21 October 2015

Practice Group(s):

Government Enforcement

Global Government Solutions

Investment Management, Hedge Funds and Alternative Investments

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SEC Enforcement Actions Against Investment Advisers

U.S. Government Enforcement Alert

By Jon Eisenberg

According to the SEC's most recent financial report, as of August 2014, SEC-registered investment advisers managed $62.3 trillion in assets.[1] Not surprisingly, investment advisers attract a great deal of attention from the SEC's Enforcement Division. The Division of Enforcement's Asset Management Unit has 75 professionals spread across all 12 SEC offices. The group has developed strong industry expertise: it includes more than a half-dozen former industry professionals and works closely with the examination teams of the Office of Compliance Inspections and Examinations, as well as with the Divisions of Investment Management and Economic and Risk Analysis. In the first 10 months of 2015, it brought over two dozen cases, resulting in over $190 million in settlements; nearly a dozen cases are being litigated.

The Investment Advisers Act of 1940 provides a powerful tool in the SEC's enforcement arsenal. In *SEC v. Capital Gains Research Bureau, Inc.,* 375 U.S. 180 (1963), the Supreme Court held that even though Section 206 of the Act nowhere mentions the word "fiduciary" and, instead, prohibits conduct that operates as a "fraud or deceit," the Act "reflects a congressional recognition 'of the delicate fiduciary nature of an investment advisory relationship,' as well as a congressional intent to eliminate, or at least to expose, all conflicts of interest which might incline an investment adviser — consciously or unconsciously — to render advice which was not disinterested." The Court added, "Courts have imposed on a fiduciary an affirmative duty of 'utmost good faith, and full and fair disclosure of all material facts,' as well as an affirmative obligation 'to employ reasonable care to avoid misleading' his clients." Subsequent Supreme Court cases have construed *Capital Gains* as recognizing a federal fiduciary duty for investment advisers. Perhaps in deference to the "fraud or deceit" language in Section 206, however, the Commission almost always alleges that the breach was accompanied by inadequate disclosure.

Recent SEC enforcement actions provide the best source of guidance on the ways investment advisers run afoul of their fiduciary and other obligations. While there are some variations each year, SEC enforcement actions against investment advisers have many similarities from year to year. Moreover, even when the nature of the conduct differs, the cases provide insights as to how the SEC will apply key principles in other contexts.

We have organized this year's SEC enforcement actions against investment advisers into the following 15 categories, each of which we discuss below:

1. The adviser took fees to which it was not entitled.
2. The adviser used fund assets to pay for expenses the adviser should have borne.

3. The adviser "cherry-picked" investments - allocating profitable trades to itself and less-profitable or losing trades to its clients.
4. The adviser failed to provide best execution to investors, because it chose a share class that was less favoable to clients than another share class.
5. The adviser misvalued illiquid assets, or misrepresented the basis for its valuation.
6. The adviser made investments violating a public pension fund client's investment restrictions.
7. The adviser inadequately disclosed conflicts of interest to investors, a compliance department, or a board of directors.
8. The adviser failed to provide independent directors with adequate or accurate information material to the renewal of the advisory contract for a registered investment company.
9. The adviser failed to satisfy the requirements that apply to the custody of client assets.
10. The adviser misrepresented or omitted facts regarding the nature of the investments being made.
11. The adviser misrepresented or omitted facts regarding the fund's performance, the assets under management, and/or the adviser's background and disciplinary history.
12. The adviser misrepresented or omitted facts regarding the risks of the investments.
13. The adviser failed to safeguard confidential account information.
14. The adviser waited too long to reimburse investors after it discovered errors.
15. The adviser failed to adopt adequate compliance procedures or failed to devote adequate resources to compliance.

