

MEMO# 947

February 2, 1989

SEC SANCTIONS ADVISER FOR VIOLATIONS OF PERFORMANCE ADVERTISING RULES

February 2, 1989 TO: INVESTMENT ADVISER MEMBERS NO. 7-89 INVESTMENT ADVISER
ASSOCIATE MEMBERS NO. 7-89 RE: SEC SANCTIONS ADVISER FOR VIOLATIONS OF
PERFORMANCE ADVERTISING RULES

On December 27, 1988, the Securities and Exchange Commission brought proceedings against an investment adviser for violations of, among other things, a recent position taken by the Division of Investment Management concerning the investment adviser performance advertising rule. A copy of the administrative proceeding is attached. According to the SEC order, the adviser provided a market timing service for its clients. The SEC order states that the adviser (1) published advertisements that failed to disclose that the application of the adviser's timing signals to hypothetical investments in certain mutual fund combinations produced substantially different and, except for one fund, lower performance results than had been advertised; (2) advertised that the total gain and the compounded annual gain of a hypothetical investment in an unnamed mutual fund with the adviser's conversion signals applied were greater than they actually were; and (3) inaccurately advertised that the performance of a hypothetical investment in an unnamed mutual fund with the adviser's timing signals applied was superior to the performances of other indices to which this hypothetical investment's performance was compared. Moreover, the SEC's order stated that the adviser willfully violated Rule 206(4)-1(a)(5) by directly and indirectly publishing, circulating or distributing an advertisement that was misleading because the adviser failed to deduct advisory fees when computing and displaying the adviser's investment performance. (For additional discussion of this issue, see Memorandum to Investment Adviser Members No. 42-88 and Investment Adviser Associate Members No. 43-88, dated October 3, 1988.)

Robert L. Bunnan, Jr. Assistant General Counsel Attachment