6) thereunder (which impose certain recordkeeping requirements). Pursuant to an offer of settlement, the Adviser, without admitting or denying the Commission's findings, consented to the issuance of an order instituting the proceedings and imposing certain remedial sanctions. According to the Commission's order, a portfolio manager then associated with the Adviser frequently delayed designation of the account for which trades in Standard & Poor's 500 Stock Index Futures were being conducted until after the trades were effected. The Commission found that the portfolio manager allocated more favorable trades to a private profit-sharing plan for the Adviser's employees and less favorable trades to two mutual funds managed by the Adviser. As a result, the Commission found that the Adviser caused the profit-sharing plan to engage as a principal in futures transactions under a joint arrangement with the mutual funds, in violation of the Investment Company Act. The Commission also found that this trading activity resulted in the Adviser causing the profit-sharing plan, acting as principal, to engage with the mutual funds in purchase and sale transactions prohibited by the Act. Finally, the Commission found that the Adviser failed reasonably to supervise the portfolio manager with a view to preventing these violations and violations of certain record-keeping requirements under the Act. The Commission ordered that the Adviser cease and desist from committing or causing the violations described above; that it be censured; that it pay \$9.2 million to be distributed for the benefit of shareholders, which will satisfy both the SEC and Commodity Futures Trading Commission proceedings against the Adviser; and that it retain an independent consultant to review the Adviser's policies and procedures related to trading in connection with its investment advisory and investment company operations. A copy of the Commission's order is attached. Paul Schott Stevens General Counsel

Attachment

abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.