I. Receipt of Unauthorized or Inadequately Disclosed Fees

Advisers are entitled to be paid for their services, but the fees they are paid should be consistent with any governing documents and clearly disclosed. The largest settlements in 2015 involved advisers who had received fees or expense reimbursements to which the Commission concluded they were not entitled

In one of the largest settlements this year, three related investment advisers to private equity funds agreed to pay nearly $39 million largely because the SEC concluded that they had not disclosed their receipt of “accelerated monitoring fees.”[2] The advisers disclosed that they charged monitoring fees to each portfolio company owned by the funds, which covered advisory and consulting services to the portfolio companies (typically for a 10-year period). The Commission concluded, however, that they did not adequately disclose that, before the private sale or initial public offering of certain portfolio companies, the adviser terminated the monitoring agreements and accelerated the payment of future monitoring fees. In announcing the settlement, the SEC enforcement staff stated, “Full transparency of fees and

conflicts of interest is critical in the private equity industry and we will continue taking action against advisers that do not adequately disclose their fees and expenses." The Commission brought the action and included a $10 million fine, even though it acknowledged a number of remedial steps that the advisers had taken. For example, it acknowledged that, prior to the SEC investigation, the advisers changed their practices and disclosed they would no longer accelerate monitoring fee payments when they exited a portfolio company through a private sale.

In a second case involving the receipt of fees, an investment adviser to collateralized debt obligation (CDO) clients agreed to pay $21 million because it retained "exchange fees" paid by issuers of securities held by the CDOs when the adviser recommended exchange transactions to CDO clients.[3] Exchanges are transactions in which the CDO returned the issuer's securities to that issuer, in return for new securities and/or other consideration. The collateral management agreement authorized the adviser to take specific actions with respect to exchanges, but did not provide for the receipt of exchange fees by the adviser. The Commission charged the adviser received exchange fees and sought to obscure them by referring to them as payment of "third-party costs." It also charged that the fees were not disclosed to clients, directors of the CDO vehicles, or in reports from the CDO trustee to investors. The Commission also sanctioned a managing director of the adviser, who drafted language in exchange transaction documents that characterized the exchange fees as compensation for third-party costs; and the chief legal officer, who reviewed and approved the receipt of exchange fees. In announcing the settlement, the Commission's enforcement staff stated, "CDO managers have an obligation to act in the best interests of their CDO clients and communicate fairly with them. [The adviser] secretly diverted funds owed to CDO clients, and concealed that diversion and the conflicts it created."

II. Use of Fund Assets to Pay for Expenses Advisers Should Have Borne

Section 12(b) of the Investment Company Act makes it unlawful to use fund assets to pay for activities primarily intended to result in the sale of fund shares outside a written Rule 12b-1 plan approved by the board. In the first case brought under the SEC's "Distribution-in-Guise Initiative" (focusing on whether advisers are being reimbursed for distribution expenses in the guise of something else), an investment adviser and fund distributor agreed to pay nearly $40 million to settle SEC charges that they unlawfully caused their funds to pay nearly $25 million for distribution-related services, rather than making the payments out of the firms' assets.[4] Here, the payments were not covered by a written 12b-1 plan, and, while the respondents treated them as payments for "sub-TA [transfer agency] services," the SEC concluded that they were payments for distribution expenses. In announcing the settlement, the enforcement staff stated that the respondents "inappropriately used money belonging to the shareholders of the funds to pay for services clearly intended to market the funds and distribute their shares. Unless part of a 12b-1 plan, the firm should bear those costs, not the shareholders."

The Commission also brought an action against a mutual fund adviser for directing brokerage transactions to a broker-dealer for promoting fund shares without complying with Rule 12b-1(h), which requires the implementation of policies and procedures reasonably designed to, among other things, ensure the selection of brokers for portfolio securities is not influenced by considerations about the sale of shares of the fund.[5] It stated the adviser failed to create and maintain an approved list of executing brokers for the funds, and failed to

maintain documentation reflecting monitoring of the funds' compliance with the Rule 12b-1(h) policies and procedures. The matter was settled for $50,000, which included both the directed brokerage and a separate custody violation.

