UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9893 / August 17, 2015

SECURITIES EXCHANGE ACT OF 1934
Release No. 75710 /August 17, 2015

INVESTMENT ADVISERS ACT OF 1940
Release No. 4174 / August 17, 2015

ADMINISTRATIVE PROCEEDING
File No. 3-16757

In the Matter of **Citigroup Alternative Investments LLC and Citigroup Global Markets Inc.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933, SECTION 15(b)(4) OF THE SECURITIES EXCHANGE ACT OF 1934, AND SECTIONS 203(e) and 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

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 8A of the Securities Act of 1933 ("Securities Act"), Section 15(b)(4) of the Securities Exchange Act of 1934 ("Exchange Act"), and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") against Citigroup Alternative Investments LLC ("CAI") and Citigroup Global Markets Inc. ("CGMI") (together, "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have 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 Respondents and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, Section 15(b)(4) of the Securities Exchange Act of 1934, and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offer, the Commission finds that:

Summary

These proceedings concern material misstatements and omissions made by Respondents between 2002 and 2007 in the offer and sale of securities in two now-defunct hedge funds—the ASTA and MAT funds ("ASTA/MAT") and the Falcon Strategies funds ("Falcon"). The ASTA/MAT and Falcon funds were recommended and sold by two groups of individuals, the "financial advisers" of Smith Barney and the "private bankers" of Citigroup Private Bank (together, the "financial advisers"), to their advisory clients. The financial advisers were associated with respondent CGMI. Both funds were managed by respondent CAI, which acted through its employees, including an employee who had a primary role in creating the funds and serving as the funds' manager during the relevant time period (the "fund manager"). Respondents raised approximately $2.898 billion from approximately 4,000 investors in ASTA/MAT and Falcon. In 2008, both funds collapsed resulting in billions of dollars in losses.

From 2002 through 2008 (the "relevant period"), financial advisers and the fund manager misrepresented the funds' risks and performance to advisory clients, who were told that the investments were "safe," "low-risk," "bond substitutes" and suitable for traditional bond investors, despite statements in marketing documents that the funds should not be viewed as a bond substitute. In addition, while the risk of principal loss was disclosed in written materials provided to clients, certain financial advisers and the fund manager orally minimized the significant risk of loss resulting from, among other things, the funds' investment strategy and use of leverage. Investors were also told that the biggest risk facing ASTA/MAT was the adoption of a flat income tax by the federal government. Financial advisers encouraged many of their advisory clients to sell portions of their bond portfolios in order to invest in the funds. In late 2007, financial advisers and the fund manager continued to offer and sell Falcon as a safe, low-risk investment, even though both funds—the Falcon fund was 20 percent invested in the ASTA/MAT fund—began experiencing increased margin calls and liquidity problems in the second half of 2007 that continued until the funds collapsed.

Moreover, the fund manager was involved in virtually all fund-related communications with the financial advisers and investors. The fund manager and the fund manager's staff were responsible for drafting and reviewing offering materials for the funds, crafting sales pitches to investors, training CAI sales personnel (who, in turn, were responsible for marketing the funds to the financial advisers), drafting quarterly investor reports, disclosing interim fund performance, and managing the funds themselves. Furthermore, throughout the fund offerings and fund operations, the fund manager and the fund manager's staff at CAI met with prospective investors and responded directly to inquiries from the financial advisers concerning the funds without sufficient oversight governing those oral communications. The fund manager and his staff at CAI had significant influence over the dissemination of information relating to the funds without review or oversight, including information relating to the funds' risks and performance. CAI failed to implement a system in which the fund manager's authority was checked adequately or to ensure that the fund manager's communications with investors and financial advisers concerning the ASTA/MAT and Falcon funds were accurate and not misleading.

Respondents

1. **CAI** is an indirect wholly-owned subsidiary of Citigroup Inc. and has its principal place of business in New York, New York. CAI was the investment manager for the ASTA/MAT and Falcon funds. CAI had its own sales force, or "wholesalers," who, along with the fund manager and the fund manager's staff, were responsible for marketing the ASTA/MAT and Falcon funds to the financial advisers. During the relevant period, CAI had approximately $59 billion in assets under management. CAI has been registered as an investment adviser with the Commission since 2002.

