

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 5009 / September 14, 2018

ADMINISTRATIVE PROCEEDING
File No. 3-18765

In the Matter of

CAPITAL ANALYSTS, 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, 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 Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Capital Analysts, LLC (“CA” 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, 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 finds¹ that:

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

SUMMARY

1. These proceedings arise from disclosure failures by Capital Analysts, LLC, a registered investment adviser, in connection with its mutual fund share class selection practices and receipt of revenue sharing payments. First, from April 2013 through March 2016 (the “Relevant 12b-1 Period”), CA invested certain advisory clients in mutual fund share classes with 12b-1 fees instead of available lower-cost share classes of the same funds without 12b-1 fees. CA’s affiliated broker-dealer, Lincoln Investment Planning, LLC (“Lincoln”), received the 12b-1 fees based on these investments. CA did not adequately disclose this conflict of interest in its Forms ADV or otherwise. CA also breached its duty to seek best execution for its clients by investing them in mutual fund share classes with 12b-1 fees rather than lower-cost share classes. During the Relevant 12b-1 Period, Lincoln received \$936,181 in 12b-1 fees as a result of CA investing clients in mutual fund share classes with 12b-1 fees instead of lower-cost share classes of the same funds without 12b-1 fees.

2. Second, from April 2013 through March 2017 (the “Relevant Revenue Sharing Period”), CA failed to adequately disclose to its clients compensation that Lincoln received through an agreement with a third-party clearing broker (“Clearing Broker”) and conflicts arising from that compensation. The Clearing Broker agreed to share with Lincoln shareholder service fee revenues that the Clearing Broker received when CA invested its advisory clients in certain no-transaction fee mutual funds that did not pay 12b-1 fees. These payments, totaling \$691,125, created a conflict of interest in that they provided a financial incentive for CA to favor certain mutual funds in the Clearing Broker’s no-transaction fee mutual fund program (“NTF Program”) over other investments when giving investment advice to its advisory clients.

3. Finally, CA failed to adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder in connection with its mutual fund share class selection practices.

4. As a result of the conduct described above, CA willfully violated Sections 206(2), 206(4) and 207 of the Advisers Act and Rule 206(4)-7 thereunder.

RESPONDENT

5. **Capital Analysts, LLC (“CA”)**, a Pennsylvania limited liability company based in Fort Washington, Pennsylvania, has been registered with the Commission as an investment adviser since 2012. On its Form ADV dated March 29, 2018, CA reported that it had approximately \$4.75 billion in regulatory assets under management. CA is a wholly-owned subsidiary of Lincoln Investment Capital Holdings, LLC, a Delaware limited liability company.

RELATED PARTY

6. **Lincoln Investment Planning, LLC (“Lincoln”)**, a Pennsylvania limited liability company based in Fort Washington, Pennsylvania, has been registered with the Commission as a broker-dealer since 1969. Lincoln also is a wholly-owned subsidiary of Lincoln Investment Capital Holdings, LLC, and is affiliated with CA through common ownership and control.

Throughout the Relevant 12b-1 and Revenue Sharing Periods, Lincoln acted as the introducing broker-dealer for CA's advisory clients.

FACTS

7. CA offered asset management services to its advisory clients through various programs, including wrap fee programs exclusively managed on a discretionary basis by CA's Investment Management & Research team, in which clients paid an all-inclusive fee for asset management and trade execution ("CAAMS Wrap Fee Programs").

Mutual Fund Share Class Selection

8. Mutual funds typically offer investors different types of shares or "classes." Each share class represents an interest in the same portfolio of securities with the same investment objective. The primary difference among the various share classes is their fee structure.

9. Class A shares were one of the more common mutual fund share classes that CA purchased for advisory clients in its CAAMS Wrap Fee Programs during the Relevant 12b-1 Period. Class A shares typically are purchased by retail brokerage customers in brokerage accounts, but also can be purchased by retail advisory clients in advisory accounts. Class A shares are sold with sales charges or sales "loads" in retail brokerage accounts based on the dollar amount of the investment, but the sales charges are often waived by the fund company when purchased in fee-based advisory accounts. However, even these "load-waived" Class A shares continue to charge what is known as a 12b-1 fee, a fee paid by a mutual fund on an ongoing basis from its assets for shareholder services, distribution and marketing expenses.² The 12b-1 fee for Class A shares typically is 25 basis points.

10. In addition to load-waived Class A shares or equivalent "no load" fund shares,³ many mutual funds in recent years have begun to offer share classes (such as "institutional" or "advisory" share classes) that do not charge 12b-1 fees to fee-based advisory accounts. The terms and eligibility requirements for any particular share class are described in a mutual fund's prospectus.

