IN THE MATTER OF

WINFIELD & CO., INC. ET AL.*

File No. 3-2249. Promulgated February 9, 1972

Securities Exchange Act of 1934—Sections 15(b),15A and 19(a)(3)

Investment Advisers Act of 1940—Section 203

BROKER-DEALER AND INVESTMENT ADVISER PROCEEDINGS

Grounds for Remedial Action

Receipt of Benefits by Affiliates in Connection with Investment Company Portfolio Transactions

Improper Valuation of and Inadequate Investigation Respecting Restricted Securities

Deviation from Fundamental Investment Policy

Service as Investment Adviser Pursuant to Contract Not Describing All Compensation

* Winfield Distributors, Inc.; David H. Meid; Robert R. Hagopian; Henry L. Jamieson; Meyerson & Co., Inc.; Winfield Underwriters, Inc.; Harry Meyerson; Dean Russell Burwell.

Inaccurate Records and Financial Report

Where investment company's investment adviser and adviser's controlling persons who were also directors and/or officers of investment company entered into arrangement with broker-dealer under which brokerage commissions on company's portfolio transactions were directed to broker-dealer in return for direct and indirect benefits provided to adviser and its principals, and caused company to purchase restricted securities without making reasonable investigation and to value such securities improperly, and to purchase, without shareholder authorization, larger percentage of one issuer's securities than permitted by its fundamental policies; adviser served as investment adviser pursuant to contract which did not describe all compensation to be paid thereunder; and investment company's and broker-dealer's records and latter's report of financial condition were inaccurate, *held*, willful violations of antifraud and other provisions of securities acts, including Sections 2(a)(39), 13(a), 15(a), 17(e)(1), 22(d) and 22(e) of Investment Company Act, and, under all the circumstances, appropriate in the public interest to accept offers of settlement providing for imposition of remedial sanctions.

APPEARANCES:

Theodore Altman, for the Division of Corporate Regulation of the Commission.

Fred C. Aldridge, Jr. and *Philip J. Fina*, of Stradley, Ronon, Stevens & Young, for Winfield & Co., Inc., Winfield Distributors, Inc., and Henry L. Jamieson.

Eugene P. Souther, of Seward & Kissel, for David H. Meid.

Fred W. Drogula, of Ginsburg, Feldman and Bress, for Robert R. Hagopian.

George A. Blackstone and *Weyman I. Lundguist*, of Heller, Ehrman, White & McAuliffe, for Meyerson & Co., Inc., Harry Meyerson, Dean Russell Burwell and Winfield Underwriters, Inc.

FINDINGS AND OPINION OF THE COMMISSION

In these proceedings pursuant to Sections 15(b), 15A and 19(a)(3) of the Securities Exchange Act of 1934 ("Exchange Act") and Section 203 of the Investment Advisers Act of 1940 ("Advisers Act"), we heretofore accepted offers of settlement submitted by the above-captioned respondents. Pursuant to such offers, in which the respondents, without admitting the allegations in the order for proceedings, consented to certain findings and sanctions, orders were issued finding violations and failure of supervision as alleged and imposing the specified sanctions. One order dealt with Meyerson & Co., Inc., a registered broker-dealer and former member of the New York Stock Exchange and other national securities exchanges; Winfield Underwriters, Inc. ("Underwriters"), a registered broker-dealer which is a whollyowned subsidiary of Meyerson & Co., and Harry Meyerson and Dean Russell Burwell, who at relevant times were officers, directors and principal stockholders of Meyerson & Co. and directors (and Burwell president) of Underwriters.[1] A second order dealt with Winfield & Co., Inc. ("Adviser"), a registered investment adviser which acts as investment adviser to Winfield Growth Fund, Inc. ("Fund"), a registered open-end investment company; Winfield Distributors, Inc. ("Distributors"), a registered broker-dealer and wholly-owned subsidiary of Adviser; and David H. Meid, Robert R. Hagopian and Henry L. Jamieson, who at relevant times were officers, directors and principal stockholders of Adviser and officers or directors of the Fund and Distributors.[2] The

[1] Securities Exchange Act Release No. 8945 (July 28, 1970).

[2] Securities Exchange Act Release No. 8980 (September 16, 1970).

sanctions imposed included suspensions, ranging variously from 30 days to 9 months, of Adviser's registration as an investment adviser and Distributors' registration as a broker-dealer, and of Hagopian, Meid, Jamieson, Burwell and Meyerson from association with any broker, dealer, registered investment company or registered investment adviser, and a bar of Meyerson from supervisory activities.

