August 1, 2013

Investment Services Regulatory Update

New Rules, Proposed Rules and Guidance

SEC Adopts Rule Amendments to Implement JOBS Act Provisions for the Elimination of Prohibitions Against General Solicitation in Private Offerings

On July 10, 2013, the SEC adopted final amendments to Rule 506 of Regulation D and Rule 144A under the Securities Act in order to implement Section 201(a) of the Jumpstart Our Business Startups Act (JOBS Act). Section 201(a)(1) of the JOBS Act directed the SEC to eliminate the prohibition against general solicitation in private security offerings made under Rule 506 provided that all purchasers of the securities are accredited investors. New Rule 506(c) permits issuers to use general solicitation and general advertising in private security offerings made under Rule 506 provided that: (1) the issuer takes reasonable steps to verify that investors are accredited investors; (2) each investor qualifies, or the issuer reasonably believes that each investor qualifies, as an accredited investor at the time of the sale of securities; and (3) all terms and conditions of Rules 501, 502(a) and 502(d) are satisfied.

The SEC noted that whether the steps taken by an issuer to verify accredited investor status are "reasonable" is an objective determination based on the particular facts and circumstances of each investor and transaction. Factors to be considered in this analysis are:

(1) the nature of the purchaser and type of accredited investor that the purchaser claims to be;

(2) the amount and type of information that the issuer has about the purchaser; and

(3) the nature of the offering, such as the manner in which the purchaser was solicited to participate in the offering, and the terms of the offering, such as the minimum investment amount.

In response to commenters' requests, Rule 506(c) also provides a non-exclusive list of specific methods that investors may use to verify an investor's accredited investor status. This list includes:

(1) with respect to verifying income, review copies of any IRS form that reports income (e.g., W-2, Form 1099 or a copy of a filed Form 1040), along with a written representation that the investor will likely continue to earn the necessary income in the current year;

(2) with respect to verifying net worth, review copies of bank statements, brokerage or other statements of securities holdings, or CDs for evidence of sufficient net worth, along with a credit report for evidence of total liabilities; or

(3) obtain a written confirmation from a broker-dealer, an investment adviser, a licensed attorney or a certified public accountant that such entity or person has taken reasonable steps to verify the investor's accredited investor status.

Section 201(a)(1) of the JOBS Act also directed the SEC to revise Rule 144A(d)(1) to provide that securities resold pursuant to Rule 144A may be offered, including by means of general solicitation, to persons other than qualified institutional buyers (QIBs) as long as the securities are sold only to persons that the seller and any person acting on behalf of the seller reasonably believe is a QIB. The SEC adopted amendments to Rule 144A as directed under the JOBS Act.

The rule amendments become effective on September 23, 2013.

SEC Adopts Rule Amendments to Disqualify Felons and Other "Bad Actors" from Rule 506 Private Offerings

On July 10, 2013, the SEC adopted final amendments to Rule 506 of Regulation D under the Securities Act to disqualify issuers from relying on the Rule with respect to an offering if the issuer or certain other "covered persons" are subject to a "disqualifying event."

The rule amendments apply to all "covered persons," which include:

(1) the issuer and any predecessors and affiliated issuers;

(2) directors, executive officers, general partners or managing members of the issuer;

(3) officers of the issuer who are not executive officers but who are participating in the offering;

(4) beneficial owners of 20% or more of the issuer's outstanding voting equity securities;

(5) promoters connected with the issuer in any capacity at the time of a sale in the offering;

(6) persons compensated for the solicitation of purchasers in connection with the sale of securities in the offering (or any general partner, managing member, director or executive officer of such solicitor); and

(7) any investment manager of an issuer that is a pooled investment fund (or any general partner, managing member, director or executive officer of such investment manager).

The rule amendments identify various "disqualifying events" and any timeframe applicable to such events. Disqualifying events generally include:

(1) criminal convictions, court injunctions and restraining orders in connection with the purchase or sale of a security, making of a false filing with the SEC or arising out of the conduct of certain types of financial intermediaries;

(2) final orders from the Commodity Futures Trading Commission, federal banking agencies and certain other federal and state financial regulatory entities, that bar the issuer from associating with a regulated entity, engaging in certain activities, or are based on fraudulent, manipulative, or deceptive conduct;

(3) certain SEC disciplinary orders relating to brokers, dealers, municipal securities dealers, investment companies, and investment advisers and their associated persons;

(4) SEC cease-and-desist orders related to violations of certain anti-fraud provisions and registration requirements of the federal securities laws;

(5) certain SEC stop orders and orders suspending the Regulation A exemption;

(6) suspension or expulsion from membership in a self-regulatory organization (SRO) or from association with an SRO member; and

(7) U.S. Postal Service false representation orders.