11. When an advisory client in a fee-based program is eligible for a non-12b-1 fee share class, it generally is in the client's best interest to invest in this share class rather than a 12b-1 fee share class of the same fund because the client's returns will not be reduced by 12b-1 fees. Accordingly, where there is no credit, offset or similar adjustment for 12b-1 fees, an advisory

² 12b-1 fees are paid to the fund's distributor or underwriter, which, in turn, generally remits a portion of the fees to intermediaries that distribute or "sell" the fund's shares. Upon receipt of the 12b-1 fees, the Clearing Broker passed through to Lincoln, as introducing broker-dealer, the 12b-1 fees associated with mutual funds acquired by CA for its advisory clients.

³ Certain mutual funds known as "no load" funds, which have no front-end sales charge, may also be offered to fee-based accounts. These funds also may charge 12b-1 fees, typically up to 25 basis points.

client will benefit from higher investment returns over time by investing in the lower-fee share class.

12. From April 2013 through March 2016, CA invested certain advisory clients in its CAAMS Wrap Fee Programs in share classes with 12b-1 fees when lower-cost share classes of those same funds without 12b-1 fees were available. As a result, CA's affiliate, Lincoln, received \$936,181 in 12b-1 fees that it would not have collected had CA invested those advisory clients in available lower-cost share classes.

Revenue Sharing with the Clearing Broker

13. During the Relevant Revenue Sharing Period, the Clearing Broker offered its NTF Program to investment advisers. As part of the NTF Program, the Clearing Broker waived, for clients of participating advisers, the transaction fees it would otherwise charge for mutual fund purchases.

14. Since at least 2013, CA and its affiliate, Lincoln, participated in the Clearing Broker's NTF Program. The terms of their participation were set forth in an agreement with the Clearing Broker. Under the agreement, the Clearing Broker agreed to share with Lincoln a certain amount of shareholder service fee revenue the Clearing Broker received when CA invested its advisory clients in certain NTF Program mutual funds that did not pay a 12b-1 fee. The payments Lincoln received under the agreement created a financial incentive for CA to recommend or favor mutual funds covered by the agreement over other investments when rendering investment advice to its clients.

15. From April 2013 through March 2017, CA purchased or held, on behalf of certain advisory clients in its CAAMS Wrap Fee Programs, mutual funds that were part of the agreement, and, as a result, Lincoln received shareholder service fee payments totaling \$691,125 from the Clearing Broker.

Disclosure and Best Execution Failures

16. As an investment adviser, CA was obligated to fully disclose all material facts to its advisory clients, including conflicts of interest between itself and its advisory clients that could affect the advisory relationship. To meet this disclosure obligation, CA was required to provide its advisory clients with sufficient information so that they could understand CA's material conflicts of interest, enabling clients to give informed consent to the conflicts or reject them.

17. During the Relevant 12b-1 Period, CA disclosed in its Forms ADV that its affiliate, Lincoln, received 12b-1 fees from mutual fund investments of its clients. However, CA failed to adequately disclose that it had a conflict of interest as a result of the additional compensation Lincoln received when CA invested advisory clients in a fund's 12b-1 fee paying share class when a lower-cost share class of the same fund without 12b-1 fees was available. CA also failed to adequately disclose that it would and did select share classes paying 12b-1 fees when less expensive share classes for the same fund were available to its advisory clients. During the Relevant Revenue Sharing Period, CA also failed to adequately disclose that Lincoln received

shareholder service fee payments under the agreement with the Clearing Broker and that these payments created a conflict of interest.

18. Furthermore, Section 206 of the Advisers Act imposes on investment advisers a fiduciary duty to act for the benefit of their clients. That duty includes, among other things, an obligation to seek best execution for client transactions – *i.e.*, “to seek the most favorable terms reasonably available under the circumstances.” *In the Matter of Fidelity Management Research Company*, Advisers Act Rel. No. 2713 (Mar. 5, 2008) (settled order). The Commission has brought several settled enforcement proceedings against investment advisers for failing to seek best execution when the advisers caused clients to purchase a more expensive share class when a less expensive share class was available.⁴ By causing certain advisory clients to invest in fund share classes that charged 12b-1 fees when such clients were otherwise eligible for lower-cost share classes, and by failing to disclose to its clients that best execution might not be sought for purchases of mutual funds with multiple available share classes, CA violated its duty to seek best execution for those transactions during the Relevant 12b-1 Period.