An investment adviser to private equity funds and other institutional investors agreed to pay $28.5 million because the private equity funds had reimbursed a large portion of the broken-deal expenses, but other co-investors had not paid for broken-deal expenses.[6] In that case, the adviser was permitted to allocate to the fund expenses that were incurred "by or on behalf of" the fund, but the SEC concluded that the funds had, in effect, also borne the broken-deal expenses of co-investors. In announcing the settlement, the SEC enforcement staff stated, "This is the first SEC case to charge a private equity adviser with misallocating broken deal expenses. Although [the respondent] raised billions of dollars of deal capital from co-investors, it unfairly required the funds to shoulder the cost for nearly all of the expenses incurred to explore potential investment opportunities that were pursued but ultimately not completed."

In a third case involving expense reimbursement, a hedge fund advisory firm was charged with improper allocation of fund assets to pay for the adviser's operating expenses, including office rent, employee salaries, and benefits.[7] The Commission's order stated the payments: 1) were not clearly authorized under the funds' operating documents and 2) were not accurately reflected in the funds' financial statements as related-party transactions. In addition to charging the firm, the SEC charged two executives for their involvement in the improper allocations, and the accountant who conducted the outside audit of the financial statements sent to investors. In announcing the settlement, the SEC enforcement staff stated that the adviser "did not make the proper disclosures for clients to decipher that the funds were footing the bill for many of the firm's operational expenses. Private fund managers must be fully transparent about the type and magnitude of expenses they allocate to the funds."

III. Improper Trade Allocations by "Cherry Picking" Favorable Trades

In a case being litigated, the Commission charged that an investment firm advisor purchased options in an omnibus or master account, and then delayed allocation of the purchases to either his or his clients' accounts until later in the day, after he saw whether or not the securities appreciated in value. According to the Commission's order instituting proceedings, his trades had an average first-day positive return of 6.28%, while his clients' trades had an average first-day loss of 5.05%.[8] In announcing the charges, the enforcement staff stated that the Division is engaged in a "data-driven initiative to identify potentially fraudulent trade allocations known as 'cherry-picking,' and this enforcement action is the first arising from that effort." Further, "Cherry-picking schemes can be extremely difficult to detect without an investor astutely noticing that something may be amiss and coming to us with a complaint about the adviser. We devised this initiative to identify specific custodians providing services to investment advisers and their clients and leverage their trading records and other data to efficiently target preferential trade allocations occurring outside the detection of even the most observant client."

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IV. Violation of the Duty of Best Execution by Choosing a More Expensive Share Class for Investors Eligible for a Less Expensive Share Class

In a settled proceeding, the Commission charged an investment adviser to a mutual fund and separately managed accounts violated its duty of best execution by selecting a more expensive share class for clients that would generate more fees for the adviser.[9] In that case, after the fund had been in existence for several years, it developed and launched a new "institutional share" class while retaining the original share class as the "investor share" class. The institutional share class had an expense ratio that was 25 points less than the investor share class. While the institutional share class had a minimum investment of $100,000 (compared to a $2,500 minimum investment for the investor share class), the fund permitted advisers to aggregate their clients' investments to qualify for purchase of the institutional share class, which meant that all of the adviser's clients qualified for the institutional share class. The Commission's order stated that the adviser made a decision not to convert certain customers to the institutional share class "because converting would have resulted in a reduction in fee revenue for [the adviser], and they viewed the fees collected from their clients through [the fund] as comparable to a negotiable investment advisory fee" and "did not believe they were required to convert their clients' [fund] holdings into the lower fee share class." The Commission concluded that by failing to place clients in the lower cost institutional share class, the adviser "failed to seek best execution for their clients on these transactions," and that the adviser also "did not adequately disclose to their clients … that they were eligible to invest" through the institutional share class, and "did not adequately disclose to their clients that they were not seeking best execution" or that "they had a conflict of interest in selecting the investor share class for their clients."

