

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**INVESTMENT ADVISERS ACT OF 1940**  
**Release No. 2633 / August 15, 2007**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-12724**

**In the Matter of**

**Schultze Asset Management  
LLC and George J. Schultze,**

**Respondents.**

**ORDER INSTITUTING  
ADMINISTRATIVE AND CEASE-AND-  
DESIST PROCEEDINGS, MAKING  
FINDINGS, AND IMPOSING REMEDIAL  
SANCTIONS AND A CEASE-AND-DESIST  
ORDER PURSUANT TO SECTIONS  
203(e), 203(f) AND 203(k) OF THE  
INVESTMENT ADVISERS 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 Sections 203(e), 203(f) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Schultze Asset Management LLC and George J. Schultze (collectively “Respondents”).

**II.**

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the “Offers”) 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 them 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, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 203(e), 203(f) and 203(k) of the Advisers Act (the “Order”), as set forth below.

**III.**

On the basis of this Order and Respondents’ Offers, the Commission finds that:

**Respondents**

1. Schultze Asset Management LLC (“SAM”), incorporated in 1998, has been registered with the Commission as an investment adviser since June 9, 2003. SAM is based in Purchase, New York and at the time of its initial registration with the Commission had assets

under management of less than \$50 million. SAM currently has approximately \$733 million in assets under management, with approximately \$629 million of those assets in hedge funds managed by SAM.

2. George J. Schultze (“Schultze”), age 37, is the sole principal of SAM. He lives in Rye Brook, New York.

### **Other Relevant Entity**

3. SAMCO Distributors Inc. (“SAMCO”), incorporated by Schultze in 2001 and dissolved in 2005, had no office space other than its registered agent’s office in Delaware. SAMCO’s only asset was an electronic database of valuation spreadsheets that SAM sold to SAMCO for \$1 pursuant to an asset sale agreement executed by Schultze on SAM and SAMCO’s behalf. SAMCO then licensed the database back to SAM at a rate of \$100 per hour. Schultze and SAM used SAMCO to secure soft dollar payments from broker-dealers to cover SAM’s operating expenses by representing to them that the payments were for research.

### **Summary**

4. This matter involves SAM’s violations of the books and records and antifraud provisions of the Advisers Act, and Schultze’s aiding and abetting of those violations. SAM misrepresented its client commission (“soft dollar”) practices to an advisory client and, when asked by the Commission’s Examination staff for documents pertaining to its soft dollar practices, SAM failed to produce and modified certain of those books and records.

5. Specifically, Schultze, on behalf of SAM, represented and certified three different times to an advisory client (“Client”) that SAM was using client commissions generated by the account *only* for expenses covered by the safe harbor provided by Section 28(e) of the Securities Exchange Act of 1934 (“Exchange Act”) when, in fact, SAM knowingly used client commissions generated by the account to pay for *non*-Section 28(e) expenses, including Schultze’s salary.

6. In addition, SAM, through Schultze, used SAMCO, to secure soft dollar payments from broker-dealers to cover some of SAM’s operating expenses. SAMCO had no business purpose other than to provide a vehicle by which SAM and Schultze could secure soft dollars to pay SAM’s operating expenses and Schultze’s personal expenses. Schultze, in an attempt to conceal SAMCO’s role from the Commission’s Examination staff, failed to provide to the Examination staff a key agreement relating to SAMCO and then gave the staff a modified version of a second agreement.

### **Facts**

#### **SAM’s False and Misleading Soft Dollar Representations**

7. Prior to the spring of 2005, SAM, through Schultze, used soft dollars generated by transactions executed on behalf of its clients to cover its operating expenses, including salary, rent and health insurance. Such expenses were and are plainly outside of the safe harbor created by Section 28(e) of the Exchange Act, which, under certain circumstances, enables a money

manager, consistent with its fiduciary duty, to use commissions generated by client transactions to pay for certain “brokerage and research services.”<sup>1</sup>

8. In January 2004, Schultze, on behalf of SAM, entered into an advisory contract with Client under which SAM agreed to limit its use of soft dollars from executions on Client’s behalf to expenses within the Section 28(e) safe harbor, that is, to brokerage and research services. In each subsequent quarter of 2004, Schultze certified to Client in writing that it was in compliance with this soft dollar policy. Despite these representations, however, SAM willfully obtained, between 2004 and 2005, over \$20,000 in soft dollars generated by transactions on behalf of Client to pay for SAM’s operating expenses, including Schultze’s salary – expenses that were, and are, outside the Section 28(e) safe harbor.

#### SAM Failed to Provide Records and Modified an Agreement

9. During an inspection in the spring of 2005, the Commission’s Examination staff sought information from SAM concerning its soft dollar practices. In conducting its examination, the staff discovered references to SAMCO and asked for all agreements between SAM and SAMCO.

10. SAMCO was formed by Schultze in 2001 and, shortly thereafter, he executed an asset sale agreement transferring SAM’s electronic database of valuation models – Microsoft Excel spreadsheets Schultze created to analyze investment opportunities for SAM’s clients – to SAMCO in exchange for \$1. SAM, through Schultze, failed to produce this agreement to the Examination staff. Also in 2001, Schultze executed a second agreement whereby SAMCO licensed the database back to SAM at a rate of \$100 per hour. The licensing agreement stated that all payments made to SAMCO were to “fall within the purview of section 28(e).” SAM, through Schultze, failed to produce the original, executed licensing agreement to the Examination staff and, as described below, produced a modified version of the agreement to the Examination staff.