2. **CGMI** is an affiliated company of Citigroup Inc. and has its principal place of business in New York, New York. During the relevant period, Smith Barney was a business division of CGMI. The financial advisers who recommended and sold ASTA/MAT and Falcon fund shares to investors were associated persons of CGMI. In 2009, Smith Barney entered into a joint venture with Morgan Stanley Global Wealth Management Group to become Morgan Stanley Smith Barney, in which Citigroup owned a 49 percent stake in the venture and Morgan Stanley owned the remaining 51 percent. In 2012, Morgan Stanley purchased Citigroup's interest in the joint venture. CGMI has been registered with the Commission since 1960 as both an investment adviser and a broker-dealer.

Background

3. From September 2002 through February 2007, Respondents offered and sold approximately $1.962 billion of investments in ASTA/MAT to approximately 2,700 investors and advisory clients of CGMI. ASTA/MAT was a municipal arbitrage fund that purchased municipal bonds and used a Treasury or LIBOR swap to hedge interest rate risks. The ASTA/MAT fund employed 8-12 times leverage.

4. From October 2004 through October 2007, Respondents offered and sold approximately $936 million of investments in Falcon to approximately 1,300 investors and advisory clients of CGMI. Falcon was a multi-strategy fund that invested in ASTA/MAT and other fixed income strategies, such as CDOs, CLOs, and asset-backed securities. The Falcon fund employed 5-6 times leverage.

5. Falcon and ASTA/MAT were managed in accordance with disclosed investment strategies, including leverage guidelines. Falcon and ASTA/MAT were not offered generally to retail investors, but were limited to "qualified purchasers" as defined by Section 2(a)(51)(A) of the Investment Company Act of 1940 and "accredited investors" within the meaning of Rule 501(a) of Regulation D of the Securities Act of 1933. In addition, Respondents recommended that investors in Falcon invest no more than 10 percent of their assets and that investors in ASTA/MAT invest no more than 5 percent of their assets.

6. Investors in the ASTA/MAT and Falcon funds paid advisory fees for essentially receiving two tiers of investment advice. First, the investors in both ASTA/MAT and Falcon were advisory clients of the financial advisers (who were associated with CGMI) and paid for investment advice, including placement fees relating to their investments. Secondly, CAI, acting primarily through the fund manager and the fund manager's staff, managed both the ASTA/MAT and Falcon funds and received management fees from the investors. Investors in ASTA/MAT and Falcon directly or indirectly paid CAI and CGMI a total of approximately $212.5 million in fees associated with investments in the two funds. Of this amount, the Respondents returned approximately $72.5 million to investors as compensatory payments following the collapse of the funds.

7. Respondents, acting through associated persons—the financial advisers, in the case of CGMI, and the fund manager, in the case of CAI—made material misstatements and omissions to investors in the offer and sale of shares in the ASTA/MAT and Falcon funds.

Respondents' Violations

8. Financial advisers and the fund manager orally represented to investors that Falcon was a "safe," "low-risk" investment, akin to a "bond substitute" or "bond alternative" that had the same risk profile as a municipal bond investment but with a slightly higher return. Internal sales pitches stated that Falcon "walks like a bond, talks like a bond, [has] cashflow like a bond" and described Falcon as a "better version of a bond." Consistent with that marketing theme, Falcon was benchmarked against the Lehman Aggregate Bond Index, which is used to evaluate the performance of bond portfolios. Some investors were encouraged to sell their unleveraged bond portfolios in order to purchase shares in the Falcon fund.

9. Financial advisers, the fund manager and other CAI staff involved in the marketing of the funds also orally represented to investors that ASTA/MAT was a "safe," "low-risk" investment, notwithstanding certain risk disclosures in the ASTA/MAT offering materials. Financial advisers, the fund manager and other CAI staff involved in the marketing of the funds told investors that ASTA/MAT had a very low risk of permanent loss, particularly if investors were willing to hold the investment for at least five years. Financial advisers and the fund manager also told investors that the biggest risk facing the ASTA/MAT fund was the adoption of a flat income tax by the federal government. Some investors were encouraged to sell their bond portfolios in order to purchase shares in the ASTA/MAT fund.

