

**MEMO# 5397**

December 10, 1993

# **SEC SANCTIONS AN INVESTMENT ADVISER'S OFFICER CONCERNING ITS ALLOCATION OF SECURITIES AND AGENCY CROSS TRANSACTIONS**

December 10, 1993 TO: COMPLIANCE COMMITTEE NO. 29-93 INVESTMENT ADVISER ASSOCIATE MEMBERS NO. 46-93 INVESTMENT ADVISER MEMBERS NO. 57-93 RE: SEC SANCTIONS AN INVESTMENT ADVISER'S OFFICER CONCERNING ITS ALLOCATION OF SECURITIES AND AGENCY CROSS TRANSACTIONS

The Securities and Exchange Commission recently sanctioned the former Chief Investment Officer (the "Officer") and head of the fixed-income desk of an asset management division of a registered investment adviser for causing and willfully aiding and abetting violations of the Investment Advisers Act of 1940 and the rules thereunder. The Commission's action was based on findings that certain securities transactions were not timely allocated to client accounts and that the Officer failed to obtain best price and execution for certain agency cross transactions. A copy of the Commission's order is attached. Specifically, the Commission found that the Officer failed to allocate purchase transactions in mortgage-backed securities to particular client accounts for periods of two to nine business days. The Officer's failure to write timely trade tickets allocating such transactions caused the investment adviser's books and records to be inaccurate and not current in violation of Section 204 of the Advisers Act and Rules 204-2(a)(3), 204-2(c)(1) and 204-2(c)(2) thereunder. In addition, the Commission found that the Officer caused two securities transactions to be executed between client accounts managed by the investment adviser without taking the necessary steps to ensure that best price and execution were obtained for the clients. By causing these transactions to be executed, the Officer was found to have breached the adviser's stated policy regarding the execution of cross transactions as well as its fiduciary duty under Section 206(2) of the Advisers Act, which has been interpreted to include the duty to obtain the best price and execution of client transactions. At a recent conference, Doug Scheidt, Assistant Director, Office of Enforcement Liaison of the SEC's Division of Investment Management, noted that the Commission had declined to allege a violation of Section 206(3) of the Advisers Act with respect to the agency cross transactions. He stated that this decision reflects the Commission's determination to reconsider the position it had taken in an earlier case in which the Commission had found that an adviser who had executed an agency cross transaction had "in effect acted as broker for both the Selling and the Purchasing Clients" for purposes of Section 206(3) of the Investment Advisers Act. (See In the Matter of Dimitri Balatsos; Memorandum to Investment Adviser Members No. 43-92, Investment Adviser Associate Members No. 35-92 and Compliance Committee No. 14-92,

dated September 23, 1992.) The Commission's characterization of the adviser as "in effect acting as a broker" had raised some concern in the industry about whether in any agency cross transaction, the adviser would be deemed to be "acting as broker" for purposes of Section 206(3). Amy B.R. Lancellotta Associate Counsel Attachment

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