V. Improper Valuation of Illiquid Assets

Valuation issues continue to generate enforcement actions. In a case that settled for $5 million, the SEC charged a hedge fund advisory firm with using inflated, internally derived valuations for unlisted, thinly traded residential mortgage-backed securities, even though it claimed to be using independent price quotes from broker-dealers.[10] The Commission charged that the adviser supplied its own prices for broker-dealers to pass off as their own to the fund's administrator and auditor, and scripted the broker-dealer's conversation with the auditor. In announcing the settlement, the enforcement staff stated, "The integrity of the portfolio valuation process is critical to fund investors, especially when it involves illiquid securities. [The adviser] claimed to use market-grounded price quotes from brokers when in fact it relied on its own rosy view of market conditions to price its portfolio."

In a second improper-valuation case, which some of the respondents settled for $1.3 million, the Commission charged that in order to generate larger management fees, an investment adviser claimed that the fund had purchased an illiquid security (to which it then assigned an allegedly inflated value) when, in fact, it had purchased a different security of a publicly traded company with quoted stock prices.[11] In announcing the action, the enforcement staff stated, "[The adviser] manipulated the value of certain fund assets to manufacture millions of dollars in illusory profits that he used to line his pockets with fees he did not truly earn."

In a third valuation case, which is being contested, the Commission charged an adviser to funds with more than $2.5 billion in assets, much of which were invested in distressed loans, valued nearly all the loan assets at their price at acquisition even though many of the

borrowers had made only partial or no interest payments.[12] In announcing the action, the enforcement staff stated, "We allege that instead of informing their clients about the declining value of assets in the [collateralized loan obligation] funds, [the adviser] consistently misled investors and collected almost $200 million in fees and other payments to which they were not entitled. [The adviser] violated her fiduciary duty to her clients when she exercised subjective discretion over valuation levels, creating a major conflict of interest that she never disclosed to them."

VI. Violation of Public Pension Fund Clients' Investment Restrictions

In a case that is currently being litigated, the Commission charged that an investment adviser steered public pension fund clients to invest in alternative investment fund investments that did not comply with state law investment restrictions for public pension funds.[13] The order stated that in July 2012, the state of Georgia began to allow public pension plans to invest in alternative investments, subject to certain restrictions — for example, the pension plan's investment could not be more than 20% of the capital in the alternative fund, there had to be at least four other investors in the fund, and the fund had to have at least $100 million in assets. The Commission charged that the adviser steered public pension funds into alternatives investments, even though it knew the investments did not comply with the state law's restrictions. In announcing the contested action, the Commission stated, "[The adviser] breached a fiduciary duty to public pension fund clients by recommending investments it knew did not comply with legal requirements."

VII. Inadequately Disclosed Conflicts of Interest

The Asset Management Unit is, and has been for several years, particularly focused on the adequacy of disclosure of conflicts of interest by investment advisers. Indeed, Julie M. Riewe, the co-chief of the Asset Management Unit, entitled her February 26, 2015, remarks to the 17th Annual Investment Advisers Compliance Conference, "Conflicts, Conflicts Everywhere."[14] She stated, "In nearly every ongoing matter in the Asset Management Unit, we are examining, at least in part, whether the adviser in question has discharged its fiduciary obligation to identify its conflicts of interest and either (1) eliminate them, or (2) mitigate them and disclose their existence to boards or investors. Over and over again we see advisers failing properly to identify and then address their conflicts."

Three recent cases illustrate this. In one case, settled with a $20 million penalty, the Commission alleged that the adviser failed to disclose a $50 million loan that a senior executive of the adviser had received from an advisory client, and that the adviser had caused other advisory clients to invest in transactions in which the client who made the loan co-invested.[15] It stated the adviser made neither the compliance department nor other clients aware of the potential conflict of interest. In announcing the action, the enforcement staff stated, "As fiduciaries, investment advisors must be vigilant about disclosing all material facts to their clients, including actual and potential conflicts of interest. [The advisor] unlawfully failed to disclose the conflict of interest created by the outside business activity of one of its senior executives and the $20 million penalty reflects the significance of this and other regulatory failures."

