

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 5586 / September 21, 2020

INVESTMENT COMPANY ACT OF 1940
Release No. 34017 / September 21, 2020

ADMINISTRATIVE PROCEEDING
File No. 3-20039

In the Matter of

**PALMER SQUARE
CAPITAL MANAGEMENT
LLC,**

Respondent.

**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
REMEDIAL SANCTIONS AND A
CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that 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 Palmer Square Capital Management LLC (“Palmer Square” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has 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 it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this 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 Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent’s Offer, the Commission finds that:

Summary

From at least July 2014 through September 2016 (the “Relevant Period”), Palmer Square, a registered investment adviser, cross traded securities between approximately forty client accounts that it advised. Palmer Square prearranged buys and sells of the same security in the same amount from one client account to another 351 times during this period. When effecting almost all of these trades, Palmer Square failed to comply with the statutory provisions regarding unlawful cross trades with Registered Investment Companies (“RICs”). In addition, certain trades were principal transactions made without the required disclosures and consent. Palmer Square’s violations were caused in part by its failure to adopt and implement adequate policies and procedures to prevent unlawful cross and principal trading effectuated by its trading personnel. Based on this conduct, Palmer Square violated Sections 206(3) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, and caused violations of Sections 17(a)(1) and 17(a)(2) of the Investment Company Act and Rule 38a-1 thereunder.

Respondent

1. Palmer Square Capital Management, LLC is a Delaware registered limited liability company with its principal place of business in Mission Woods, Kansas. Palmer Square registered with the Commission as an investment adviser on January 3, 2011. During the Relevant Period, Palmer Square provided discretionary investment advisory services to five RICs (collectively, the “Palmer Square Funds”), several private funds and collateralized loan obligation (“CLO”) vehicles, and numerous separately managed accounts of institutions and high net worth individuals. As of June 2020, Palmer Square reported approximately \$10.2 billion in assets under management.

Palmer Square Engaged In Prohibited Cross Trades and Principal Transactions

2. From July 2014 through September 2016, Palmer Square effected 351 cross trades between its client accounts. Through an independent broker-dealer, Palmer Square would sell a security from one client account it managed to another Palmer Square client account. The trades were always prearranged. The Palmer Square client on the purchasing side of the cross trade always paid a markup, which was retained by the executing broker-dealer, on the sale price of the security. The trades occurred among all types of clients advised by Palmer Square. Thirteen of these trades were principal transactions.

3. During the Relevant Period, Palmer Square effected these cross trades in instances where it decided to sell a security in the ordinary course, for example, to meet a redemption request or to otherwise conform to a client’s investment objective. When Palmer Square believed that the

securities it sold on behalf of these clients were good investments, it sought to move them through cross trades into other client portfolios. By engaging in cross trades, Palmer Square believed it was saving its clients market and transaction costs. Palmer Square effected the cross trades by arranging a simultaneous buy and sell of the same security between client accounts through an independent broker-dealer. In many cases, Palmer Square traders would refer to the trades as cross trades in their communications with the broker-dealers.

4. Internal cross trades can benefit clients because the practice enables a manager to move securities among client accounts without having to expose the security to the market, thereby saving transaction and market costs that would otherwise be paid to executing broker-dealers. However, these transactions also pose substantial risks to registered-fund clients due to the inherent conflict of interest for the adviser, which has a fiduciary duty of loyalty to its clients and also must seek to obtain best execution for both its buying and selling clients. To guard against potential concerns that affiliated persons of a RIC may engage in self-dealing transactions with the fund, Sections 17(a)(1) and 17(a)(2) of the Investment Company Act generally prohibit any affiliated person of a RIC, or any affiliated person of such affiliated person, acting as principal, from knowingly selling a security to, or purchasing a security from, the investment company unless the person first obtains an exemptive order from the Commission pursuant to Section 17(b) of the Investment Company Act. The interpositioning of a dealer in these transactions does not remove them from the prohibitions of Section 17(a). *See* Section 48(a) of the Investment Company Act; Exemption of Certain Purchase or Sale Transactions Between a Registered Investment Company and Certain Affiliated Persons Thereof, IC Rel. No. 11136, 1980 WL 29973, Note 10 (Apr. 21, 1980) (the “17a-7 Release”).

