

NEW YORK PENSION FUND SCANDAL WIDENS; NEW YORK STATE ATTORNEY GENERAL CREATES TASK FORCE OF 36 STATE ATTORNEYS GENERAL TO INVESTIGATE PENSION FUND ABUSE

The “pay to play” scandal involving investments by the New York State Common Retirement Fund (the “Retirement Fund”) continues to widen in scope, with implications for investment advisers and private equity firms that may use finders or placement agents to locate investors. The New York State Attorney General’s Office and the Securities & Exchange Commission have previously filed actions against a number of individuals based on allegations that David Loglisci, former Deputy Controller and Chief Investment Officer of the Retirement Fund, required firms seeking investments from the Retirement Fund to pay millions of dollars in gratuitous “finders” fees to a number of his associates.¹ The New York State Attorney General and the SEC continue to file criminal and civil charges against additional firms and individuals. On April 30, 2009, the New York State Attorney General’s Office filed a criminal complaint against Saul M. Meyer, a founding partner of Aldus Equity, a private equity firm and investment advisor. Also on April 30, the SEC filed a Second Amended Complaint in its previously filed action alleging investment adviser fraud against Meyer and Aldus. Meyer and Aldus are alleged to have agreed to pay sham placement agents as a quid pro quo for obtaining investments from the Retirement Fund, thus defrauding the Retirement Fund.

On May 1, 2009, New York State Attorney General Andrew M. Cuomo announced that representatives from the offices of 36 state attorneys general had agreed to create a multi-state task force to explore pension fund abuse. Cuomo also announced that his office has sent subpoenas to over 100 investment firms and their placement agents seeking information about the use of unlicensed placement agents. According to the New York State Attorney General’s Office, the subpoenas include questions designed to uncover:

- which firms used which unlicensed agents, why, and in what manner;
- what fees unlicensed agents were paid, and for what services, if any;
- how the firm came to retain the unlicensed agent;
- whether the firms did any due diligence about the unlicensed agents; and
- whether payments to unlicensed agents were disclosed to the pension fund.²

¹ People v. Henry “Hank” Morris And David Loglisci, Defendants, Indictment No. 25/2009 (March 19, 2009); SEC v. Henry Morris, David J. Loglisci, et al., No. 09-cv-2518 (S.D.N.Y. March 19, 2009).

² Press Release, “Cuomo Announces Investigation Into Use Of Unregistered Middlemen Marking New Phase In Pension Fund Investigation,” May 1, 2009 (http://www.oag.state.ny.us/media_center/2009/may/may1a_09.html).

The New York State Attorney General's Office noted that its preliminary investigation found that a large proportion, 40% to 50%, of the placement agents used in connection with Retirement Fund investments were unlicensed.

In the wake of these investigations asset managers should be prepared for additional scrutiny by state and federal regulators of their use of finders or placement agents. Asset managers should revisit existing policies and procedures with respect to the use of finders or placement agents, particularly as to their licensed status, and should consider additional training for employees to avoid even the appearance of improper conflicts of interest among sales agents. Early indications are that SEC examiners are increasing their focus on such payment arrangements and also on political contributions made by asset managers. We expect such scrutiny to continue even where there is no suggestion that the underlying investments were unsuitable or otherwise inappropriate for the investors.

It is also possible that the scandal will spur rulemaking or legislation on the use of finders and placement agents for public retirement funds, as well as a reexamination of the role of political contributions made by asset managers. Already, as a result of the current case, the New York State Comptroller has banned placement agents, paid intermediaries and registered lobbyists from involvement in investments made by the \$122 billion Retirement Fund. In 1999 the SEC considered, but failed to adopt, a rule regulating the contributions of investment advisers to the campaigns of state and local officials who might have influence over the selection of money managers used by the jurisdiction.³ The 1999 proposal would have prohibited an investment adviser from providing advisory services for compensation to a government client for two years after the adviser or any of its partners, executive officers or solicitors made a contribution to certain elected officials or candidates. The current scandal may well prompt the SEC to reconsider the issue.

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³ Proposed Rule: Political Contributions by Certain Investment Advisers, Securities And Exchange Commission, 17 CFR Part 275 (Release No. IA-1812; File No. S7-19-99) (August 5, 1999) (<http://www.sec.gov/rules/proposed/ia-1812.htm>).

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