UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 51624 / April 28, 2005

INVESTMENT ADVISERS ACT OF 1940
Release No. 2380 / April 28, 2005

INVESTMENT COMPANY ACT OF 1940
Release No. 26860 / April 28, 2005

ADMINISTRATIVE PROCEEDING
File No. 3-11916

In the Matter of **MICHAEL J. LAUGHLIN,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934, SECTIONS 203(f) AND 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940, AND SECTIONS 9(b) AND 9(f) OF THE INVESTMENT COMPANY ACT OF 1940**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act"), Sections 203(f) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act"), and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act") against Michael J. Laughlin ("Laughlin" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the

purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Section 15(b) of the Securities Exchange Act of 1934, Sections 203(f) and 203(k) of the Investment Advisers Act of 1940, and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Summary

1. This proceeding against Respondent Laughlin, a former officer of Alliance Capital Management, L.P. ("Alliance Capital"), a registered investment adviser to the Alliance Capital mutual funds, arises from Alliance Capital's arrangement with its largest market timer. In return for investments in Alliance Capital's hedge funds, Alliance Capital provided "timing capacity" in certain of its mutual funds ("Funds") to Daniel Calugar ("Calugar"), the owner and President of Security Brokerage, Inc. ("Security Brokerage"), a registered broker-dealer in Las Vegas, Nevada. Laughlin, Alliance Capital's former Executive Vice President and Executive Committee member, was one of Alliance Capital's senior executives that in effect approved Calugar's market timing arrangement. Laughlin aided and abetted Alliance Capital's violative conduct by not disclosing Calugar's arrangement that was potentially harmful to the Funds, and by failing to apprise the Funds of the conflict of interest created by this arrangement which increased Alliance Capital's advisory fees.

Respondent

2. **Laughlin**, age 58 and a resident of Massachusetts, was until November 6, 2003, Executive Vice President and Executive Committee member of Alliance Capital. He was also Chairman of AllianceBernstein Investment Research and Management, Inc. ("ABIRM") (formerly Alliance Fund Distributors, Inc.), a registered broker-dealer and wholly-owned subsidiary of Alliance Capital, which served as the principal underwriter and distributor of Alliance Capital's U.S. mutual funds and served as a placing or distribution agent for most of Alliance Capital's offshore mutual funds. On November 10, 2003, Laughlin resigned at the request of Alliance Capital.

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[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Other Relevant Parties

3. **Alliance Capital**, a Delaware limited partnership located in New York, New York, is an investment adviser registered with the Commission under the Advisers Act. It is an investment adviser to several mutual funds that had market timing arrangements. Alliance Capital provides investment advisory services to the Funds, and for these services, the Funds pay Alliance Capital a fee as a percentage of average daily net assets the Funds hold. As of September 30, 2003, Alliance Capital had approximately $438 billion in assets under management.

4. **Calugar**, age 49 and a resident of Las Vegas, Nevada, at all relevant times was the President and owner of Security Brokerage, a registered broker-dealer located in Las Vegas, Nevada.

Facts

Market Timing at Alliance Capital

5. Mutual fund market timing is the practice of (a) frequent buying and selling of shares of the same mutual fund or (b) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing, while not illegal *per se*, can harm other mutual fund shareholders because it can dilute the value of their shares, if the market timer is exploiting pricing inefficiencies, or disrupt the management of the mutual fund's investment portfolio and cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

6. The Funds' prospectuses state: "You should consider an investment in the Fund as a long-term investment." Regarding the purchase and sales of shares of the Funds, the prospectuses state: "A Fund may refuse any order to purchase shares. In particular, the Funds reserve the right to restrict purchases of shares (including through exchanges) when there appears to be evidence of a pattern of frequent purchases and sales made in response to short-term considerations." Neither the prospectuses, nor any public documents, disclosed Alliance Capital's practice of providing timing capacity to market timers in return for investments in Alliance Capital's hedge funds.

