

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 5345 / September 13, 2019

INVESTMENT COMPANY ACT OF 1940
Release No. 33625 / September 13, 2019

ADMINISTRATIVE PROCEEDING
File No. 3-19452

In the Matter of

GARRISON
INVESTMENT GROUP LP
and GARRISON CAPITAL
ADVISERS LLC,

Respondents.

ORDER INSTITUTING
ADMINISTRATIVE AND CEASE-AND-
DESIST PROCEEDINGS PURSUANT TO
SECTIONS 203(e) and 203(k) OF THE
INVESTMENT ADVISERS ACT OF 1940
AND SECTIONS 9(b) and 9(f) OF THE
INVESTMENT COMPANY ACT OF 1940,
MAKING FINDINGS, AND IMPOSING 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 Sections 203(e) 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 Garrison Investment Group LP (“GIG”) and Garrison Capital Advisers LLC (“GCA”) (together, “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 it and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Public Administrative and Cease-and-Desist Proceedings Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 and Sections 9(b) and 9(f) of the Investment Company Act of 1940, Making Findings, and Imposing a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds¹ that:

Summary

1. This matter concerns a series of loan transactions in which GCA's client, Garrison Capital, Inc. ("GARS"), a publicly-listed business development company, participated alongside GIG's private fund clients (the "Private Funds") and third party co-investors ("Co-Investors"). On November 21, 2012, Respondents sought relief from the Commission to allow GARS to participate in loan transaction with certain private funds managed by GIG and its affiliates. While the application and several amendments were pending, Respondents effected nine loan transactions involving the Private Funds, GARS, and Co-Investors. On December 11, 2014, Respondents submitted to the Commission their sixth amended and restated application for an order. That application, in violation of Section 34(b) of the Investment Company Act, omitted certain entities that would participate in the loan transactions from the list of applicants and did not state that GIG would receive the Co-Investors' *pro rata* share of the upfront fee revenue, per agreement with the Co-Investors. On January 12, 2015, the Commission issued an order ("Co-Invest Order")² that allowed GARS to participate in loan transactions with affiliates if Respondents complied with certain conditions. Respondents effected an additional seven loan transactions after the Co-Invest Order was issued, but did not comply with the Co-Invest Order due to the participation of the parties not listed in the application and because Co-Investors paid GIG their *pro-rata* portion of the upfront fee revenue for services performed by GIG. By effecting the nine loan transactions while the application was pending and the seven loan transactions after the Co-Invest Order was issued, Respondents, who were affiliates of GARS, violated Section 57(a)(4) of the Investment Company Act and Rule 17d-1 thereunder.

2. In addition, from at least October 2010 to April 2017, GIG violated Advisers Act Section 206(4) and Rule 206(4)-2 thereunder (the "Custody Rule") because an affiliate maintained custody of client assets without subjecting it to a surprise examination by an independent public accountant and because GIG pooled advisory client assets in a bank account with its own fee revenue.

Respondents

3. Garrison Investment Group LP is a Delaware limited partnership and New York-based investment adviser that has been registered with the Commission since 2010. GIG is affiliated with several relying advisers and GCA through which it shares management, staff, and a compliance program. As of March 29, 2019, GIG managed \$3.13 billion in assets.

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

² See Garrison Capital Inc. (File No. 812-14097), Release No. IC-31409 (January 12, 2015)(order); Release No. IC-31373 (December 15, 2014)(notice).

4. Garrison Capital Advisers LLC is a Delaware limited liability company and New York-based investment adviser that has been registered with the Commission since 2011. GCA's sole advisory client is GARS, a closed-end investment company that elected to be regulated as a business development company pursuant to Section 54(a) of the Investment Company Act. As of March 28, 2019, GCA managed \$504 million in assets.

Background

5. GIG's Private Fund clients invest in the debt securities and loans of U.S.-based companies with annual earnings before interest, taxes, depreciation, and amortization between \$5 million and \$30 million (collectively, "Commercial Loans"). GIG allocates Commercial Loan investments among the Private Funds based on the Private Funds' investment mandates and available capital according to GIG's allocation policy. When GIG's Private Fund clients do not have available capital or otherwise are not able to fully fund a Commercial Loan, GIG seeks third party co-investors to invest in the Commercial Loans.