10. Financial advisers, the fund manager and other CAI staff involved in the marketing of the funds made false and misleading statements regarding the risks associated with an investment in the ASTA/MAT and Falcon funds. The funds were not bond substitutes, and an investment in the funds carried significantly greater risk than a bond investment. The funds used significant amounts of leverage that increased the risk of both margin calls and loss in value. In fact, Citigroup Private Bank had an internal risk rating system that rated the funds as having "significant risk to principal." That rating, however, was not shared with the majority of investors and financial advisers.

11. Furthermore, CAI performed back-testing on a hypothetical ASTA/MAT portfolio to evaluate the fund's performance over a period of time. The back-testing analysis showed that an investment in the ASTA/MAT fund carried far greater risk than that described to investors. CAI, however, misrepresented the results of that back-testing analysis. Some financial advisers and investors were told that the hypothetical ASTA/MAT portfolio had been back-tested over a five-year period (1996 to 2001), and that, over such period, the largest decline in the portfolio was approximately 7 percent. That statement was false because the back-testing actually showed that the portfolio, when fluctuations in bond prices over the entire time period were analyzed, declined by up to 32 percent in value. Moreover, CAI actually had back-tested the hypothetical ASTA/MAT portfolio over a six-year period (1995 to 2001), during which time the portfolio declined by approximately 48 percent. Consequently, the risk of loss associated with an investment in the ASTA/MAT fund, which also accounted for approximately 20 percent of Falcon's investments, was significantly higher than conveyed to some financial advisers and investors.

12. CAI and CGMI failed to require any changes in the way in which the funds were described to investors, even as the funds' performance significantly declined and the risk of investor losses increased.

13. In August 2007, the Falcon fund experienced margin calls. Lender or leverage provider valuations for fund assets declined significantly while the amount of collateral demanded by those lenders increased. In order to generate necessary liquidity and to meet increasing margin calls, the fund manager sold approximately $2 billion of fund assets, and made an "urgent request" for a "contingency liquidity plan"—essentially a loan from CAI or Citigroup Inc.—in the amount of $200 million for Falcon, which was denied.

14. As the Falcon fund experienced significant declines in liquidity, the fund manager and some financial advisers misrepresented the fund's performance and liquidity to investors, who were assured that Falcon had low liquidity risks and secure financing terms. The investors were not informed of Falcon's liquidity issues, the sale of $2 billion in fund assets to meet margin calls, or the fund manager's request for a $200 million loan from CAI or Citigroup Inc.

15. In September and October 2007, the financial advisers and CAI, acting through the fund manager and the fund manager's staff, recommended, offered and sold additional shares in the Falcon fund, and raised approximately $110 million from new investors without disclosing

how the declining market conditions of the time were affecting Falcon's liquidity. In fact, CAI and CGMI continued to recommend the funds as safe, low-risk investments.

16. From November 2007 through March 2008, Falcon continued to experience a severe liquidity shortage. Internally, the fund manager stated that the fund's liquidity was "getting close to dangerous territory." The fund manager sold over $6.4 billion of fund assets between November 2007 and January 2008 to generate liquidity, and re-submitted a contingency liquidity plan request to supervisors at CAI for $400 million. This, too, was denied. By January 2008, the fund manager had drawn up potential "liquidation scenarios" for the Falcon fund.

17. During this period, the fund manager and some financial advisers, however, continued to misrepresent Falcon's performance and liquidity to investors by telling them that Falcon had "adequate liquidity" and reassuring investors that the fund was "well capitalized." They failed to disclose the fund's requests for liquidity support—which were denied by CAI and Citigroup Inc. —the increasing margin calls, and the sale of over $8.4 billion in fund assets to meet Falcon's margin calls. CAI lacked policies and procedures that would have ensured that communications with investors were consistent with the funds' actual performance and liquidity position.

18. During this same time period—late 2007 and early 2008—the fund manager also orally misrepresented the condition of the ASTA/MAT fund and its ability to survive a declining market. By the fall of 2007, the fund manager was instructed by supervisors at CAI to begin selling ASTA/MAT assets in order to reduce the fund's leverage. Despite the negative market conditions and instructions to begin reducing leverage, the fund manager continued to tell investors that the biggest risk to the fund was the adoption of a flat income tax by the federal government. The fund manager reassured investors just weeks before the fund collapsed that the risk of loss was minimal.

