



THE MONEY MANAGEMENT INSTITUTE

Legal/Regulatory Affairs Conference for General
Counsels & Chief Compliance
December 6, 2005

New Developments in SMAs and their Regulatory Dimensions

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C O U N S E L O R S A T L A W

New Developments in SMAs

- Model Account Programs
- Hedge Funds in SMA accounts
- Use of variable annuities in SMA accounts
- Distribution and Sales Practices
- “Suppression” of Customer Notices

Model Account Programs

- Legal relationship between model manager & clients
 - Client or 3rd party beneficiary?
- ADV delivery issues / Showing sleeve manager performance
 - Will delivery foster impression of client relationship?
- Timing of model updates
 - How often?
 - Affect on investment opportunities of other clients?
 - Ability to delay
 - Issues under proposed SEC rules for dissemination of holdings information
- Trade sequencing issues

Hedge Funds in SMA accounts

- Types of hedge funds
- Marketing and private placement issues
 - Regulation D
 - NASD advertising issues & risk disclosures
- Suitability issues
 - Due diligence
 - Layering of fees
 - Liquidity & complications in rebalancing
- Eligibility issues
 - Accredited investor/qualified purchaser issues
 - ERISA issues
- Reporting issues
 - Valuation
- Compensation issues
 - Sales loads
 - Placement agent fees

Variable Annuities in SMA Accounts

- Regulatory Backdrop
 - NASD Concerns & Proposed Risk Disclosure Document
 - Recent NASD Enforcement Actions
- Suitability
 - Both at annuity contract level and the underlying fund level
 - Layering of fees and costs
 - Surrender charges and IRS penalties
 - Sales charges
 - Fees (including mortality and administrative fees, investment advisory fees and charges for riders or special features)
- Licensing and agent appointments
 - Finders fee issues

Distribution and Sales Practices

- Increasing sales through intermediaries
 - From wire houses to smaller firms & financial planners
 - Co-advisers versus solicitors
- Sales loads/termination penalties
 - Constellation Financial, SEC Staff No-Action letter (January 9, 2003)
- Fee differential issues
 - Especially where fee varies for same strategy between
 - Affiliated versus unaffiliated managers
 - Different programs offered
 - Disclosure and suitability

“Suppression” of Customer Notices

- Trade Confirmations
- Notices of Agency-Cross Trades (pursuant to Advisers Act Rule 206(3)-2 and ERISA PTCE 86-128)
- Prospectuses and SAIs
- Rule 173 Registration Notices
- Shareholder Communications, including Proxies, Annual Reports & Tender Offer Communications
- Reorganization & Bankruptcy Notices
- SEC Fairness Fund Notices
- Class Action Notices and Proofs of Claim
- Payment for Order Flow Disclosures
- Margin Account Disclosure
- Options Disclosure Documents



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