In a second case, settled for $12 million, the Commission charged that an adviser should have disclosed to the fund's board of directors that one of the portfolio managers had founded a company that formed a joint venture with a publicly owned company; the fund had

a significant ownership interest in the publicly owned company.[16] In that case, the compliance department and others were aware of the investment, but did not escalate the issue to the board level, or disclose it to advisory clients. This is the only case to date in which the SEC charged, among other violations, a violation of SEC Rule 38a-1 under the Investment Company Act, which requires annual reports to the board of "each material compliance matter" that occurred since the date of the last report. The SEC also charged the chief compliance officer with causing certain violations, following which Commissioner Daniel M. Gallagher issued a statement explaining that he had dissented from that part of the Commission's action on the ground that the Commission should "strive to avoid the perverse incentives that will naturally flow from targeting compliance personnel who are willing to run into the fires that so often occur at regulated entities."[17] In announcing the settlement, enforcement staff stated, "[The advisor] violated its fiduciary obligation to eliminate the conflict of interest created by [the portfolio manager's] outside business activity or otherwise disclose it to [the] fund boards and advisory clients. By failing to make such disclosure, [the adviser] deprived its clients of their right to exercise their independent judgment to determine whether the conflict might impact portfolio management decisions."

In a third case, which is being litigated, the SEC charged that an investment adviser, without adequate disclosure of conflicts, caused clients to invest more than $40 million in companies in which the owner of the adviser had a significant interest.[18] The Commission charged that the adviser and others "abused their clients' trust and placed their own interests ahead of their clients' interests."

VIII. Inadequate Review of Investment Advisory Agreements

Section 15(c) of the Investment Company Act imposes a duty on board members of a registered investment company to request and evaluate, and a duty on the adviser to furnish, such information as may reasonably be necessary for the board to evaluate the terms of an investment advisory contract. Section 30(e) of the Act, and Rule 30e-1 thereunder, require that, following the board's approval or renewal of an advisory contract, the fund's next report to shareholders must discuss, in reasonable detail, the material factors and conclusions that formed the basis for the board's approval or renewal of the agreement.

In June, the SEC took the unusual step of bringing a settled action against trustees on two mutual fund boards and an investment adviser based on Section 15(c) violations.[19] The Commission's order states that the trustees, with the assistance of independent counsel, requested and received extensive information, but that, in some instances, they did not receive complete or accurate information in response to their requests. It stated that because the trustees did not follow up to obtain missing information, they violated Section 15(c) by approving the advisory contracts "without having all the information they requested as reasonably necessary for their evaluation" and that the adviser caused the fund to violate Section 30(e) and Rule 30e-1 by failing to provide an appropriate discussion of the 15(c) process in its March 2010 shareholder report. As part of the settlement, three trustees agreed to pay a penalty of $3,250 each and the adviser agreed to be jointly and severally liable for a $50,000 penalty. In announcing the settlement, the SEC enforcement staff stated that the trustees "fell short as the shareholders' watchdog by essentially rubber-stamping the adviser's contract and related fee."

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IX. Improper Handling of Fund Assets

The SEC's Custody Rule (Rule 206(4)-2) requires that advisers who have custody of client assets put in place a set of procedural safeguards to prevent loss of those assets. In addition, Section 17(f)(5) of the Investment Company Act states that if funds maintain securities in the custody of a qualified bank, the cash proceeds from the sale of such securities should also be kept in the custody of the bank.

In a recent settled enforcement action, the Commission charged that an investment adviser that managed approximately $3.5 billion in assets failed to ensure, for a nine-month period, that $247 million in cash collateral was maintained at the bank.[20] Instead, broker-dealer counterparties held the cash collateral. In announcing the settlement, the enforcement staff stated, "Mutual funds must ensure that all fund assets are properly protected. [The adviser] failed to implement the required policies and procedures to ensure all cash collateral was held in the custody of the funds' bank."