6. With one exception, GIG structured the Co-Investors' participation in the transactions at issue through two GIG affiliates: Garrison Middle Market Funding Co-Invest LLC and Garrison Middle Market Co-Invest II LLC (collectively, the "Co-Investment Vehicles"). Prior to November 2014, the Co-investment Vehicles were wholly owned by one of the Private Funds. After November 2014, the Co-Investment Vehicles' ownership was transferred for tax-related reasons to Garrison Strategic Advisers II LLC ("GSA II"), a special purpose vehicle affiliated with GIG.

7. Rule 17d-1 of the Investment Company Act prohibits any affiliate of a registered investment company from participating with the registered investment company in or effecting any joint enterprise, other joint arrangement, or profit-sharing plan unless it first obtains an order from the Commission regarding the joint enterprise.

8. On November 21, 2012, Respondents filed an application ("Application") with the Commission for an order that would allow GARS to participate in certain Commercial Loan transactions with the Private Funds and Co-Investors ("Co-Investment Transactions"). While the application and several amendments were pending, GARS participated in nine Co-Investment Transactions.

9. In each of the Co-Investment Transactions, the corporate borrowers paid an upfront fee (sometimes also referred to by GIG as an origination fee or closing fee) that typically ranged in value from 1% to 2% of the face value of the Commercial Loan. The upfront fee was distributed *pro-rata* among the lending entities (i.e., the Private Funds, GARS, and the Co-Investors) based on the percentage each contributed to the Commercial Loan. The Private Funds and GARS each received their *pro-rata* share of the upfront fees, and the Co-Investors agreed to pay their *pro-rata* share to GIG as compensation for its work in originating, monitoring, and reporting on the Co-Investment Transactions.

Respondents Effected Prohibited Joint Transactions

10. GIG originated nine Co-Investment Transactions from December 2012 through December 2014 in which the Private Funds, GARS, and Co-Investors participated as lenders before an order was in place. GIG originated the Co-Investment Transactions and negotiated with the corporate borrowers over the terms of the Commercial Loans including the price, maturity provisions, and other financial covenants, and Respondents advised their clients to invest in the Co-Investment Transactions.

11. Respondents, by effecting transactions that involved GARS, a business development company, and advisory affiliates as joint participants, engaged in prohibited transactions.

Respondents Submitted an Application Containing Material Omissions

12. On December 11, 2014, Respondents submitted their final (sixth amended and restated) Application³ to the Division of Investment Management. The Application stated that “[a]ll existing entities that currently intend to rely upon the Order have been named as applicants.” However, the Application did not reflect the change in ownership of the Co-Investment Vehicles from the Private Funds, which were listed on the application, to GSA II, which was not. As a result, the list of entities that would participate in Co-Investment Transactions with GARS did not include the Co-Investment Vehicles. In addition, Respondents did not state in the Application that GIG would receive upfront fee revenue from the Co-Investment Transactions.

Respondents Did Not Comply with the Co-Invest Order and Continued to Engage in Prohibited Transactions

13. On January 12, 2015, the Commission issued the Co-Invest Order that allowed GIG, GCA, and the Private Funds to participate in joint transactions with GARS “on the basis of the information set forth in the application” and “subject to the conditions contained in the application.” One of the conditions for complying with the Co-Invest Order was that no advisers “will receive additional compensation or remuneration of any kind in connection with or as a result of a Co-Investment Transaction” except for advisory fees paid in accordance with the advisory agreements between the advisers and their clients.

14. In total, between January 13, 2015 and June 28, 2016, GIG originated seven Co-Investment Transactions that included participants (*i.e.*, the Co-Investment Vehicles) that were not listed in the Application (“Post-Relief Transactions”). In four of the Post-Relief Transactions, the Co-Investors agreed that GIG could receive their *pro-rata* share of the upfront fees paid by the corporate borrowers. By effecting transactions that involved GARS—a business development company—and advisory affiliates as joint participants, and by GIG receiving the *pro-rata* share of the upfront fees, Respondents did not comply with the Co-Invest Order.

³ Additional amendments were filed on February 25, 2013, August 12, 2013, January 16, 2014, and May 21, 2014.

15. In July 2016, GIG's Chief Compliance Officer identified the omission of parties from the Application and the resulting non-compliance with the Co-Invest Order and informed the GARS Board of Directors. As a result, new entities through which the Co-Investors would participate in the Co-Investment Transactions were created in order to comply with the terms of the Co-Invest Order on a go-forward basis.