We now issue our detailed findings and opinion with respect to the issues presented in these proceedings, which essentially relate to or arise out of transactions in portfolio securities of the Fund during the period beginning in October 1966.[3]

ARRANGEMENTS FOR RETURN OF PORTFOLIO BROKERAGE COMMISSIONS TO ADVISER AND ITS PRINCIPALS

In September 1966, Meid, Hagopian and Jamieson together acquired a controlling interest in Adviser. At that time, Distributors, the sponsor-distributor of Winfield Investment Programs, a unit investment trust investing solely in shares of the Fund, was also the Fund's principal underwriter. Adviser and its principals ("the Adviser respondents"), pursuant to an agreement with Burwell, immediately began allocating commissions on Fund portfolio transactions ("brokerage commissions") to Meyerson & Co., both by designating that firm as executing broker for such transactions and by directing "give-ups" to it on transactions executed by others, and to arrange for the sale to that firm of the Fund's underwriter, to be represented by a new corporate vehicle. In February 1967, they organized Underwriters for this purpose, and in June 1967 Adviser sold Underwriters to Meyerson & Co. for $25,000. In fact, however, the Adviser respondents retained control of Underwriters, and the transaction was part of a scheme to divert large amounts of Fund brokerage commissions for their own benefit.[4]

---

[3] Respondents consented that we could base findings on material contained in our public files and obtained by our staff in the investigation of the matters involved herein.

[4] This was not the first instance of such use of Fund brokerage commissions. In early 1966, when Meid was an employee of Adviser and was acquiring increasing influence over the direction of the Fund's portfolio transactions, he and Hagopian had decided to purchase control of Adviser with the assistance of Jamieson, who is Hagopian's father-in-law. Hagopian had then obtained employment with a broker-dealer after arranging with Meid that the latter would channel Fund portfolio transactions to that broker-dealer. During the approximately eight months that Hagopian was employed by the broker-dealer, Meid directed a total of $129,000 in brokerage commissions, representing more than half of such commissions generated by the Fund, to that firm. Out of this amount, Hagopian received approximately $40,000 after expenses. Hagopian's activities during this period were devoted to the promotion and sale of Fund shares. He played no role in the execution of portfolio transactions, and the Fund was essentially his only customer. Shortly after Hagopian left the broker-dealer to join Adviser, the allocation of Fund brokerage transactions and commissions to the broker-dealer ceased.

In 1967 and 1968, Adviser directed almost $2,250,00 of Fund brokerage commissions, representing about 33 percent of the total commissions generated by the Fund, to Meyerson & Co.[5] Whenever possible, Meid, who placed the Fund's portfolio transactions, placed orders directly with Meyerson & Co. In addition, he directed other New York Stock Exchange members who executed Fund portfolio transactions to give up part of their commissions to Meyerson & Co. Adviser respondents also directed commissions derived from transactions of other clients to Meyerson & Co. Thus, the Meyerson firm was designated as broker for a significant number of Adviser's privately-advised accounts, and give-ups were directed to it through a broker who executed transactions for an off-shore fund account of Adviser.

As noted above, a large amount of Fund brokerage commissions found its way back from Meyerson & Co. to the Adviser respondents, largely through the vehicle of Underwriters. Notwithstanding the sale of that company to Meyerson & Co., Hagopian, who had established the underwriting organization, continued to exercise full direction over its activities, including all advertising and other promotional activities. Underwriters had no full-time employees. Its offices were contiguous to those of Adviser and were occupied by personnel of Adviser who performed substantailly all underwriting-related administative and managerial tasks. In 1967 and 1968, Meyerson & Co. paid some $2 million to or for the benefit of the Adviser respondents, including direct payments to Adviser for a portion of its rent and salary expenses, and amounts totalling about $1.8 million paid on behalf of Underwriters for various expenses incurred by or in accordance with the directions of Hagopian or other Adviser personnel.[6] When allocations of brokerage commissions to Meyerson & Co. decreased following the ban on customer-directed give-ups in December 1968, the payments by that firm to or for the benefit of the Adviser respondents also decreased. For example, at the end of 1968 it ceased paying the portion of Adviser's salary and rent expense which it had been paying.

---

[5] This income accounted for about 30 percent of Meyerson & Co.'s gross revenues during those two years.