5. Rule 17a-7 under the Investment Company Act exempts from the prohibitions of Section 17(a) certain purchases and sales between RICs and certain affiliated persons, where the affiliation arises solely because the two have a common investment adviser, common directors, and/or common officers, provided that the transactions are effected in accordance with the requirements set forth in Rule 17a-7. Among those requirements is that the adviser execute the cross trade at “the average of the highest current independent bid and lowest current independent offer, determined on the basis of reasonable inquiry.” Rule 17a-7(b)(4). In addition, if the adviser causes a client to pay a brokerage commission, fee, or other remuneration in connection with the cross trade, the transaction is not eligible for the exemption. *See* Rule 17a-7(d). Moreover, the board of directors of the investment company must determine at least quarterly that these trades were effected in compliance with Rule 17a-7. *See* Rule 17a-7(e)(3).

6. Section 206(3) of the Advisers Act generally prohibits principal transactions, requiring that an investment adviser provide written disclosure to, and obtain consent from, affected clients.

7. Palmer Square did not seek exemptive relief, nor did it comply with the requirements of Rule 17a-7 for any of the cross trades involving RICs. Specifically, Palmer Square did not engage in a process to determine, on the basis of reasonable inquiry, the average of the highest current independent bid and lowest current independent offer as required by Rule 17a-7. It also caused clients to pay a brokerage commission, fee, or other remuneration in connection

with the cross trades. In addition the board of directors of the registered investment company did not, at least quarterly, determine that the cross trades were effected in compliance with Rule 17a-7.

8. Palmer Square incorrectly believed that it did not need to comply with the requirements of Rule 17a-7 if the cross trades were executed through an independent broker-dealer. Prior to engaging in the cross trades, Palmer Square consulted its fund administrator about potential cross trades. The administrator requested that Palmer Square advise it in advance before engaging in any cross trades to ensure the trades were permitted under the Investment Company Act. Based on the consultation, Palmer Square inaccurately believed that the transactions at issue were not cross trades for purposes of Rule 17a-7, and therefore the requirements of Rule 17a-7 were not applicable. As Palmer Square believed the prearranged trades were not cross trades, Palmer Square did not provide the administrator advance notice of the trades.

9. Palmer Square sought to effect cross trades at a market price that it believed was fair to both clients, but it did not engage in a process whereby it determined, on the basis of reasonable inquiry, the average of the highest current independent bid and lowest current independent offer as required by Rule 17a-7. Palmer Square typically provided prices for the cross trades to the brokers, which it arrived at in various ways. For example, certain transactions were effected at prices informed by the prices of comparable securities or single broker quotes. For certain of the cross trades at issue, Palmer Square did not retain contemporaneous documentation showing how the prices for the cross trades were set.

10. For each cross trade, Palmer Square paid a markup to the broker, which the purchasing account paid. Collectively, the broker mark-ups for the 351 cross trades totaled \$242,193.

11. In addition, Palmer Square did not supply written prior disclosure to, or receive consent from, clients who were parties to principal transactions.

Palmer Square's Policies and Procedures Were Inadequate to Detect and Prevent Its Violations

12. Palmer Square did not adopt and implement policies and procedures that were reasonably designed to prevent violations of the federal securities laws and Commission rules governing cross trading. Palmer Square personnel did not receive training on cross trades or Rule 17a-7.

13. The Palmer Square compliance manual in effect at the time of the conduct was largely silent regarding cross trades and stated that Palmer Square may do cross trades "when permitted." The Palmer Square compliance manual prohibited principal transactions. However, Palmer Square did not have policies, procedures, or controls in place to identify or monitor cross trades or principal transactions.

14. The compliance policies applicable to the Palmer Square Funds allowed cross trades as long as the requirements of 17a-7 were followed and the trades were reported to, and approved by, the board of directors for the Palmer Square Funds. However, Palmer Square failed to adequately implement these policies. Palmer Square inaccurately informed the board each quarter that it had not engaged in any cross trades. Palmer Square also did not ensure that the trades complied with other requirements of Rule 17a-7.

