

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 5585 / September 18, 2020

ADMINISTRATIVE PROCEEDING
File No. 3-20030

In the Matter of

**Northern Trust Hedge Fund
Services LLC and Northern
Trust Global Fund Services
Cayman Limited,**

Respondents.

**ORDER INSTITUTING CEASE-AND-
DESIST PROCEEDINGS PURSUANT TO
SECTION 203(k) OF THE INVESTMENT
ADVISERS 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 cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Northern Trust Hedge Fund Services LLC and Northern Trust Global Fund Services Cayman Limited (“Respondents” or “Northern Trust”).

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 Cease-and-Desist Proceedings Pursuant to Section 203(k) of the Investment Advisers 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' Offer, the Commission finds¹ that:

Summary

1. These proceedings arise out of the role of Respondents, Northern Trust Hedge Fund Services LLC and Northern Trust Global Fund Services Cayman Limited (collectively, "Northern Trust" or the "Firm"), as the fund administrators for the LR Global Frontier Master Fund, Ltd. ("Master Fund") and two feeder funds, the LR Global Frontier Fund, Ltd. (offshore) and the LR Global Frontier Fund LP (onshore) (collectively, the "Frontier Funds" or "Funds").

2. Beginning in 2010, L-R Managers, LLC ("L-R Managers" or the "Manager") was the investment adviser to the Frontier Funds. Donald S. LaGuardia, Jr., through L-R Managers (collectively, the "Advisers"), defrauded the Frontier Funds and their investors, starting at least as early as 2013 through mid-2017. Among other things, the Advisers misappropriated money from the Frontier Funds and then directed that some of the misappropriated amounts be recorded as a promissory note and receivable "due from" L-R Managers to the Funds to conceal the misappropriation. The Advisers also instructed the Funds' administrators, including Northern Trust after it assumed fund administration responsibilities in 2016, that rather than expensing Frontier Fund costs when incurred, these expenses be accounted for as another receivable "due from" L-R Managers. In addition, the Advisers directed that a hypothetical gain or performance "true-up" be recorded on the Funds' books and records as a receivable due from the Advisers.

3. From approximately January 2016 through August 2017, Northern Trust performed fund administration services for the Frontier Funds pursuant to a contract with the Funds and L-R Managers. Northern Trust succeeded another fund administrator (the "Prior Fund Administrator") which calculated the Funds' NAV through December 2015. Prior to beginning to provide fund administration services, Northern Trust personnel failed to adequately escalate concerns they identified regarding LaGuardia and L-R Managers. During its engagement, Northern Trust permitted the Advisers to withdraw approximately \$211,000 from the Funds without support and followed the Adviser's instruction to account for the withdrawals as part of a receivable "due from" L-R Managers to the Funds. In addition, at the direction of the Advisers, Northern Trust personnel accounted for another receivable, the promissory note and the "true-up" as assets of the Funds despite information that should have caused them to question whether L-R Managers would be able to repay these amounts. Northern Trust provided, through a portal, monthly statements to the Funds' investors. As a result of the receivables, promissory note and "true-up," the statements that Northern Trust provided reflected materially inflated capital account balances and returns. Finally, Northern Trust did not obtain sufficient pricing support, as set forth in the valuation guidance provided in its professional services agreement, for a significant holding of the Funds that was an illiquid investment in a private company affiliated with the Manager.

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.

4. As a result of the foregoing, Northern Trust caused the Advisers' violations of Section 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder.

Respondents

5. **Northern Trust Hedge Fund Services LLC and Northern Trust Global Fund Services Cayman Limited** are indirect wholly-owned subsidiaries of Northern Trust Corporation which is a financial services company headquartered in Chicago, Illinois. Northern Trust Hedge Fund Services LLC and Northern Trust Global Fund Services Cayman Limited provided fund administration services for the Frontier Funds from approximately January 1, 2016 until August 30, 2017 when Respondents resigned their positions as fund administrator. Northern Trust was paid approximately \$15,096 during this period for its fund administration services. Beginning in approximately October 2015, Northern Trust also served as custodian to the Funds but did not receive any payment for these services.