[6] The amounts thus paid by Meyerson & Co. far exceeded commissions retained by Underwriters on the sale of Fund shares. Simultaneously with the transfer of Underwriters to Meyerson & Co., the dealer allowance had been raised from 7 percent to 8¼ percent, out of the maximum sales load of 8½ percent. The remaining ¼ of 1 percent produced commissions for Underwriters of only about $545,000 during the two-year period ended June 30, 1969.

The Adviser respondents deried additional compensation from Fund brokerage commissions through other arrangements and transactions with Meyerson & Co. Thus, from November 1966 on, after alocations of brokerage commissions to Meyerson & Co. had reached a level exceeding $5,000 per month, it made monthly payments to Adviser for research services, amounting at first to $5,000 and later to $6,000 and totalling $142,000 through 1968. The services were furnished at weekly meetings of approximately one hour's duration and consisted largely of oral presentations by Meid or another officer of Adviser. We note that an individual not associated with Adviser or Meyerson & Co. paid Adviser only $100 a month for the privilege of attending these meetings. In April 1968 Meyerson & Co. purchased from Jamieson and others a school teaching "cram courses" for qualifying examinations given by the National Association of Securities Dealers, Inc. Although the school had virtually no book value and no history of earnings, Meyerson & Co. paid $23,463. In addition, it agreed to pay Jamieson $85,000 out of the net profits of the school. However, even though Meyerson & Co. did not maintain separate records for the school and was therefore unable to determine whether the school was operating at a profit, it commenced payments to Jamieson on the basis of a percentage of each student's tuition.

Meid, Hagopian, and Jamieson, as officers of the Fund and as persons responsible for directing the execution of its portfolio transactions, and Adviser, by virtue of its position as investment adviser, were fiduciaries of the Fund. As such, they were under a duty to act solely in the best interests of the Fund and its shareholders.[7] However, in violation of that duty, they entered into arrangements designed to further their own interests and to obtain benefits for themselves in the form of rebates of a portion of the commissions generated by the execution of Fund portfolio transactions. Moreover, they committed themselves and the Fund, for their personal benefit, to a relationship with Meyerson & Co. which did not permit them to retain the freedom of judgment and action in selecting broker-dealers to execute Fund portfolio transactions that as managers they owned to the Fund.[8]

Meyerson & Co. and its principals and Underwriters ("the Meyerson respondents") knowingly participated in and were

[7] See *Provident Management Corporation*, 44 S.E.C. 440, 445 (1970), and cases cited there.

[8] See *Provident Management Corporation*, *supra*, at p. 446.

an integral element of the unlawful rebate arrangements which, as found above, violated the Adviser respondents' fiduciary obligation to the Fund and its shareholders.

Accordingly, we conclude that the Adviser respondents and Distributors engaged in a scheme to defraud and in a practice which operated as a fraud upon the Fund and its shareholders, and that thereby they willfully violated, or willfully aided and abetted violations, of the antifraud provisions of Section 17(a) of the Securities Act of 1933, Section 10(b) of the Exchange Act and Rule 10b–5 thereunder, and Sections 206(1) and 206(2) of the Advisers Act. We further conclude that the Meyerson respondents willfully violated or willfully aided and abetted violations of those provisions.

we further find that by engaging in the conduct described above, the Adviser respondents willfully violated Section 17(e)(1) of the Investment Company Act of 1940, and the Meyerson respondents willfully aided and abetted such violations.[9] As pertinent, here, that section makes it unlawful for any affiliated person of a registered investment company "acting as agent, to accept from *any source* any compensation . . . for the purchase or sale of any property to or for such registered investment company . . . except in the course of such person's business as an underwriter or broker." [Emphasis added]. The Adviser respondents, who were affiliated persons of the Fund, were acting as its agents in placing orders for the purchase and sale of its portfolio securities and the exceptions provided in the section were not applicable. They were not engaged in the brokerage business and did not in fact perform any brokerage services in connection with the execution of the Fund's portfolio transactions.[10] Although many of the activities of these respondnets, especially Hagopian, were related to the promotion and underwriting of Fund shares, the benefits received by them were not received in the course of an underwriting business but were in the nature of compensation for the allocation of brokerage commissions to Meyerson & Co. In light of the objective of Section 17(e) "to prevent affiliated persons from having their judgment and fidelity impaired by conflicts of interest,"[11] it is evident that

[9] See *Provident Management Corporation*, *supra*, at p. 447.