7. As an investment adviser, Alliance Capital owes a fiduciary duty to its mutual fund advisory clients – a duty of utmost good faith and full and fair disclosure of all material facts and material conflicts of interest. This fiduciary duty requires Alliance Capital to act for the benefit of its mutual fund clients and not to use its clients' assets to benefit itself.

8. In dealing with market timers, including Calugar, Alliance Capital was subject to conflicts of interest and at times advanced its own interest over those of its mutual fund clients, without disclosure of all material facts to the mutual fund boards or shareholders.

9. The fee structure through which Alliance Capital earned management fees meant that Alliance Capital earned fees from the timing relationships. First, Alliance Capital earned fees

from management of mutual funds based on a percentage of assets under management, generally one percent. Thus, to the extent timers increased assets under management, Alliance Capital earned greater fees.

10. Second, Alliance Capital also sponsored and managed hedge funds. The hedge fund is a potentially lucrative source of income, both to Alliance Capital and the hedge fund's portfolio managers. In addition to receiving a fee based on a percentage, generally one percent, of assets under management, Alliance Capital and the hedge fund portfolio manager also received a performance fee based on a percentage, generally 20 percent, of net return on investment.

11. Alliance Capital permitted certain of its mutual funds to be timed by agreement with certain timers, and with brokers acting on behalf of timers. In return for this "timing capacity," Alliance Capital solicited, at various times and in varying proportions, timers to make long-term investments, so-called "sticky assets," in hedge funds, mutual funds, and other investment products managed by Alliance Capital. In particular, with respect to Calugar, Alliance Capital permitted timing in the Funds in return for sticky asset investments in hedge funds managed by the same portfolio managers. Thus, Alliance Capital used timing capacity in its mutual funds to obtain investments in its hedge fund products.

<u>Alliance Capital's Biggest Timer – Daniel Calugar</u>

12. Alliance Capital's single largest timer was Calugar, the owner of Security Brokerage. At his peak in 2003, Calugar had $220 million in timing capacity in Alliance Capital's Funds. Alliance Capital initiated its relationship with Calugar in April 2001, when an Alliance Capital hedge fund salesman negotiated an agreement with Calugar providing market timing capacity in certain Alliance Capital mutual funds in exchange for Calugar's investments in the hedge funds in a ratio of 10:1 mutual fund timing capacity to hedge fund investment. The terms of this agreement were summarized in the text of an April 24, 2001 note from Calugar to a hedge fund salesman:

> I very much appreciate the $10 million timing position that was given to me in Alliance Technology (ALTFX) and Alliance Growth (AGRFX). … You indicated that the managers of these two funds also run hedge funds at Alliance. I have been an active investor in timing mutual funds for 15 years, and have never invested in a hedge fund or similar investment, however, I am willing to make an investment in Alliance hedge funds equal to 10% of the timing allocation that I maintain in your mutual funds. I will keep the hedge fund position as long as I have the timing allocation in the mutual funds. My understanding is that you would be able to give me an exit opportunity from the hedge funds at the end of any month, however, I would not exercise that opportunity as long as I continue to have the timing allocation on the mutual fund side.

13. Shortly thereafter, Calugar began timing the Alliance Technology mutual fund ("Tech Fund") and the Alliance Growth mutual fund, and invested in Alliance Capital hedge funds, including a hedge fund managed by the Tech Fund portfolio managers. As a hedge fund sales

executive later explained in an email, “Calugar would only invest in our hedge funds if we provided him with market-timing space within our [mutual funds].”

14. In June 2001, Alliance Capital agreed to increase Calugar’s market timing capacity to $100 million in the Tech Fund and $20 million in the Alliance Premier Growth mutual fund (“Premier Growth Fund”) with four round trips per month in return for a 20 percent investment in Alliance Capital hedge funds.

15. Laughlin was aware that Calugar was a market timer at Alliance Capital. Laughlin and other members of mutual fund management were copied on a June 2001 series of emails from hedge fund sales personnel. Those emails described aspects of the Calugar arrangement: The Tech Fund portfolio managers “did indeed authorise [sic] up to $100 million of market timing money for Dan Calugar in the Tech fund. Dan has subsequently subscribed to [the portfolio managers’] hedge fund for 20% of the underlying assets as of June 1 in anticipation of this.”