Other Relevant Parties

6. **Donald S. LaGuardia, Jr.** LaGuardia, age 53, resides in Lavallette, New Jersey. LaGuardia was one of the founders of, and controlled, L-R Managers. He served as Chief Executive Officer and one of two Managing Principals of L-R Managers which, beginning in approximately 2010, was the investment adviser to the Frontier Funds. LaGuardia was also a portfolio manager of the Frontier Funds. On June 24, 2019, the Commission filed a civil injunctive action against LaGuardia in the United States District Court for the Southern District of New York alleging securities fraud violations relating to the Funds.

7. **L-R Managers or the Manager.** Beginning in approximately 2010, L-R Managers was the investment adviser to, among other clients, the Frontier Funds. The Manager was not registered as an investment adviser with the Commission or a State. L-R Managers had its principal place of business at 430 Park Ave., New York, New York. On June 7, 2017, L-R Managers filed for Chapter 7 bankruptcy protection in the U.S. Bankruptcy Court for the Southern District of New York.

8. **The Frontier Funds or Funds.** Launched in approximately 2010, the Frontier Funds were structured as a Master Fund with two feeder funds. During the time of Northern Trust's administration, the Funds never purported to have had more than \$3 million in assets under management.

FACTS

Background

9. From January 2016 through August 2017, Northern Trust served as fund administrator for the Frontier Funds. Pursuant to its contract to provide fund administration services, Northern Trust agreed to, among other things, calculate monthly NAVs and prepare monthly financial statements for the Funds and to produce and distribute periodic reporting of account balances to investors. The Firm also provided pricing and valuation verification services to the Funds pursuant to guidelines agreed to with L-R Managers. Northern Trust calculated the monthly NAV of the Frontier Funds for January 2016 through September 2016. Through the online portal, for the same months, Northern Trust provided investors with monthly capital account statements reflecting the purported value and investment returns generated in their accounts.

Northern Trust Personnel Failed to Adequately Escalate Concerns Regarding the Advisers Before Beginning to Provide Fund Administration Services to the Frontier Funds

10. In May 2015, the Manager selected Northern Trust to assume administration of the Frontier Funds from the Prior Fund Administrator. Northern Trust's due diligence process occurred between approximately August and December of 2015. During this period, Northern Trust failed to identify a civil action filed by an investor in August 2015 against L-R Managers, LaGuardia and others, which included allegations that he had been defrauded.

11. Between approximately August 2015 and December 2015, Northern Trust was "onboarding" the Funds – that is, transitioning the Funds' records to Northern Trust and learning about the Advisers, the Funds and their assets before Northern Trust began to provide fund administrative services. During the onboarding process, Northern Trust communicated with the Prior Fund Administrator regarding the Funds' financials, among other things. During this period, certain Northern Trust personnel learned that L-R Managers had cash flow issues, that L-R Managers had transferred money from the Frontier Funds to the Manager and accounted for those transfers as a promissory note and receivable, that this promissory note was not repaid on time, that payments purportedly related to the Funds' expenses had also been booked as a receivable "due from" the Manager and that one of the Funds' significant holdings was a private entity which was affiliated with L-R Managers. During this time, Northern Trust employees also questioned whether L-R Managers possessed sufficient assets to meet its current liabilities.

12. Employees also became aware that although the Private Placement Memoranda for the Frontier Funds stated that an independent firm had been retained to audit the Funds and that investors in the feeder funds would receive audited financial statements, the Frontier Funds had not, in fact, been audited in spite of the fact that the Funds were "live for ~3yrs." Instead, as reflected in an internal email, it appears that Northern Trust accepted the Manager's representation that they intended to "do an audit for the first time (presumably inception to date) now that they have/are getting more external money."