[10] See *Provident Management Corp.*, *supra* at p. 447. Our recent decision in *First Multifund of America, Inc.*, 44 S.E.C. 678 (1971) is not to the contrary. In that case we found that the adviser of an open-end investment company which invested solely in the shares of other open-end companies acted as broker in effecting portfolio purchases and was entitled to receive concessions of up to 1 percent from the principal underwriters of such shares under the provisions of Section 17(e) (2) of the Act.

[11] *U.S.* v. *Deutsch*, 451 F.2d 98 (C.A. 2, 1971), *cert. denied* 404 U.S. 1019 (1972).

the acceptance of compensation pursuant to an arrangement which, as indicated, carried with it an inherent conflict of interest between the Adviser respondents and the Fund, fell within its prohibition.

PURCHASE AND VALUATION OF RESTRICTED SECURITIES

Additional violations by Adviser, Meid and Jamieson occurred in connection with the Fund's purchases, during the period beginning July 1, 1967, of "restricted" securities, i.e., securities that canot be offered for public sale without first being registered under the Securities Act.

From July 1, 1967 to December 31, 1968, the Fund purchased restricted securities of 12 different issuers at a total cost of $21,497,960. The record shows that proper valuation procedures were not followed with respect to such securities. Section 2(a)(39)) (now 2(a)(41)) of the Investment Company Act and Rule 2a–4 thereunder require that in determining net asset value, "securities for which market quotations are readily available" must be valued at current market value while other securities and assets must be valued at "fair value as determined in good faith by the board of directors." For valuation purposes, restricted securities constitute securities for which market quotations are not readily available and their value must therefore be determined by the directors.

Notwithstanding that requirement, the Fund's board of directors never considered the matter of valuing restricted securities prior to September 1968. Up to that point, Meid alone determined such valuation. At first he generally valued them at the market price of unrestricted securities of the same class, if any, and later he applied a uniform 10 percent discount to such price. In Septemer 1968, when restricted securities represented about 10 percent of the Fund's total net asset value of $180 million, the board ratified the valuation of securities in the portfolio at June 30, 1968 as "representing fair market value as determined in good faith." With respect to future valuations, the board considered the possibility of giving separate consideration to each restricted security but rejected it after Meid represented that such procedure would create a time-consuming administrative burden. Instead, the board concluded that in view of current market conditions a 12 percent discount should be applied in valuing restricted securities, unless an "unusual security" was involved. However, there was no discussion at subsequent board meetings as to whether any securities fell into this category. Indeed, the record indicates that further acquisitions of restricted securities were not thereafter brought to the board's attention.

It is evident that proper valuation of portfolio securities by an investment company is of critical importance. Such valuation largely determines the price at which shares of the company are sold and redeemed and the compensation of the investment adviser where, as here, such compensation is based on net assets. Moreover, investors may be misled by the reported performance of an investment company where portfolio securities are not properly valued.

Adviser and Meid caused the Fund's board to fail to comply with its obligation to determine the fair value of each issue of restricted securities. The valuations that were made by Meid, and subsequently by the board, were clearly improper.[12] Moreover, because the restricted securities were purchased at substantial discounts from the market prices for unrestricted securities, the inflated valuations created an appearance of "instant performance," particularly in those instances where such market price increased between the date on which the Fund made its commitment to purchase and the date on which the securities were first included in the Fund's portfolio for pricing purposes.[13]

Moreover, in causing the Fund to purchase restricted securities, Adviser and Meid failed to make reasonable investigations to obtain pertient information concerning such securities. The record shows that in many cases Meid relied on unsubstantiated representations of other persons, described by him as "research sources," and that such persons frequently had a substantial economic interest in the offering or the issuer of such securities. Adviser and Meid had an obligation to make a reasonable investigation before causing the Fund to purchase any securities.[14] With reference to restricted securities, that obligation would necessarily encompass a thorough inquiry into factors which are of special relevance to such securities, including factors pertinent to the legal restrictions concerning a subsequent resale of the securities. Here Adviser

---

[12] See Investment Company Act Release No. 5847 (October 21, 1969); *Mates Financial Services*, 44 S.E.C. 245 1970).

[13] For example, while the restricted securities purchased between July 1, 1967 and December 31, 1968 had an aggregate cost of $21,497,960, they were assigned a value of $28,223,375 as of the days on which each was first included in the portfolio.