16. Later in 2001, Alliance Capital increased Calugar’s market timing capacity in the Tech Fund to $150 million with the understanding that Calugar would make long-term investments in Alliance Capital hedge funds in a ratio of 5:1 mutual fund capacity to hedge fund investment. Throughout the latter part of 2001, Calugar continued to make additional investments in Alliance Capital hedge funds consistent with the agreed ratios.

<u>Renegotiation of the Calugar Arrangement</u>

17. In January 2002, the Tech Fund portfolio manager complained about a large exchange Calugar made in the Tech Fund, and Alliance Capital cancelled Calugar’s trade. In response, Calugar wrote an email reviewing in detail his arrangement with Alliance Capital, the amount that he was market timing in Alliance Capital mutual funds ($215 million in two mutual funds), and his corresponding investments in Alliance Capital hedge funds ($53 million in three hedge funds). Addressing the potential disruption of his trading to fund management, Calugar suggested the possibility of transferring some market timing funds from the Tech Fund to another one of the Funds, or redeeming part of his investments at Alliance Capital and investing his funds elsewhere. After reading this email, the Tech Fund portfolio manager called the head of hedge fund sales and said he wanted to keep Calugar as a hedge fund client, but he wanted to get him out of the Tech Fund due to the negative impact of Calugar’s frequent trading.

18. Thereafter, Calugar and Alliance Capital representatives (other than Laughlin) had further discussions concerning the terms of his timing capacity in the Funds. Following those discussions, in late January 2002, Laughlin learned that the Tech Fund portfolio manager had experienced cash management problems due to Calugar’s market timing in the Tech Fund.

19. On January 29, 2002, Laughlin sent an email to Alliance Capital’s President, which reviewed the details of Calugar’s timing arrangement and noted the potential for a renegotiated agreement:

> Following our telephone conversation, I spoke with [the head of hedge fund sales and the Tech Fund portfolio manager] to get the latest on Dan Calugar who has placed roughly $150 million of "timer" money into the Tech Fund and $30 million into the Tech Hedge Fund. Calugar also placed $55 million into Premier Growth as an offset to $17 million into Alpha 20 and $4 million in the Muni Hedge Fund. Apparently the original ratio of "timer" money to Hedge Fund investments was negotiated at 5 to 1 . . .. This deal was negotiated outside the system that [the head of domestic mutual fund sales] set up … which generally discourages "timers" altogether, but controls the few we do have.
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> [The head of hedge fund sales] has spoken to Calugar, and thinks he can negotiate a better deal for Alliance. [The head of hedge fund sales] is also going to speak with [the Market Timing Supervisor] to set up better controls over the round trips in order to protect the fund shareholders. According to [the Tech Fund portfolio manager], this has not been an issue except for a brief volatile period in January when he was forced to reduce his cash position from 6% to 4% in order to cover a redemption. …
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> Obviously, [the Tech Fund portfolio manager], [the head of hedge fund sales] and presumably the other portfolio managers want to keep the relationship. According to [the head of hedge fund sales], [the Alliance Capital Chief Executive Officer] is OK with this. From purely a Mutual Funds standpoint, we get very little out of this, and would not be disappointed to see Calugar go away. As you know, he has made a lot of money on this deal by trading the funds. [The head of hedge fund sales] points out that the Hedge Funds appear to be virtual loss leaders for his timing practice.

20. In an email reply, Alliance Capital's President noted the financial benefit to Alliance Capital from the relationship with Calugar in the form of increased management fees: "Assuming the assets stay in [t]he funds for a year our fund management fees come out to about $1.8 million per year. Assuming no impact on our shareholders and no unique operational issues it is beneficial to our funds group by retaining 55% of the fees."