Northern Trust's Conduct as Fund Administrator

13. Beginning in January 2016, Northern Trust began to provide fund administration services for the Frontier Funds. Once Northern Trust began as fund administrator, there were no additional investor subscriptions into the Funds. Starting in October 2015, Northern Trust also assumed custodial responsibilities when the Funds' prior custodian began delivering the Funds' assets, including the purported promissory note, to the Firm. With respect to the custody of the assets, the Firm has retained custody of the assets of the Frontier Funds during the pendency of the investigation.

14. From January 2016 through March 2017, the Advisers misappropriated approximately \$211,000 from the Frontier Funds mostly pursuant to "Letters of Authorization" which contained no support for the withdrawals. The majority of this money was transferred within the first few months after Northern Trust began providing fund administration services. The Advisers instructed Northern Trust to add these outgoing funds to a large receivable that already existed as "due from" L-R Managers to the Funds on the Funds' accounting records from the Prior Fund Administrator. In response to an inquiry from a Northern Trust employee about money transferred from the Funds to L-R Managers, the director of operations of L-R Managers wrote, "there is no back up support. This is part of the big receivable we intend to pay back to the fund." Accounting for these withdrawals as a receivable "due from" the Manager enabled the Advisers to conceal their misappropriation of Fund assets.

15. In addition, notwithstanding that the promissory note had not been repaid upon maturity and was instead "extended" by the Advisers, Northern Trust accounted for the promissory note at face value, and accrued interest on the note for the purpose of NAV and return calculations.

16. The Manager also instructed Northern Trust not to deduct certain operating expenses related to the Funds from the Funds' profits but rather, to book them as an offsetting reimbursement due from L-R Managers on the Funds' accounting records. In an exchange during the onboarding process regarding these expenses, the L-R Managers' director of operations wrote to Northern Trust personnel: "These are booked as [...] due from L-R Managers, LLC. As the fund is in start up mode with friends/family \$\$\$, we have used the Master to fund the management co on certain expenses all the while realizing we need to repay these funds" Again, without questioning whether L-R Managers could, in fact, "repay these funds," Northern Trust simply followed L-R Managers' instruction to book the operating expenses as an offsetting reimbursement. As of September 30, 2016, this Fund expense receivable had grown to approximately \$830,000, artificially inflating the NAV of the Funds.

17. Also, beginning with the January 2016 NAV calculations, Northern Trust carried out instructions from the Advisers to increase the Funds' monthly income by the amount of a hypothetical performance gain or "true-up" reflecting the estimated performance of previous investments of the Funds. The Manager represented to Northern Trust that these holdings had been liquidated during the conversion to Northern Trust's platform and had not been reinvested, but that the Manager purportedly wanted to "reimburse" the investors for any gains they would have received had the investments been retained. Northern Trust was instructed to record these

hypothetical gains as a receivable “due from” L-R Managers. Northern Trust carried out the Advisers’ instruction to record the receivable without performing an analysis of the basis for the “true-up” or whether it would be appropriate to account for such amounts as assets of the Funds. As of September 30, 2016, the cumulative effect of the performance “true-up” artificially inflated the NAV reported to the Funds’ investors by approximately \$347,000.

18. In addition, Northern Trust included the promissory note and interest in its calculations of investors’ capital account balances and returns for the months of June, July, August and September 2016 even though Northern Trust knew at the time that the promissory note had matured but had not been repaid or extended. In May 2017, the Advisers asked Northern Trust to write off the note.

19. Northern Trust’s accounting policies and procedures did not require its employees to conduct an assessment of whether the promissory note, receivables and “true-up” were collectible before booking those amounts as assets of the Funds. Northern Trust calculated that in total, as of September 30, 2016, the amount “due from” L-R Managers to the Funds had grown to nearly \$2 million, which was approximately 73% of the purported value of the Funds’ NAV. By accepting the Advisers’ instructions to include the promissory note, receivables and “true-up” as assets of the Funds, Northern Trust provided investors with monthly statements that reflected materially inflated capital account balances and returns.