11. After execution of the sale and license agreements, Schultze continued, as before, conducting investment research and creating valuation spreadsheets for the benefit of SAM’s clients at his home and at SAM’s offices. However, SAMCO had no employees, no physical address, no clients and did not seek to obtain clients for its valuation research database. Instead, Schultze used SAMCO to secure soft dollar payments from broker-dealers to cover some of SAM’s operating expenses and his own personal expenses by representing to broker-dealers that the payments were for research services. Schultze accomplished this by regularly preparing invoices from SAMCO to SAM for “Electronic Database Research Services” and then forwarding the invoices to broker-dealers for payment. The broker-dealers, in turn, paid SAMCO with soft dollars generated by brokerage transactions executed on behalf of SAM’s clients. Schultze used the approximately \$350,000 in soft dollar payments made to SAMCO to pay SAM’s operating expenses and his own personal expenses. Those expenses were, and are, outside the safe harbor provided by Section 28(e).

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<sup>1</sup> See generally Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act, Release No. 34-54165 (July 18, 2006).

12. In response to the Examination staff's inquiries regarding SAMCO, Schultze tried to recast SAMCO as a vehicle to pay his salary. Thus, during the examination, SAM, through Schultze, printed out an electronic version of the 2001 licensing agreement, but with an added sentence not contained in the executed version. The added sentence stated that "all payments to [SAMCO] under this agreement will subsequently be credited to George Schultze as salary." The change was designed to cloud the true nature of SAMCO. Schultze signed this modified version of the agreement and provided it to the Examination staff as if it were the original licensing agreement.

#### SAM's Return of Funds and Retention of a Compliance Consultant

13. When the Examination staff continued questioning the SAMCO payments, SAM undertook certain remedial efforts. SAM voluntarily returned approximately \$350,000 to its clients, representing all soft dollar payments made by broker-dealers to SAMCO. In addition, SAM voluntarily retained the services of an outside compliance consulting firm to assist SAM with fulfilling its obligations under the Advisers Act.

#### Violations

14. Section 206(1) of the Advisers Act prohibits an investment adviser from employing any device, scheme, or artifice to defraud any client or prospective client. Section 206(2) of the Advisers Act makes it unlawful for an adviser to engage in any transaction, practice or course of business that operates as a fraud or deceit upon any client or prospective client. As a result of the conduct described above, SAM willfully violated, and Schultze willfully aided and abetted and caused SAM's violations of, Sections 206(1) and 206(2) of the Advisers Act by misrepresenting to Client that it was restricting its use of soft dollars, with respect to Client, to those expenses covered by Section 28(e) of the Exchange Act and by using soft dollar payments associated with transactions on Client's behalf to cover SAM's operating expenses, including Schultze's salary.

15. Section 204 of the Advisers Act requires that investment advisers registered with the Commission maintain and preserve such books and records as the Commission may prescribe by rule and make them available to Commission representatives during examinations. Rule 204-2(a) under the Advisers Act requires that registered investment advisers "make and keep true, accurate and current . . . (10) [a]ll written agreements (or copies thereof) . . . relating to the business of such investment adviser." As a result of the conduct described above, SAM willfully violated, and Schultze willfully aided and abetted and caused SAM's violations of, Section 204 of the Advisers Act and Rule 204-2(a)(10) promulgated thereunder by failing to maintain and provide to Commission Examination staff true, accurate or current written agreements relating to SAM's business.

#### Remedial Efforts

16. In determining to accept Respondents' Offers, the Commission considered the remedial acts voluntarily undertaken by SAM.

#### IV.

##### Undertakings

Respondent SAM undertakes to:

17. Mail or cause the hedge fund administrator to mail a copy of this Order to each existing investor in any hedge fund SAM manages and to each investment advisory client of SAM within 30 days following the entry of this Order. The Order shall be sent by certificate of mailing, along with a cover letter in a form not unacceptable to the staff of the Commission. Within seven calendar days after the expiration of the 30-day period following the entry of this Order, SAM shall notify Bruce Karpati, Assistant Regional Director of the New York Regional Office, in writing that this undertaking has been completed.

18. From the effective date of this Order until the expiration of 12 months, provide a copy of the Order to all prospective investors in hedge funds managed by SAM and prospective investment advisory clients of SAM not less than 48 hours prior to entering into any written or oral investment arrangement (or no later than the time of entering into such contract, if the investor has the right to terminate the contract without penalty within five business days after entering into the contract). Within one month after the expiration of this 12-month period, SAM shall notify Bruce Karpati, Assistant Regional Director of the New York Regional Office, in writing that this undertaking has been completed.

#### V.

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

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 203(e) of the Advisers Act, SAM be, and hereby is, censured;

B. Pursuant to Section 203(f) of the Advisers Act, Schultze be, and hereby is, censured;

C Pursuant to Section 203(k) of the Advisers Act, SAM and Schultze cease and desist from committing or causing any violations and any future violations of Sections 204, 206(1) and 206(2) of the Advisers Act and Rule 204-2(a) promulgated thereunder;

D. SAM and Schultze, within 30 days of the entry of this Order, pay civil money penalties in the amounts of \$100,000 and \$50,000, respectively, to the United States Treasury. Such payments shall be: (A) made by United States postal money orders, certified checks, bank cashier's checks or bank money orders; (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 letters that identify SAM and Schultze as Respondents in these proceedings and the file number of these proceedings, copies of which cover letters and money orders or checks shall be sent to Bruce Karpati, Assistant Director,

Division of Enforcement, Securities and Exchange Commission, New York Regional Office, 3  
World Financial Center, New York, NY 10281.

E. SAM shall comply with the undertakings enumerated in paragraphs 17-18, above.

By the Commission.

Nancy M. Morris  
Secretary