As adopted, disqualification applies only for disqualifying events that occur after the effective date of the rule amendments. However, matters that existed before the effective date that would otherwise be disqualifying must be disclosed in writing to investors a reasonable time prior to the sale. In addition, an issuer will not be disqualified from relying on Rule 506 when it can show it did not know and, in the exercise of reasonable care, could not have known that a covered person with a disqualifying event participated in the offering.

The rule amendments become effective on September 23, 2013.

SEC Proposes Additional Amendments to Form D, Regulation D and Rule 156 under the Securities Act

In connection with the final amendments adopted to Rule 506, the SEC proposed additional amendments to Form D, Regulation D and Rule 156 under the Securities Act to allow it to monitor Rule 506 offerings and to address issues that arise in connection with allowing general solicitation and general advertising for such offerings. Specifically, the SEC proposed to increase the informational requirements of Form D by amending several items and adding new items. The SEC proposed to require filing of Form D no later than 15 days prior to the first use of general solicitation in a Rule 506 offering and filing of a closing Form D amendment no later than 30 days after the termination of a Rule 506 offering. Also, the signature block on Form D would be revised to include a certification by issuers that the offering is not disqualified from reliance on Rule 506.

In addition to the proposed changes to Form D, the SEC proposed further amendments to Regulation D, including:

- an amendment to Rule 507 to disqualify an issuer from relying on Rule 506 for one year if the issuer, or any predecessor or affiliate of the issuer did not comply within the last five years with all of the Form D filing requirements for a Rule 506 offering;
- new Rule 509 to require issuers to include prescribed legends in any general solicitation materials informing potential investors as to whether they are qualified to participate in the offering, the type of offering being conducted and the risks associated with the offering. Private funds also would be required to include a legend disclosing that securities being offered are not subject to the 1940 Act and to include additional disclosures in solicitation materials that include performance data. New Rule 509 would disqualify an issuer from relying on Rule 506 if such issuer or its predecessor has been subject to a court order enjoining it for failure to comply with Rule 509; and
- new Rule 510T to require issuers to temporarily submit their general solicitation materials to the SEC on a non-public basis.

Finally, the SEC proposed to amend Rule 156 under the Securities Act (the rule applicable to investment company sales literature) to apply to sales literature used by private funds in Rule 506 offerings.

Comments on the proposed amendments are due by September 23, 2013.

SEC Proposes Money Market Fund Rule Amendments

On June 5, 2013, the SEC proposed amendments to certain rules under the 1940 Act that govern money market funds. The proposed rule amendments seek to: (1) limit money market funds' susceptibility to heavy redemptions during periods of market stress, (2) improve money market funds' ability to deal with contagion from heavy redemptions, (3) preserve to the extent possible the benefits of money market funds for investors, and (4) increase risk transparency in money market funds. The SEC proposed two principal alternative reforms—a floating NAV and liquidity fees/ redemption gates—that could be adopted alone or in combination. In addition, the SEC proposed changes to money market fund diversification and disclosure requirements that would apply under either of the alternative reforms.

As proposed, the floating NAV rule amendments would:

- prohibit money market funds, other than government and retail money market funds, from using the amortized cost method to value portfolio securities and require fund share prices to reflect market-based valuation factors—i.e., allow NAV per share to float instead of remaining at a stable $1.00 share price;
- require money market funds, other than government and retail money market funds, to round share prices to the nearest 1/100th of 1% (basis point rounding method), instead of rounding to the nearest 1% (penny rounding method), in order to allow fund investors to see the fluctuations in share price; and
- allow government money market funds (funds that hold at least 80% of their assets in cash, government securities or repurchase agreements collateralized with government securities) and retail money market funds (funds that limit each shareholder's redemptions to no more than $1 million per business day) to use the penny rounding method to maintain a stable NAV per share, but prohibit the use of the amortized cost method.