21. The head of hedge fund sales then renegotiated with Calugar the terms of his timing arrangement and sent an email to Laughlin and others describing the new arrangement, including: (1) "ratios are reset from 5:1 mutual to hedge investment to 4:1 for Premier Growth and 3:1 for Tech;" (2) "Calugar's mutual fund trades will be made in $10MM 'blocks';" and (3) Calugar "will redeem all hedge fund positions" annually.

22. The renegotiated terms benefited Alliance Capital. The new ratios meant more money for the hedge funds for the same timing capacity. The annual redemption of Calugar's hedge fund positions also benefited Alliance Capital. By Calugar agreeing to redeem and reinvest his hedge fund positions annually, Alliance Capital increased its opportunity to profit from Calugar's hedge fund investments. Each time Calugar redeemed, Alliance Capital would be

eligible to earn performance fees from any increase in value, without having first to earn back any prior losses.

Calugar's Market Timing Continued

23. In or about July 2002, Alliance Capital increased Calugar's timing capacity in the Premier Growth Fund from $17 million to $57 million. In or about September 2002, Alliance Capital granted Calugar $56 million timing capacity in the Alliance Growth & Income mutual fund ("Growth & Income Fund"), and Calugar invested in a hedge fund managed by the same portfolio manager.

24. Alliance Capital made substantial efforts to accommodate and retain Calugar's business. Thus, when another portfolio manager complained about Calugar's trading, Alliance Capital reduced Calugar's timing capacity in that mutual fund, only to increase his timing capacity in other Alliance Capital mutual funds. For example, in early 2003, the portfolio manager for the Premier Growth Fund complained about Calugar's trading in his mutual fund. Thereafter, Alliance Capital decreased Calugar's timing capacity in the Premier Growth Fund by $20 million and increased his timing in the Tech Fund and another mutual fund by the same amount. As the head of hedge fund sales explained in an email to Calugar: "In order further to reduce your exchanges in Premier Growth Fund from $70MM to $50MM … [a portfolio manager in another mutual fund] has agreed to increase your exchange limit … from $43MM to $53MM and [the Tech Fund portfolio manager] has agreed to increase your exchange limit on Tech from $100MM to $110MM."

25. In late January 2003, the Tech Fund portfolio manager told Laughlin that he was concerned that Calugar's market timing in the Tech Fund could hurt fund performance. The Tech Fund portfolio manager also told Laughlin that Calugar's investment in the Technology hedge fund was an important source of incentive compensation for his personnel and he was worried that if he reduced Calugar's timing capacity, Calugar might withdraw his hedge fund investment.

26. On January 31, 2003, Laughlin, the Tech Fund portfolio manager, the head of hedge fund sales and others discussed Calugar's arrangement with Alliance Capital ("January 31, 2003 Meeting"). At this meeting, the Tech Fund portfolio manager complained about Calugar's market timing but said that Calugar's hedge fund investments could be potentially valuable to Alliance Capital.

27. By January 2003, Calugar's investments were critical to Alliance Capital's hedge funds. By early 2003, Calugar's investments in the Alliance Capital hedge funds became such a large percentage of the hedge fund assets that the hedge funds could not survive without Calugar. In their discussion at the January 31, 2003 Meeting, the head of hedge fund sales noted that Calugar's investments were important to the continued survival of the hedge funds.

28. Immediately after the January 31, 2003 Meeting, Laughlin met with Alliance Capital's President and discussed the Calugar arrangement. Laughlin said that the Tech Fund portfolio manager was concerned that Calugar's trading was disruptive to the Tech Fund, but the

Tech Fund portfolio manager was worried about losing Calugar as a hedge fund investor if he reduced Calugar's market timing capacity.

29. Although Laughlin was aware that the linkage between Calugar's market timing activity and hedge fund investments was improper, Calugar's timing activity continued.

30. Laughlin did not advise the Funds' Board of Directors about Calugar's arrangement with Alliance Capital.

31. Timers harmed the Tech Fund. In July 2003, at a meeting of the Tech Fund board of directors (which Laughlin did not attend), the portfolio manager gave a presentation on the performance of the Tech Fund. In a chart entitled, "Impact From Market Timers," the portfolio manager stated his belief that, the performance of the Tech Fund was diminished by 1.4 percent during the first six months of 2003 due to market timers.