19. CAI failed to adopt and implement policies and procedures to prevent the misrepresentations made to investors. The fund manager had virtually complete control of the information disseminated to investors without sufficient review to ensure that those communications were accurate. CAI employed its own sales personnel, or wholesalers, who were educated on the funds by the fund manager. The fund manager and the fund manager's staff drafted sales pitches for the wholesalers that were not subject to review or approval by anyone outside of the fund manager's staff, including anyone in the compliance group. Those sales pitches and talking points misrepresented the risks of the funds. The wholesalers, in turn, were responsible for marketing the funds to the financial advisers. The fund manager and the fund manager's staff were also responsible for educating the financial advisers on the risks of the funds, and fielded client and other inquiries from financial advisers concerning the funds. Finally, in many instances, the fund manager and the fund manager's staff also had direct communications with investors, during which they misrepresented the funds' risks. CAI failed to exert reasonable oversight for the sales pitches, talking points, and oral communications made by the fund manager to the financial advisers and investors.

20. In addition, the fund manager and the fund manager's staff played a significant role in drafting and disseminating information regarding the funds to investors and financial advisers without sufficient review or oversight to ensure that the information given to investors was accurate. In particular, the fund manager and the fund manager's staff designed, implemented and analyzed the back-testing for ASTA/MAT. They also drafted the quarterly investor reports and provided investors and financial advisers with performance information orally in meetings and on conference calls that did not fully disclose negative fund performance. CAI failed to exert reasonable oversight over these functions.

21. As a result of the conduct described above, CAI and CGMI willfully violated Sections 17(a)(2) and 17(a)(3) of the Securities Act, which prohibit fraudulent conduct in the offer or sale of securities. In addition, CGMI willfully violated Section 206(2) of the Advisers Act, which prohibits any adviser from engaging in any transaction, practice or course of business which operates as a fraud or deceit upon any client or prospective client, and CAI willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 promulgated thereunder, which prohibit an investment adviser from providing investment advice to clients without adopting and implementing written policies and procedures reasonably designed to prevent violation of the Act and the Rules adopted under the Act, and Rule 206(4)-8 promulgated thereunder, which prohibits an investment adviser to a pooled investment vehicle from making any untrue statement of a material fact or omitting to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle.

IV.

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

Accordingly, pursuant to Section 8A of the Securities Act, Section 15(b)(4) of the Exchange Act and Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that**:**

A. Respondents CAI and CGMI shall cease and desist from committing or causing any violations and any future violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act. Additionally, CGMI shall cease and desist from committing or causing any violations and any future violations of Section 206(2) of the Advisers Act, and CAI shall cease and desist from committing or causing any violations and any future violations of Section 206(4) of the Advisers Act and Rules 206(4)-7 and 206(4)-8 promulgated thereunder.

B. Respondents CAI and CGMI are censured.

C. Respondents shall, within ten days of the entry of this Order, pay disgorgement of $139,950,239 and prejudgment interest of $39,612,089 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. Payment must be made in one of the following ways:

(1) Respondents may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
(2) Respondents may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or
(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Citigroup Alternative Investments LLC and Citigroup Global Markets Inc. as Respondents in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Sanjay Wadhwa, Senior Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, New York Regional Office, Brookfield Place, 200 Vesey Street, Suite 400, New York, NY 10281.

D. A plan of distribution shall be submitted within 120 days of payment in full by Respondents of the disgorgement and prejudgment interest ordered. Commission staff may extend the deadline for plan submission for good cause shown. Respondents shall bear the costs of any administration and distribution of funds to investors in the ASTA/MAT and Falcon funds ordered hereunder, including all fees of professionals that provide related services to the distribution of the fund, including tax administration. A fund administrator shall be entitled to reasonable fees and reimbursement for reasonable costs and expenses in connection with overseeing and administering the fund distribution. Respondents will pay all reasonable costs and expenses associated with the administration of the distribution, including the cost of the fund administrator bond.

By the Commission.

Brent J. Fields
Secretary