As proposed, the liquidity fees and redemption gates rule amendments would:

- require money market funds to charge a liquidity fee of 2% on redemptions if the fund's weekly liquid assets (assets such as cash, U.S. Treasury obligations, certain other government securities with remaining maturities of 60 days or less and securities that convert into cash in one week) fall below 15% of total assets, unless the board determines it is not in the best interest of the fund or approves a lower fee;
- allow the board of a money market fund to temporarily suspend, or "gate," redemptions if the fund's weekly liquid assets fall below 15% of total assets;
- require that any redemption gate imposed must be lifted within 30 days and limit redemption gates to no more than 30 days in a 90-day period;
- require prompt public disclosure of the crossing of the 15% weekly liquid assets threshold, the imposition and removal of any liquidity fee or redemption gate and the board's analysis in determining whether or not to impose a liquidity fee or a redemption gate;
- allow all money market funds to use the penny rounding method to maintain a stable NAV per share, but prohibit the use of the amortized cost method; and
- exempt government money market funds from the requirement to impose a liquidity fee, but permit them to impose liquidity fees and redemption gates if there is appropriate disclosure in the fund's prospectus.

The SEC also stated that it is considering a combination of the two alternatives. If a combination of the two alternatives is adopted, money market funds, other than government and retail money market funds, would be required to maintain a floating NAV and non-government money market funds would be able to impose liquidity fees and redemption gates in certain circumstances.

In addition to the two alternative reforms, the SEC proposed rule amendments to:

- improve disclosure by requiring money market funds to disclose (1) on the money market fund's website, on a daily basis, the fund's daily and weekly liquid assets and market-based NAV, (2) new events such as the imposition of a liquidity fee or gate, sponsor support, portfolio security defaults and a decline in NAV per share below $0.9975 on a new Form N-CR, and (3) historic instances of sponsor support in the fund's statement of additional information;
- amend Form N-MFP to add new reporting requirements and to eliminate the 60-day delay on the public availability of the information filed;
- amend Form PF to enable the SEC to monitor the movement of assets from money market funds to private liquidity funds in response to money market fund reforms by requiring liquidity fund advisers with at least $1 billion in combined money market fund and liquidity fund assets to report substantially the same portfolio information on Form PF as registered money market funds would report on Form N-MFP;
- tighten the diversification requirements under Rule 2a-7 by requiring money market funds to (1) aggregate affiliates for purposes of determining whether they are complying with the 5% concentration limitation in any one issuer, (2) remove the rule, which allows as much as 25% of the value of securities held in a money market fund's portfolio to be subject to guarantees or demand features from one institution, and (3) aggregate all of the asset-backed securities vehicles sponsored by the same entity for purposes of the 10% guarantor diversification limit, unless the board determines that the money market fund is not relying on the sponsor's strength or the structural enhancements of the asset-backed security; and
- require money market funds to stress test against the fund's level of weekly liquid assets falling below 15% of total assets.

Comments on the proposed amendments are due by September 17, 2013.

Division of Investment Management Issues Guidance Update Regarding Compliance with Exemptive Orders

In May 2013, the SEC's Division of Investment Management issued a guidance update emphasizing the importance of complying with representations and conditions of exemptive orders. The guidance follows a June 2011 report from the SEC's Office of Inspector General which noted examples of firms failing to comply with the representations and conditions of exemptive orders and made recommendations intended to enhance the SEC's oversight of compliance with exemptive orders. Additionally, in February 2013, the SEC's Office of Compliance Inspections and Examinations listed compliance with exemptive orders as a 2013 examination focus area. For entities that receive and rely on exemptive orders, the guidance update serves as a reminder that non-compliance with the representations and conditions of such orders may result in a violation of the federal securities laws and that the consequences of non-compliance may be severe. The Division of Investment Management suggests that investment companies and investment advisers adopt and implement policies and procedures reasonably designed to ensure compliance with each representation and condition of an order.

Other News

SEC Commissioner Gallagher Discusses the Need for Proxy Advisory Service Reform

In a July 11, 2013 speech to the Society of Corporate Secretaries & Governance Professionals, SEC Commissioner Daniel Gallagher expressed concerns about whether investment advisers are fulfilling their fiduciary duties to investors when they rely on, and follow, proxy advisory firm recommendations. Commissioner Gallagher stated that investment advisers may view their proxy voting responsibilities with more of a compliance mindset than a fiduciary mindset. He attributed this shift in voting practices, in part, to two SEC staff no-action letters issued in 2004 that provide a potential safe harbor against claims of conflicts of interest when an investment adviser votes client proxies based on the recommendations of an independent third party, even though the recommendations may be consistent with the investment adviser's own interests.