X. Misrepresentations or Omissions Regarding the Nature of the Investments

Investment advisers are required to provide accurate information about their investment strategy and their investments. The SEC charged that, during the financial crisis, an investment adviser for a registered investment company that had been marketed as a fund that primarily invested in distressed debt changed course by purchasing large amounts of credit default swaps (CDS), and that the change in investment strategy resulted in significant losses.[21] The Commission charged that the adviser failed to update the fund's offering memorandum to reflect the change from a long-credit investment strategy to a short-credit investment strategy, that the fund's shareholder reports misrepresented the investment strategy, and that the fund's investment letters inaccurately described the fund's CDS exposure. The Commission also charged that the change in investment strategy was not adequately disclosed to the fund's board. As part of the settlement, the advisers agreed to pay $17.5 million, which included disgorgement, compensation to investors, and a $3 million penalty. In announcing the settlement, the enforcement staff stated, "Advisers must provide investors and fund boards with accurate information about a fund's investment strategy. Here [the advisor] completely reversed the fund's strategy — from investing in distressed debt to betting against it — without adequately disclosing the change."

XI. Misrepresentations or Omissions Regarding a Fund's Performance, Assets Under Management, and/or the Adviser's Background and Disciplinary History

Each year, the Commission charges a number of advisers with misrepresenting a fund's performance, assets under management, or the adviser's background. Sometimes these charges are accompanied by allegations that the advisers stole the money that they raised, or sent bogus account statements, or conducted a Ponzi scheme. These charges are often accompanied by parallel criminal proceedings. As the cases cited in the endnote show, 2015 was no exception.[22]

SEC Enforcement Actions Against Investment Advisers

XII. Misrepresentations Regarding Investment Risks

The Commission charged that, in addition to a number of other violations, an investment adviser represented to clients his trading strategy was safe; involved little or no risk; and produced guaranteed, predictable profits when, in fact, the securities he purchased and held were high risk and volatile.[23] The investments included inverse exchange-traded funds and other securities known to be speculative and highly volatile. The Commission charged that the adviser "had no reasonable basis to predict the long term performance of these exchange traded products, which he knew or was reckless in not knowing were risky and speculative and which, if held long-term, would tend to result in losses."

XIII. Failure to Adopt and Implement Cybersecurity Policies and Procedures

Rule 30(a) of Regulation S-P under the Securities Act of 1933 requires every registered investment adviser (as well as brokers, dealers, and investment companies) to adopt written policies and procedures reasonably designed to insure the security and confidentiality of customer records, protect against any anticipated threats or hazards to such records and information, and protect against unauthorized access to or use of customer records or information that could result in substantial harm or inconvenience to any customer.

The SEC fined an investment adviser $75,000 for failing to establish required cybersecurity policies and procedures in advance of a breach that compromised the information of approximately 100,000 individuals, including thousands of the firm's clients.[24] The order stated the information was maintained on a third party-hosted web server; that in July 2013, the server had been attacked by an unknown hacker in China; and that prior to the attack, the firm had failed to conduct periodic risk assessments, implement a firewall, encrypt the personal information stored on the server, or maintain a response plan for cybersecurity incidents. Although the firm acted appropriately after the attack (retaining consultants, providing notice of the breach to every individual whose information may have been compromised, and offering free identity theft monitoring through a third party) and there was no indication of a client suffering financial harm from the attack, the Commission stated that the firm was required to have done more before the attack. In announcing the settlement, the enforcement staff stated, "As we see an increasing barrage of cyber attacks on financial firms, it is important to enforce the safeguards rule even in cases like this when there is no apparent financial harm to clients. Firms must adopt written policies to protect their clients' private information and they need to anticipate potential cybersecurity events and have clear procedures in place rather than waiting to react once a breach occurs."