GIG Failed to Comply with the Custody Rule

16. GIG maintained custody of the Private Funds' assets through Garrison Loan Agency Service LLC ("GLAS"), GIG's wholly-owned subsidiary and the administrative agent for the Co-Investment Transactions. Pursuant to GLAS's Limited Liability Company Agreement, GIG, as the sole managing member, has exclusive control of GLAS's management, operations, and activities. GIG has authority to disburse funds from GLAS's bank account. Accordingly, the Custody Rule required GIG to have an independent public accountant conduct a surprise examination of GLAS. GIG violated the Custody Rule because from when GIG first registered with the Commission in October 2010 to April 7, 2017, GIG did not engage an independent public accountant conduct a surprise examination of GLAS.

17. The Co-Investors provided funds directly to the Co-Investment Vehicles for the Co-Investment Transactions. The Co-Investment Vehicles disbursed the funds in their own name to GLAS. GLAS pooled the funds of the Co-Investors, Private Funds, and GARS in a bank account in GLAS's name and disbursed the funds to the corporate borrowers. GLAS also received principal, interest payments and fees from the corporate borrowers on behalf of the lenders and distributed them to the lenders. In addition, GIG used GLAS's bank account to hold GIG's upfront fee revenue from the Co-Investment Transactions. GIG's use of GLAS's bank account for purposes other than holding advisory clients' funds violated the Custody Rule.

Violations

18. As a result of the conduct described above, Respondents willfully⁴ violated Section 57(a) of the Investment Company Act and Rule 17d-1 thereunder. Section 57(a) of the Investment Company Act prohibits any person related to a business development company from knowingly effecting any transaction where it is a joint participant with such person. *See* Section 57(i) of the Investment Company Act (providing that Rule 17d-1 applies to Section 57(a) of the Investment Company Act.)

⁴ "Willfully," for purposes of imposing relief under Section 9(b) of the Investment Company Act and Section 203(e) of the Advisers Act "means no more than that the person charged with the duty knows what he is doing." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor "also be aware that he is violating one of the Rules or Acts." *Tager v. SEC*, 344 F.2d 5, 8 (2d Cir. 1965). The decision in *The Robare Group, Ltd. v. SEC*, which construed the term "willfully" for purposes of a differently structured statutory provision, does not alter that standard. 922 F.3d 468, 478-79 (D.C. Cir. 2019) (setting forth the showing required to establish that a person has "willfully omit[ed]" material information from a required disclosure in violation of Section 207 of the Advisers Act).

19. As a result of the conduct described above, Respondents willfully violated Section 34(b) of the Investment Company Act which makes it unlawful for any person to make any untrue or misleading statement of material fact in any registration statement, application, report, account, record, or other document filed with the Commission under the Investment Company Act, or to omit from any such document any fact necessary in order to prevent the statements made therein from being materially misleading. A violation of Section 34(b) does not require a finding of scienter. *In re Fundamental Portfolio Advisers, Inc.*, Investment Company Act Release No. 26099 (July 15, 2003) (Commission Opinion).

20. As a result of the conduct described above, GIG willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-2 thereunder, which requires that an investment adviser with custody maintain each client's funds in bank accounts containing only client funds and securities and that the client funds be verified by an independent public accountant at least once a year without prior notice to the investment adviser.

Remedial Efforts

In determining to accept the Offers, the Commission considered the remedial acts undertaken by Respondents and cooperation afforded the Commission staff.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondents' Offers.

Accordingly, pursuant to Sections 203(e) and 203(k) of the Advisers Act and Sections 9(b) and 9(f) of the Investment Company Act, it is hereby ORDERED that:

A. Respondents cease and desist from committing or causing any violations and any future violations of Sections 57(a) and 34(b) of the Investment Company Act and Rule 17d-1 thereunder, and GIG cease and desist from committing or causing any violations and any future violations of Section 206(4) of the Advisers Act and Rule 206(4)-2 thereunder.

B. Respondents are censured.

C. Respondents shall, within thirty (30) days of the entry of this Order, pay, jointly and severally, a civil money penalty in the amount of \$250,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. 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) Respondents 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 GIG and/or GCA 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 Panayiota K. Bougiamas, Assistant Regional Director, New York Regional Office, Securities and Exchange Commission, 200 Vesey Street (Brookfield Place), Suite 400, New York, NY, 10281 or such other address as the Commission staff may provide.

By the Commission.

Vanessa A. Countryman
Secretary