Commissioner Gallagher concluded his speech by stating that the no-action letters should be replaced with SEC-level guidance to ensure that investment advisers "take responsibility for their voting decisions rather than engaging in rote reliance on proxy advisory firm recommendations." In addition, he suggested that the SEC undertake a fundamental review of the role and regulation of proxy advisory firms and explore possible reforms, including, but not limited to, requiring a universal code of conduct, ensuring recommendations are designed to increase shareholder value, increasing transparency and overall accountability and ensuring that conflicts of interests are appropriately dealt with.

Litigation and Enforcement Actions

Seventh Circuit Seeks Clarification Regarding Insider Trading Prohibitions and Mutual Fund Redemptions

On July 22, 2013, the U.S. Court of Appeals for the Seventh Circuit reversed the district court ruling in *Securities and Exchange Commission v. Bauer* and remanded for further proceedings to consider the novel issue of whether and how the "misappropriation theory" of insider trading applies to mutual fund redemptions.

In the fall of 2000, Jilaine H. Bauer (the Defendant) served as general counsel, chief compliance officer, and chairperson of the pricing committee for Heartland Advisors, Inc. (HAI). The Defendant also served as vice president and secretary of Heartland Group, Inc. (HGI), an open-end fund complex. HAI was the investment adviser, principal underwriter and distributor for the HGI mutual funds, including the Short Duration Fund and the High Yield Fund (the Funds). Beginning in 1999 and continuing through October 2000, the Funds experienced substantial net redemptions, resulting in significant decreases in NAV and increased illiquidity. In addition, several of the Funds' portfolio securities had defaulted or were in danger of default. In order to generate the cash required to meet redemption demands, the Funds began selling off securities at discounted prices. The Defendant redeemed all of her shares in the Short Duration Fund on October 3, 2000. Ten days later, HAI's pricing committee instituted across-the-board "haircuts" on the Funds' securities, resulting in NAV decreases of 44.02% and 69.41% for the two Funds, which entered receivership five months later.

On December 11, 2003, the SEC charged the Defendant with insider trading, and on May 25, 2011, the U.S. District Court for the Eastern District of Wisconsin granted summary judgment to the SEC under the "classical theory" of insider trading, which "targets a corporate insider's breach of duty to shareholders with whom the insider transacts." However, the SEC abandoned the "classical theory" on appeal, instead arguing that the Defendant was liable under the "misappropriation theory" of insider trading whereby the disclosure obligation "runs to the source of the information"—in this case, the Funds—rather than the trading counterparty. In reversing the district court's order of summary judgment, the Seventh Circuit found that the lower court did not "weigh the novelty of the SEC's claims in the mutual fund context" and remanded for further proceedings to consider the applicability of the "misappropriation theory" of insider trading to the Defendant's redemptions and to resolve questions of fact related to the materiality of the Defendant's non-public information and whether the Defendant acted with scienter.

Second Circuit Affirms Dismissal of Class Action Against ProShares ETFs

On July 22, 2013, the U.S. Court of Appeals for the Second Circuit affirmed the dismissal of a class action lawsuit against ProShares Trust and ProShares Trust II (ProShares) in *In re ProShares Trust Securities Litigation*. The plaintiffs were investors in leveraged ProShares exchange-traded funds (the ETFs), each of which pursued an investment objective whereby it sought a return equal to a stated multiple of a benchmark index on a daily basis. The complaint alleged that the plaintiffs suffered losses due to ProShares' failure—in violation of Sections 11 and 15 of the Securities Act—to adequately disclose the risks of holding investments in the ETFs for periods longer than one day.

Affirming the ruling of the U.S. District Court for the Southern District of New York, the Second Circuit found that ProShares adequately disclosed the risks of long-term investments in the ETFs. The court rejected the plaintiffs' primary argument that ProShares made a material omission by not disclosing that an ETF investor could experience an "actual loss" despite correctly predicting the direction of the underlying index's movement over the period of investment. The court found that the disclosure clearly contemplated this scenario by stating that the value of a long-term investment in an ETF may "diverge significantly" from the value of the underlying index. Given the robust risk disclosure contained throughout the registration statements, the court found it implausible that the decision of a reasonable investor would be influenced by the allegedly material omission. The court further stated that subsequent disclosure revisions, which clarified that volatility could cause an investment in an ETF to "move in [the] opposite direction as the index," did not constitute an admission of the inadequacy of the prior disclosure. The plaintiffs also alleged that ProShares possessed an "undisclosed mathematical formula" and was aware that certain market conditions could place long-term ETF investors in a "must lose" position. In dismissing this allegation, the Second Court noted that ProShares "cannot be expected to predict and disclose all possible negative results across any market scenario."