XIV. Inadequate Response to the Discovery of Errors

The staff expects that when an investment adviser discovers an error, it will act promptly to reimburse clients who were affected by the error. In one case, the staff charged that, due to a coding error, the adviser inadvertently charged $6.5 million in asset management fees for investments it did not manage, which involved hundreds of millions of dollars of trades initiated by an institutional client.[25] The adviser identified the coding issue in or around January 2013, but waited a year to bring it to the attention of the client and almost another year to credit the management fees owed. In the same action, the Commission alleged that the adviser allocated $80 million worth of bonds of a particular issuer across 10 client accounts in a manner that conflicted with the underwriter's minimum allocation requirement.

It charged the adviser failed to follow its policies and procedures on documenting trade errors by mislabeling the trade error as a "trade fail" and a "trade revision" and failing to include all of the information required under the adviser's policies and procedures. The principal violation in that case, however, involved the failure to disclose a substantial loan, and it is unclear whether the inadequate response to the discovery of errors would have, by itself, led to an enforcement action.

XV. Inadequate Compliance Procedures or Compliance Resources

Many of the investment adviser enforcement cases include allegations of inadequate compliance procedures because they failed to address the violations at issue or were "off-the-shelf" compliance procedures not tailored to the adviser's business. In most cases, those allegations are secondary — the underlying substantive violations were clearly central.

In one 2015 case, however, the central claim was that the compliance program was inadequate.[26] The Commission stated that the firm hired a CCO who had limited prior experience and training in compliance; the CEO at the time failed to provide the CCO with sufficient guidance regarding his duties and responsibilities, and did not provide him with staff to assist with compliance; the CCO lacked experience, resources, and knowledge as to how to adopt and implement an effective compliance program; that, because of his other responsibilities, he was only able to devote 10%–20% of his time on compliance matters; he failed to complete timely annual compliance program reviews for 2009 or 2010; he told the then-CEO that he needed help to fulfill his compliance responsibilities, but the CEO delayed in providing additional resources; that a lack of resources contributed to the delay in completing annual compliance reviews; and a number of violations were uncovered during that review. The Commission charged the adviser violated Section 206(4) of the Act and Rule 206(4)-7, which require an investment adviser: (1) to adopt and implement written policies and procedures reasonably designed to prevent violations; and (2) review, at least annually, the adequacy of its policies and procedures and the effectiveness of their implementation. The Commission suspended the former CEO from association in a compliance capacity and supervisory capacity with any investment adviser for 12 months, ordered the firm to pay a civil money penalty of $150,000, and ordered the former CEO to pay a civil money penalty of $45,000.

In a second case, the Commission charged an investment adviser with violating Section 204A of the Investment Advisers Act, which requires investments advisers to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material nonpublic information, but did not charge an independent insider trading violation.[27] In that case, an investment adviser and its affiliated broker-dealer were found to have shared information with one another despite Information Barrier Procedures that were intended to ensure that they conducted business as separate and distinct organizations. The adviser shared information about, among other things, its 800,000 short position in an exchange-traded note that, because the issuer had suspended new issuances of the note, was trading at a premium, while the affiliated broker-dealer, which was a market-maker in the note, shared information about its trading positions, activities and strategies. The Commission also charged the broker-dealer with violating a similar provision under the Securities Exchange Act. In announcing the settlement, the enforcement staff stated, "The federal securities laws require not only careful establishment

of policies and procedures to prevent the misuse of material, nonpublic information, but also vigorous maintenance and enforcement of those policies and procedures."

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Looking forward, we can expect more of the same. In Ms. Riewe's February 2015 speech,[28] she stated that, for registered investment companies, the Asset Management Unit's priorities include valuation and performance, and the advertising of that performance; funds deviating from their investment guidelines or pursuing undisclosed strategies; boards and advisers failing to discharge their obligations under Section 15(c) when they evaluate advisory and other types of fee arrangements; and advisers causing funds to use fund assets to make distribution payments to intermediaries outside the funds' Rule 12b-1 plan. For hedge funds and private equity funds, she stated that the priorities included undisclosed fees, undisclosed conflicts, valuation issues, using proprietary risk analytics to identify hedge funds with suspicious returns, and undisclosed and misallocated fee and expense cases. For separately managed accounts and/or retail accounts, she stated that the priorities included conflicts of interest, fee arrangements, and compliance.