32. Calugar benefited from the relationship. From 2001 to 2003, Calugar generated approximately $64 million in profits from timing the Alliance Capital mutual funds, including the Tech Fund. During the same period, the net asset value of the Tech Fund declined substantially.

Violations

33. As a result of the conduct described above, Laughlin willfully aided and abetted and caused Alliance Capital's violations of Sections 206(1) and 206(2) of the Advisers Act. Specifically, Laughlin knowingly, recklessly and/or negligently: (1) was one of the Alliance Capital senior executives that in effect approved excessive short-term trading by Calugar in the Funds that was not disclosed in the Funds' prospectus and that was potentially harmful to the Funds; and (2) failed to ensure that the Funds' Boards or the Funds' shareholders were apprised of the conflict of interest created by Alliance Capital entering into a market timing arrangement with Calugar that was potentially harmful to the Funds, but that increased Alliance Capital's advisory fees from the Funds and from Alliance Capital's hedge funds.

34. As a result of the conduct described above, Laughlin willfully aided and abetted and caused Alliance Capital's violations of Section 17(d) of the Investment Company Act and Rule 17d-1 thereunder, which make it unlawful for any affiliated person of, or principal underwriter for a registered investment company, or any affiliated person of such a person or principal underwriter, acting as principal to effect any transaction in which such registered company, or company controlled by such registered company, is a joint or a joint and several participant with such person, principal underwriter, or affiliated person, in contravention of such rules and regulations as the Commission may prescribe for the purpose of limiting or preventing participation by such registered or controlled company on a basis different from or less advantageous than that of such other participant. Rule17d-1 makes it unlawful for any affiliated person to participate in any such joint arrangement unless it files an application regarding such joint enterprise or arrangement with the Commission. Specifically, Alliance Capital, as investment adviser, was an affiliated person of the Funds and caused the Funds to enter into joint arrangements whereby Alliance Capital accepted long-term assets from Calugar in Alliance Capital hedge funds pursuant to an arrangement

allowing Calugar to engage in market timing activities which were inconsistent with the Funds' prospectuses. As Executive Vice President of Alliance Capital, Laughlin was one of the officers who in effect approved the arrangements, and the Commission never granted an order approving the transactions.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Laughlin's Offer.

Accordingly, it is hereby ORDERED that**:**

A. Pursuant to Section 203(k) of the Advisers Act and Section 9(f) of the Investment Company Act, that Respondent Laughlin cease and desist from committing or causing any violations and any future violations of Sections 206(1) and 206(2) of the Advisers Act and Section 17(d) of the Investment Company Act and Rule 17d-1 thereunder;

B. Pursuant to Section 15(b) of the Exchange Act, Section 203(f) of the Advisers Act and Section 9(b) of the Investment Company Act, Respondent Laughlin shall be, and hereby is, suspended for a period of twelve months from the date of the Order from association with any broker, dealer, or investment adviser; and is prohibited from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter for a period of twelve months, effective on the date of the Order.

C. For three years from the date of this Order, Respondent Laughlin shall not serve as a chairman, director, or officer of any broker, dealer, investment adviser or registered investment company.

D. Respondent Laughlin shall, upon the entry of this Order, pay a civil penalty in the amount of $325,000 and disgorgement in the amount of $1 to the United States Treasury. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies Michael J. Laughlin as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Helene Glotzer, Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, 233 Broadway, New York, NY 10279. Such civil money penalty may be distributed pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002 ("Fair Fund distribution"). Regardless of whether any such Fair Fund distribution is made, amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that he shall not, after offset or reduction in any Related Investor Action based on Respondent's payment of disgorgement in this action, further benefit by

offset or reduction of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that he shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the United States Treasury or to a Fair Fund, as the Commission directs. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Jonathan G. Katz
Secretary