D.C. Circuit Affirms District Court Ruling on Industry Challenges to CFTC Rule 4.5

On June 25, 2013, the U.S. Court of Appeals for the District of Columbia Circuit affirmed the district court ruling in Investment Company Institute et al. v. Commodity Futures Trading Commission (CFTC). The plaintiffs in the case, the ICI and the U.S. Chamber of Commerce, challenged amendments to Rule 4.5 under the Commodity Exchange Act (CEA), which sets forth the conditions pursuant to which a registered investment company may claim an exclusion from the definition of "commodity pool operator," and amendments to Rule 4.27. The plaintiffs alleged that the rule-making process did not meet the standards set forth in the CEA relating to cost-benefit analysis and was arbitrary and capricious under the Administrative Procedures Act (APA).

On December 12, 2012, the U.S. District Court for the District of Columbia denied the plaintiffs' motion for summary judgment, granted the CFTC's motion to dismiss in part and granted the CFTC's cross-motion for summary judgment. The plaintiffs appealed the ruling granting summary judgment to the CFTC. In affirming the district court, the D.C. Circuit found the following:

- The CFTC engaged in "reasoned decisionmakng" and provided an adequate basis for the shift in its views from the 2003 amendments to Rule 4.5;
- The CFTC considered the costs and benefits as required and the CFTC's cost-benefit analysis was not arbitrary and capricious;
- Three specifically challenged provisions—the inclusion of swaps in the registration threshold, the exclusion of risk management strategies from the definition of "bona fide hedging transactions" and the 5% registration threshold itself—were sufficiently explained such that the CFTC's actions were not arbitrary and capricious; and
- The CFTC provided "adequate opportunity for notice and comment," satisfying the requirements of the APA.

Former Mutual Fund Directors Settle Claims That They Failed to Properly Oversee Asset Valuation

On June 13, 2013, the SEC settled enforcement proceedings against eight former directors, including six independent directors, of five registered investment companies advised by Morgan Asset Management, Inc. (Morgan Keegan). The SEC's order instituting enforcement proceedings (Original Order), brought on December 10, 2012, alleged that the directors failed to satisfy their statutory obligations with respect to the fair valuation of mortgage-backed securities held by the funds. The June 13 settled order (Settled Order) found that the directors delegated their asset-pricing responsibilities to Morgan Keegan without giving adequate guidance on how fair valuations should be made or ascertaining how fair values were determined. The SEC's settlement with the directors follows a related $200 million settlement by Morgan Keegan with the SEC, state regulators and FINRA in 2011.

The Original Order stated that between January 2007 and August 2007, a significant portion (in some cases up to 60%) of the funds' portfolios contained below-investment grade debt securities, including a large number of securitized products backed by subprime mortgages, for which market quotations were not readily available. The Original Order noted that, pursuant to Section 2(a)(41)(B) of the 1940 Act, such securities were required to be valued at a fair value as determined in good faith by the directors. The SEC alleged that the process employed in making fair valuation determinations for the funds' securities was deficient in many respects. The Original Order alleged that the directors did not know and did not inquire as to the manner in which Morgan Keegan was making fair value determinations for particular types of securities and did not receive information that would allow the directors to understand the methodology that was being used to fair value securities. The Original Order alleged that these failures were "particularly egregious" given that fair valued securities made up the majority of the funds' net asset values.

The findings of the Settled Order generally followed the allegations of the Original Order; however, the SEC made several findings in the Settled Order that were not alleged in the Original Order. The Settled Order found that the valuation procedures did not require the directors to ratify any fair value determinations made by Morgan Keegan, and the directors did not ratify any such determinations. The Settled Order alleged that Morgan Keegan repeatedly accepted price adjustments from the portfolio manager, but the directors never provided any guidance as to how Morgan Keegan should evaluate the reasonableness of such adjustments. The Settled Order also discussed the directors' statutory responsibilities with respect to determining the fair value of securities and reviewed SEC guidance with respect to securities valuation. The Settled Order stated that SEC guidance indicated that "the ultimate responsibility for determining fair value lies with a fund's directors, and that this responsibility cannot be delegated away."