Compliance Deficiencies

19. In addition, from April 2013 through March 2016, CA failed to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder in connection with disclosure of conflicts of interest presented by its mutual fund share class selection practices.

VIOLATIONS

20. As a result of the conduct described above, CA willfully⁵ violated Section 206(2) of the Advisers Act, which prohibits an investment adviser, directly or indirectly, from 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) may rest on a finding of simple negligence. *SEC v. Steadman*, 967 F.2d 636, 643n.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.*

21. As a result of the conduct described above, CA willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, which require a registered investment adviser to

⁴ See, e.g., *In the Matter of SunTrust Investment Services, Inc.*, Advisers Act Rel. No. 4769 (Sept. 14, 2017) (settled order) (collecting cases).

⁵ A willful violation of the securities laws means merely “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.” *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder.

22. As a result of the conduct described above, CA willfully violated Section 207 of the Advisers Act, which makes it “unlawful for any person willfully to make any untrue statement of a material fact in any registration application or report filed with the Commission . . . or willfully to omit to state in any such application or report any material fact which is required to be stated therein.”

REMEDIAL EFFORTS

23. In determining to accept the Offer, the Commission considered remedial acts taken by Respondent and cooperation afforded by it to the Commission staff. Beginning in March 2016, CA began to invest CAAMS Wrap Fee Program clients in the lowest-cost share class available for the same fund on the Clearing Broker’s platform, subject to eligibility restrictions imposed by the funds. At the same time, CA initiated the process of converting existing mutual fund investments in Class A shares (or comparable classes) held by CAAMS Wrap Fee Program clients to the lowest-cost share classes available for the same funds on the Clearing Broker’s platform, subject to eligibility restrictions imposed by the funds.

IV.

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

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

A. Respondent shall cease and desist from committing or causing any violations and any future violations of Sections 206(2), 206(4) and 207 of the Advisers Act and Rule 206(4)-7 promulgated thereunder.

B. Respondent is censured.

C. Respondent shall pay disgorgement and prejudgment interest, totaling \$1,049,873, to compensate past and present advisory clients that were affected by the 12b-1-fee-related conduct detailed in this Order, as follows:

(i) Respondent shall pay disgorgement of \$936,181 and prejudgment interest of \$113,692, consistent with the provisions of this Subsection C.

(ii) Within ten (10) days of the entry of this Order, Respondent shall deposit \$1,049,873, (the “Distribution Fund”) into an escrow account at a financial institution not unacceptable to the Commission staff and Respondent shall provide the Commission staff with evidence of such deposit in a form acceptable to the Commission staff. If timely payment into the escrow account is not made,

additional interest shall accrue pursuant to SEC Rule of Practice 600 [17 C.F.R. § 201.600].

- (iii) Respondent shall be responsible for administering the Distribution Fund and may hire a professional to assist it in the administration of the distribution. The costs and expenses of administering the Distribution Fund, including any such professional services, shall be borne by Respondent and shall not be paid out of the Distribution Fund. Respondent shall distribute the amount of the Distribution Fund to the applicable past and present advisory clients in Respondent's CAAMS Wrap Fee Programs, who from April 2013 through March 2016 incurred 12b-1 fees on investments in mutual fund share classes where Respondent could have invested such clients in mutual fund share classes of the same funds without 12b-1 fees, pursuant to a disbursement calculation (the "Calculation") that will be submitted to, reviewed, and approved by the Commission staff in accordance with this Subsection C. The Calculation shall be subject to a *de minimis* threshold, as described in Paragraph iv below. No portion of the Distribution Fund shall be paid to any affected advisory client account in which Respondent, or any of its past or present officers or directors, has a financial interest.
- (iv) Respondent shall, within sixty (60) days of the entry of this Order, submit a proposed Calculation to the staff for its review and approval that identifies, at a minimum, (1) the name of each affected past or present advisory client account, (2) the exact amount of the payment to be made from the Distribution Fund to each affected past or present advisory client account, and (3) the amount of any *de minimis* threshold to be applied. Respondent shall also provide to the Commission staff such additional information and supporting documentation as the Commission staff may request for the purpose of its review. At or around the time of submission of the proposed Calculation to the staff, Respondent, along with any third parties or professionals retained by Respondent to assist in formulating the methodology for its Calculation and/or administration of the Distribution, shall make themselves available for a conference call with the Commission staff to explain the methodology used in preparing the proposed Calculation and its implementation, and to provide the staff with an opportunity to ask questions. In the event of one or more objections by the Commission staff to Respondent's proposed Calculation or any of its information or supporting documentation, Respondent shall submit a revised Calculation for the review and approval of the Commission staff or additional information or supporting documentation within ten (10) days of the date that Respondent is notified of the objection, which revised Calculation shall be subject to all of the provisions of this Subsection C.
- (v) After the Calculation has been approved by the Commission staff, Respondent shall submit a payment file (the "Payment File") for review and acceptance by the Commission staff demonstrating the application of the methodology to each affected past or present advisory client account. The Payment File should identify, at a

minimum, (i) the name of each affected harmed investor; (ii) the exact amount of the payment to be made; and (iii) the amount of any *de minimis* threshold to be applied.