If one looks backwards, one would find considerable overlap with the 2015 categories. The overlap is not complete — for example, in the first 10 months of 2015, there were no market timing cases, no principal trading or cross-trade cases, no usurpation of investment opportunity cases, and no pay-to-play cases. Moreover, the 2015 cybersecurity case was new. But, as the saying goes, "history doesn't repeat itself but it does rhyme"; in most respects, the types of cases that arose in 2015 were the types of cases that arose before 2015, and are likely to be the types of cases that will arise in 2016 and beyond. For that reason, these cases provide a wealth of useful information that forward-looking advisers should consider as they evaluate their business practices, compliance programs, and supervisory procedures.

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1 Agency Financial Report: Fiscal Year 2014 at 123.
2 Investment Advisers Act Release No. 4219 (Oct. 7, 2015).
3 Securities Exchange Act Release No. 75814 (Sept. 2, 2015).
4 Investment Advisers Act Release No. 4199 (Sept. 21, 2015).
5 Investment Company Act Release No. 31455 (Feb. 12, 2015).
6 Investment Advisers Act Release No. 4131 (June 29, 2015).
7 Securities Exchange Act Release No. 74828 (Apr. 29, 2015).
8 Securities Exchange Act Release No. 75319 (June 29, 2015).
9 Investment Advisers Act Release No. 4126 (June 23, 2015).
10 Investment Advisers Act Release No. 4135 (July 1, 2015).
11 S*EC v. Summit Asset Strategies Investment Management*, Case 2:15-cv-01429, filed Sept. 4, 2015.
12 Investment Advisers Act Release No. 4053 (Mar. 30, 2015).
13 Securities Act Release No. 9789 (May 21, 2015).
14 Julie M. Riewe, "Conflicts, Conflicts Everywhere" Remarks to the IA Watch 17th Annual IA Compliance Conference: The Full 360 View," Feb. 26, 2015.
15 Investment Advisers Act Release No. 4163 (Aug. 10, 2015).
16 Investment Advisers Act Release No. 4065 (Apr. 20, 2015).
17 Commissioner Daniel M. Gallagher, "Statement on Recent SEC Settlements Charging Chief Compliance Officers With Violations of Investment Advisers Act Rule 206(4)-7," (June 18, 2015).

18 *SEC v. Lee Weiss et al.*, Case 1:15-cv-13460 (D. Mass., filed Sept. 29, 2015).
19 Investment Company Act Release No. 31678 (June 17, 2015).
20 Investment Company Act Release No. 31455 (Feb. 12, 2015).
21 Securities Act Release No. 9964 (Oct. 16, 2015).
22 E.g., *SEC v. Paul Lee Moore*, Case 3:15-cv-01575 (S.D. Cal., filed July 16, 2015); *SEC v. William J. Wells and Promitor Capital*, Case 1:15-cv-07738 (S.D.N.Y., filed Oct. 1, 2015); *SEC v. Michael Donnelly*, Civil Action No. 15-5873 (E.D. Pa. Oct. 19, 2015).
23 Securities Exchange Act Release No. 76079 (Oct. 5, 2015).
24 Investment Advisers Act Release No. 4204 (Sept. 22, 2015).
25 Investment Advisers Act Release No. 4163 (Aug. 10, 2015).
26 Investment Advisers Act Release No. 4126 (June 23, 2015).
27 Securities Exchange Act Release No. 76109 (Oct. 8, 2015).
28 Julie M. Riewe, "Conflicts, Conflicts Everywhere" Remarks to the IA Watch 17th Annual IA Compliance Conference: The Full 360 View," Feb. 26, 2015.

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