[14] *Cf.* Securities Act Release No. 4445 (February 2, 1962) and cases cited there, with respect to the duty of a broker-dealer to make reasonable investigation before recommending a security. The obligation of a broker-dealer in this area arises under the antifraud provisions of the federal securities laws. Those provisions are, of course, applicable as well to an Investment Company Act. *Cf. Brown* v. *Bullock*, 294 F.2d 415 (C.A. 2, 1961).

and Meid failed to make the necessary inquiries. For example, in one instance they failed to discover that there was a restrictive covenant prohibiting transfer of the securities which the Fund had agreed to purchase. As a result, the Fund did not actually acquire those securities until some months after they had been included in its portfolio for pricing purposes and then only after protracted negotiations and a settlement.

We conclude that by engaging in the conduct described above, Adviser, Meid and Jamieson, who as president and a director of the Fund and board chairman of Adviser had a duty to assure that proper practices were followed in the acquisition and valuation of restricted securities, willfully violated or willfully aided and abetted violations of the antifraud provisions of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b–5 thereunder and Sections 206(1) and 206(2) of the Investment Advisers Act, and of Sections 2(a)(39), 22(d) and 22(e) of the Investment Company Act and Rule 2a–4 thereunder.[15]

OTHER VIOLATIONS

1. Although it was a stated "fundational policy" of the Fund to limit acquisitions of any class of securities of any one issuer to 10 percent in January 1968 Meid caused the Fund to purchase restricted securities of one issuer amounting to about 12 percent of that company's common stock. By thus causing the Fund to deviate from its policy without the shareholder authorization required for such action under Section 13(a) of the Investment Company Act, Adviser, Meid and Jamieson willfully aided and abetted a violation of that Section.

2. During the period after October 1, 1966, Adviser, willfully aided and abetted by Meid, Hagopian and Jamieson, willfully violated Section 15(a) of the Investment Company Act in that Adviser served as investment adviser of the Fund pursuant to a written contract which failed to describe precisely all compensation to be paid thereunder. The contracts which were in effect during the period under consideration failed to describe the return of brokerage commissions to those respondents

[15] Sections 22(d) and 22(e) of the Investment Company Act, which deal respectively with sales and redemptions of their shares by investment companies, are both predicated on net asset value properly determined.

under the arrangements with Meyerson & Co. or the extent to which the advisory fees, which under the contracts were based on net asset value of the Fund, had been inflated as a result of the improper valuation of restricted securities.

3. The books and records concerning allocation of orders for portfolio transactions maintained for the Fund by the Adviser respondents were inaccurate and inadequate. Among other things, the Fund's records falsely showed "research" as the reason for allocating orders to Meyerson & Co. The records either gave no reason or contained the designation "special" as the reason for allocating orders to a number of other brokers who provided services to the Adviser respondents or the Fund, or paid give-ups to Meyerson & Co. No one connected with the Fund was able to explain the exact meaning of "special." Thus, the Adviser respondents willfully aided and abetted violations of Section 31(a) of the Investment Company Act and Rule 31a–1(b)(9) thereunder in that they caused the Fund to make and maintain records which did not reflect the actual basis for allocating orders for the purchase and sale of portfolio securities.

4. The Meyerson respondents willfully violated or willfully aided and abetted violations of Section 17(a) of the Exchange Act and Rules 17a–3 and 17a–5 thereunder. Books and records maintained by Meyerson & Co. and Underwriters did not accurately reflect accounts payable and accrued expenses, and a report of financial condition as of August 31, 1968 filed by Meyerson & Co. understated those items.

In determining to accept the offers of settlement submitted by the respondents, we took into account, among other things, the fact that Adviser agreed to pay to the Fund $270,000 in mitigation of any damages which the Fund may have suffered as a result of the matters alleged in the order for proceedings, in addition to benefits in the amount of $350,000 which it was providing to the Fund pursuant to a court order approving the settlement of private litigation. We also considered its undertaking to formulate and adopt written standards with respect to information to be obtained and considered by its portfolio managers in connection with decisions to acquire restricted securities. With respect to the Meyerson respondents, we gave consideration to the fact that Meyerson & Co. and Underwriters were being liquidated,[16] and that in civil proceedings

[16] In April 1970 Distributors again became principal underwriter for the Fund.

instituted by us Meyerson & Co. agreed to consent to a permanent injunction against certain violations of antifraud provisions.

By the Commission (Chairman CASEY and Commissioners OWENS, NEEDHAM, HERLONG, and LOOMIS).