- (vi) Respondent shall complete the disbursement of all amounts payable to affected past or present advisory client accounts within ninety (90) days of the date that the Commission staff accepts the Payment File, unless such time period is extended as provided in Paragraph x of this Subsection C.
- (vii) If Respondent is unable to distribute any portion of the Distribution Fund for any reason, including an inability to locate an affected past or present advisory client or a beneficial owner of an affected past or present advisory client account or any factors beyond Respondent's control, Respondent shall transfer any such undistributed funds to the Commission for transmittal to the United States Treasury in accordance with Section 21F(g)(3) of the Securities Exchange Act of 1934 when the distribution of funds is complete and before the final accounting provided for in Paragraph ix of this Subsection C is submitted to the Commission staff. 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 Capital Analysts, LLC as the 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 Brendan P. McGlynn, Assistant Regional Director, Asset Management Unit, Philadelphia Regional Office, Securities and Exchange Commission, 1617 JFK Blvd., Suite 520, Philadelphia, PA 19103.

- (viii) The Distribution Fund is a Qualified Settlement Fund ("QSF") under Section 468B(g) of the Internal Revenue Code [26 U.S.C. §§ 1.468B.1-1.468B.5].

Respondent shall be responsible for any and all tax compliance responsibilities associated with distribution of the Distribution Fund, including but not limited to tax obligations resulting from the Distribution Fund's status as a QSF and the Foreign Account Tax Compliance Act, and may retain any professional services necessary. The costs and expenses of tax compliance, including any such professional services shall be borne by Respondent and shall not be paid out of the Distribution Fund.

- (ix) Within 150 days after Respondent completes the distribution of all amounts payable to affected past or present advisory clients, Respondent shall submit to the Commission staff a final accounting and certification of the disposition of the Distribution Fund not unacceptable to the staff, which shall be in a format to be provided by the Commission staff, for Commission approval. The final accounting and certification shall include: (1) the amount paid to each past or present advisory client account; (2) the date of each payment; (3) the check number or other identifier of money transferred to each account; (4) the amount of any returned payment and the date received; (5) a description of any effort to locate a prospective payee whose payment was returned or to whom payment was not made for any reason; (6) the total amount, if any, to be forwarded to the Commission for transfer to the United States Treasury; and (7) an affirmation that Respondent has made payments from the Distribution Fund to affected past or present advisory clients in accordance with the distribution plan approved by the Commission staff. Respondent shall submit the final accounting and certification, together with proof and supporting documentation of such payment in a form acceptable to Commission staff, under a cover letter that identifies Capital Analysts, LLC as the Respondent in these proceedings and the file number of these proceedings to Brendan P. McGlynn, Assistant Regional Director, Asset Management Unit, Philadelphia Regional Office, Securities and Exchange Commission, 1617 JFK Blvd., Suite 520, Philadelphia, PA 19103, or such other address the Commission staff may provide. Any and all supporting documentation for the accounting and certification shall be provided to the Commission staff upon request, and Respondent shall cooperate with any additional requests by the Commission staff in connection with the accounting and certification.
- (x) The Commission staff may extend any of the procedural dates set forth in Paragraphs iv through ix of this Subsection C for good cause shown. Deadlines for dates relating to the Distribution Fund shall be counted in calendar days, except if the last day falls on a weekend or federal holiday, the next business day shall be considered the last day.

D. Respondent shall, within ten (10) days of the entry of this Order, pay, in addition to the amounts referenced in Subsection C, disgorgement of \$691,125 and prejudgment interest of \$79,351 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 SEC Rule of Practice 600 [17 C.F.R. § 201.600].

E. Respondent shall, within ten (10) days of the entry of this Order, pay a civil money penalty in the amount of \$300,000 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.

Payments referenced in Subsections D and E 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 Capital Analysts, LLC as the 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 Brendan P. McGlynn, Assistant Regional Director, Asset Management Unit, Philadelphia Regional Office, Securities and Exchange Commission, 1617 JFK Blvd., Suite 520, Philadelphia, PA 19103.

F. 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.

Brent J. Fields
Secretary