20. Further, Northern Trust did not obtain sufficient support for the valuation of a significant Manager-priced holding of the Funds, an illiquid investment in a private company affiliated with the Manager. In accordance with its valuation guidelines, Northern Trust should have received support for any Manager-priced security. Instead, Northern Trust accepted the Manager’s valuation of this holding without substantiation. Northern Trust subsequently wrote the value of this holding down to zero.

Northern Trust’s Remediation

21. Beginning in May 2017, following the Advisers’ request to write-off the promissory note, Northern Trust undertook a review of the Frontier Funds. In August 2017, Northern Trust contacted the Commission staff to report concerns about the conduct of the Advisers, including with respect to fund accounting and valuation. Subsequently, and in part as a result of those concerns, Northern Trust has implemented a number of changes to its fund administration policies, procedures and controls, including: developing a written due diligence protocol for new fund launches and conversions, creating a revised pricing verification protocol, establishing independent monitoring mechanisms to review the accounting treatment of non-investment assets, increasing compliance oversight and risk management, including through additional professional training related to fraud detection, and added testing related to the efficacy of its amended policies, procedures and controls.

Violations

22. Under Section 203(k) of the Advisers Act, the Commission may impose a cease-and-desist order upon, among others, any person that is, was, or would be a cause of another's violation, due to an act or omission the person knew or should have known would contribute to such violation of any provision of the Advisers Act.

23. Section 206(2) of the Advisers Act prohibits investment advisers from directly or indirectly engaging "in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." A violation of Section 206(2) of the Advisers Act may rest on a finding of simple negligence. *SEC v. Steadman*, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963)). Proof of scienter is not required to establish a violation of Section 206(2) of the Advisers Act. *Id.*

24. Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder make it unlawful for any investment adviser to a pooled investment vehicle to "[m]ake any untrue statement of a material fact or omit 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" or "engage in any act, practice, or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle."

25. The Advisers violated Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder, by making unauthorized and undisclosed withdrawals from the Funds, by concealing those withdrawals as receivables and a promissory note, by directing that fund expenses be recorded as a receivable and by directing the recording of a performance "true up." The Advisers did not disclose to the Funds or investors that one of the Funds' investments was an affiliated company for which the Advisers provided the valuation to the fund administrator.

26. As a result of the conduct described above, Northern Trust was a cause of the Advisers' violations of Sections 206(2) and 206(4) of the Advisers Act, and Rule 206(4)-8 thereunder.

Northern Trust's Cooperation

27. In determining to accept the Offer, the Commission considered the remedial acts undertaken by Northern Trust and the cooperation afforded the staff of the Commission.

IV.

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

Accordingly, pursuant to Section 203(k) of the Advisers Act, it is hereby ORDERED that:

- A. Respondents cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder;
- B. Respondent Northern Trust Hedge Fund Services LLC shall, within ten (10) days of the entry of this Order pay disgorgement of \$15,076 with prejudgment interest of \$2,553 and Respondents shall, jointly and severally, pay a civil money penalty in the amount of \$150,000 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600 and 31 U.S.C. §3717.

C. Payment shall 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 Northern Trust Hedge Fund Services LLC and Northern Trust Global Fund Services Cayman Limited as the Respondents in these proceedings, and the file number of these proceedings, a copy of which cover letter and check or money order must be sent to Sanjay Wadhwa, Senior Associate Director, Division of Enforcement, Securities and Exchange Commission, New York Regional Office, 200 Vesey Street, Suite 400, New York, NY 10281.

D. Pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, a Fair Fund is created for the disgorgement, prejudgment interest and penalties referenced in paragraph IV.B. above. 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, Respondents agree that in any Related Investor Action, they shall not argue that they are entitled to, nor shall they benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondents' payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondents agree that they 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 Securities and Exchange Commission. 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 Respondents 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.

Vanessa A. Countryman
Secretary