The Original Order alleged that the directors caused the funds to violate the following rules under the 1940 Act: (1) for the open-end funds, Rule 22c-1 by redeeming and repurchasing securities at a price other than the current net asset value; (2) Rule 30a-3(a) by failing to maintain internal control over financial reporting; and (3) Rule 38a-1 by failing to adopt and implement meaningful fair-valuation methodologies and related procedures. The Original Order also alleged that, as a result of their conduct, the directors caused certain of the funds' registration statements to contain statements that were false or misleading with respect to material facts or to omit material facts which were required to be stated in the registration statements. The Settled Order found only that the directors caused the funds to violate Rule 38a-1. The directors were ordered to cease and desist from committing or causing any violations and any future violations of that rule. The directors consented to the entry of the Settled Order without admitting or denying any of the findings.

SEC Settles Charges Against Proxy Adviser for Failure to Safeguard Client Information

On May 23, 2013, the SEC settled charges against Institutional Shareholder Services Inc. (ISS) for failing to safeguard the confidential proxy voting information of clients. The SEC found that from 2007 to 2012, an ISS employee provided a proxy solicitor with material nonpublic information revealing how more than 100 of ISS's clients were voting their proxy ballots. The SEC stated that, in exchange for this voting information, the proxy solicitor provided the ISS employee with approximately $11,500 in concert and sporting event tickets and charged approximately $20,000 in meals with the employee and other ISS employees. The SEC determined that ISS lacked sufficient controls over employee access to confidential client voting information. While ISS had a code of ethics prohibiting unauthorized disclosure of confidential client information, the SEC stated that ISS willfully violated Section 204A of the Advisers Act by failing to establish and enforce policies and procedures reasonably designed to prevent the misuse of confidential client information. ISS agreed to pay a civil penalty of $300,000 and to retain a compliance consultant to conduct a comprehensive review of its supervisory and compliance policies and procedures.

SEC Settles Charges Against Trustees and Service Providers of "Turnkey" Investment Company

On May 2, 2013, the SEC settled charges against the trustees, administrator and CCO service provider of the Northern Lights Fund Trust and the Northern Lights Variable Trust (the Trusts), finding that the trustees, administrator and CCO service provider violated the 1940 Act and various rules thereunder in connection with disclosures regarding the trustees' approval of certain investment advisory contracts and approval of the compliance programs of the advisers to the Trusts' series. The trustees, administrator and CCO service provider agreed to settle the SEC's charges without admitting or denying the SEC's findings. The Trusts offer multiple series managed by different unaffiliated advisers, administered by a single administrator and overseen by a single board of trustees, in an arrangement known as a "turnkey" investment company platform.

The SEC found that certain disclosures included in the Trusts' shareholder reports relating to the factors the trustees considered in approving or renewing advisory contracts contained boilerplate language with false or misleading information. The SEC stated that, in one instance, the disclosure claimed that the trustees had considered peer group information about the advisory fee, yet the trustees never received this information. The SEC noted two other instances where the shareholder report disclosure implied that the advisory fee was not materially higher than the peer group range, when it was almost twice as high as the peer group's mean. The SEC also determined that the administrator did not ensure that all applicable shareholder reports contained the mandatory disclosures about the trustees' evaluation of advisory contracts and also failed to ensure that numerous series maintained and preserved their contract renewal files.

The SEC also found that the trustees did not follow the Trusts' policies and procedures for approval of the compliance programs of advisers to the series of the Trusts. The SEC stated that the Trusts' policies and procedures called for the trustees to approve the advisers' compliance programs only after reviewing the advisers' compliance manual or after receiving a summary of the essential parts of the compliance program from the CCO service provider. However, according to the SEC, the trustees' approval of the advisers' compliance programs was based primarily on their review of a brief written statement prepared by the CCO service provider stating that the advisers' compliance manuals were "sufficient and in use" and a verbal representation by the CCO service provider that such manuals were adequate.

The SEC order found that the trustees caused violations of Section 34(b) of the 1940 Act; the trustees and the CCO service provider caused violations of Rule 38a-1 under the 1940 Act; and the administrator caused violations of Sections 30(e) and 31(a) of the 1940 Act and Rules 30e-1 and 31a-2 thereunder. The administrator and the CCO service provider agreed to pay $50,000 penalties each, and the administrator, the CCO service provider and the trustees agreed to engage an independent compliance consultant to address the violations found in the SEC order.

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