15. Because Palmer Square did not adequately train its employees, those employees failed to understand the requirements surrounding cross trades and principal transactions. Palmer Square's efforts at compliance did not extend past a consultation with its fund administrator. As a result, Palmer Square failed to take sufficient action to ensure compliance with Rule 17a-7 and Section 206(3).

Violations

16. As a result of the conduct described above, Palmer Square caused certain Palmer Square advisory account clients to violate Sections 17(a)(1) and 17(a)(2) of the Investment Company Act, which make it unlawful for any affiliated person or promoter of or principal underwriter for a RIC or any affiliated person of such a person, promoter, or principal underwriter, acting as principal (1) knowingly to sell any security or other property to such RIC or to any company controlled by such RIC, or (2) knowingly to purchase from such RIC, or from any company controlled by such RIC, any security or other property, unless the transaction complies with the exemptive requirements of Rule 17a-7 under the Investment Company Act, or the adviser obtains an exemptive order under Section 17(b) of the Investment Company Act. Palmer Square did not seek an exemptive order for any cross transaction, and the transactions were not exempt from the prohibition by virtue of Rule 17a-7, because Palmer Square did not engage in a process whereby it determined, on the basis of reasonable inquiry, the average of the highest independent bid and lowest independent offer as required by Rule 17a-7; were made through one or more broker-dealers who received remuneration in connection with the transactions; and the cross transactions were not determined to have been effected in compliance with Rule 17a-7 by the board of directors of the RICs.

17. As a result of the conduct described above, Palmer Square willfully violated Section 206(3) of the Advisers Act, which prohibits an investment adviser, acting as principal for its own account, from knowingly selling securities to or purchasing securities from the adviser's clients without disclosing to such clients in writing before the completion of such transactions in the capacity in which the adviser is acting and obtaining the consent of the clients to such transactions¹. Here, trades occurred between private funds advised by Palmer Square in which

¹ "Willfully," for purposes of imposing relief under Section 203(e) of the Advisers Act and Section 9(b) of the Investment Company 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

Palmer Square controlling persons owned more than twenty-five percent of the private funds, and other non-RIC advisory clients. Therefore, Palmer Square was acting as principal for trades involving those private funds. However, Palmer Square did not provide prior notification or obtain prior consent from the other advisory clients and, therefore, violated Section 206(3) of the Advisers Act.

18. As a result of the conduct described above, Palmer Square willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, which require, among other things, that registered investment advisers adopt and implement written policies and procedures reasonably designed to prevent violations, by the investment adviser and its supervised persons, of the Advisers Act and rules.

19. As a result of the conduct described above, Palmer Square caused the Palmer Square Funds to violate Rule 38a-1, which requires a registered investment company to adopt and implement written policies and procedures reasonably designed to prevent violations of the federal securities laws.

Palmer Square's Remedial Efforts and Cooperation

20. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Palmer Square and cooperation afforded the Commission staff. When Palmer Square became aware of its responsibilities relating to cross trades during an examination conducted by the Commission's Office of Compliance Inspections and Examinations, it implemented remedial measures. These measures included cessation of all cross trading, notifying the boards of each affected Palmer Square Fund and CLO client, obtaining board ratification of the cross trades involving the Palmer Square Funds or CLOs, hiring an in-house chief compliance officer, updating compliance policies, and repaying broker markups to affected clients for trades involving the RICs.

21. Palmer Square also retained new outside counsel with expertise in the Investment Company Act and Advisers Act, had counsel perform a detailed internal assessment, and then shared the results of that assessment with the Commission.

IV.

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

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[ted]" material information from a required disclosure in violation of Section 207 of the Advisers Act).

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

A. Palmer Square cease and desist from committing or causing any violations and any future violations of Section 17(a)(1) and 17(a)(2) of the Investment Company Act and Rule 38a-1 thereunder, and Sections 206(3), and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

B. Palmer Square is censured.

C. Palmer Square shall, within thirty (30) days of the entry of this Order, pay a civil money penalty in the amount of \$450,000 to the Securities and Exchange Commission. 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) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent 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 Palmer Square as a Respondent 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 Laura Metcalfe, Assistant Regional Director, Denver Regional Office, Securities and Exchange Commission, 1961 Stout Street, Suite 1700, Denver, Colorado 80294-1961.

D. 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, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it 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 Respondent 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