

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 92390 / July 14, 2021

INVESTMENT ADVISERS ACT OF 1940
Release No. 5776 / July 14, 2021

ADMINISTRATIVE PROCEEDING
File No. 3 - 20396

In the Matter of

**CASCADE INVESTMENT
GROUP, INC.,**

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS
PURSUANT TO SECTION 15(b) OF THE
SECURITIES EXCHANGE ACT OF 1934
AND 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 Section 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”) and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Cascade Investment Group, Inc. (“Cascade” 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 Section 15(b) of the Securities Exchange Act of 1934 and 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:

Summary

1. These proceedings arise out of breaches of fiduciary duty by Cascade, a dually registered investment adviser and broker-dealer, in connection with its mutual fund share class selection practices. From October 2014 through September 2019 (the "Relevant Period"), Cascade purchased, recommended, or held for advisory clients mutual fund share classes that charged 12b-1 fees pursuant to Rule 12b-1 under the Investment Company Act of 1940 ("12b-1 fees") instead of lower-cost share classes of the same funds that were available to the clients. Cascade and its investment adviser representatives ("IARs"), in their capacity as registered representatives of Cascade, received 12b-1 fees in connection with these investments, but Cascade did not adequately disclose this conflict of interest in its Forms ADV or otherwise. Further, by causing certain advisory clients to invest in mutual fund share classes that charged 12b-1 fees when other share classes of the same funds that presented a more favorable value for these clients under the particular circumstances in place at the time of the transactions were available to the clients, Cascade breached its duty to seek best execution for those transactions.

2. Cascade also 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.

3. Cascade, although eligible to do so, did not self-report to the Commission pursuant to the Division of Enforcement's Share Class Selection Disclosure Initiative ("SCSD Initiative").²

Respondent

4. Respondent Cascade Investment Group Inc., incorporated in Colorado and headquartered in Colorado Springs, Colorado, has been registered with the Commission as an investment adviser since 1997 and as a broker-dealer since 1994. In its Form ADV dated June 24, 2020, Cascade reported that it had approximately \$300 million in regulatory assets under management.

Mutual Fund Share Class Selection

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

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.

² See Div. of Enforcement, U.S. Sec. & Exch. Comm'n, *Share Class Selection Disclosure Initiative*, <https://www.sec.gov/enforce/announcement/scsd-initiative> (last modified Feb. 12, 2018).

6. For example, some mutual fund share classes charge 12b-1 fees to cover certain costs of fund distribution and sometimes shareholder services. These recurring fees, which are included in a mutual fund's total annual fund operating expenses, vary by share class, but typically range from 25 to 100 basis points. They are deducted from the mutual fund's assets on an ongoing basis and paid to the fund's distributor or principal underwriter, which generally remits the 12b-1 fees to the broker-dealer that distributed or sold the shares.

7. Many mutual funds also offer share classes that do not charge 12b-1 fees (*e.g.*, "Institutional Class" or "Class I" shares (collectively, "Class I shares")).³ An investor who holds Class I shares of a mutual fund will usually pay lower total annual fund operating expenses over time – and thus will generally earn higher returns – than one who holds a share class of the same fund that charges 12b-1 fees. Therefore, if a mutual fund offers a Class I share, and an investor is eligible to own it, it is often, though not always, better for the investor to purchase or hold the Class I share.

8. During the Relevant Period, Cascade purchased, recommended, or held for clients⁴ mutual fund share classes that charged 12b-1 fees when lower-cost share classes of those same funds were available to those clients. Cascade received approximately \$588,000 in 12b-1 fees during the Relevant Period that it would not have collected had Cascade's advisory clients been invested in the available lower-cost share classes. Cascade paid out 60% of the 12b-1 fee revenue to its IARs, and retained the remaining 40%.

9. In September 2019, after being contacted by Commission staff, Cascade began rebating 12b-1 fees to clients going forward. Cascade has also reimbursed to clients all 12b-1 fees that Cascade and its IARs received during the Relevant Period, plus interest.

Disclosure Failures

10. As an investment adviser, Cascade was obligated to disclose all material facts to its advisory clients, including any conflicts of interest between itself and/or its associated persons and its clients that could affect the advisory relationship and how those conflicts could affect the advice Cascade provided its clients. Relevant to the issue herein, Cascade was required to provide its advisory clients with sufficient information so they could understand the conflicts of interest of Cascade about investing in different classes of mutual funds and have an informed basis on which they can consent to or reject the conflicts.

11. During the Relevant Period, Cascade offered asset management services to its advisory clients through its Portfolio Freedom Agreement (the "PFA") whereby Cascade: (1) had discretionary authority over client accounts; (2) charged clients an asset-based advisory fee; and (3) invested assets of its advisory clients in mutual funds across numerous fund complexes. Further, Cascade entered into arrangements with its clearing broker whereby Cascade would be paid 12b-1

³ Share classes that do not charge 12b-1 fees also go by a variety of other names in the mutual fund industry, such as "Class F2," "Class Y" and "Class Z" shares. As used in this Order, the term "Class I shares" refers generically to share classes that do not charge 12b-1 fees.

⁴ In many cases, mutual funds permit certain advisory clients who hold shares in classes charging 12b-1 fees to convert those shares to Class I shares without cost or tax consequences to the client.

fees that the clearing broker received from mutual fund investments made through Cascade advisory accounts.

12. From 2014 through January 2017, Cascade disclosed in the PFA: “It is possible that [Cascade] may receive payments directly from mutual fund companies, which could cause the total fees paid to exceed the stated amounts.”

13. In February 2017, Cascade revised the PFA to incorporate the following language: “[Cascade] possibly will receive additional compensation from the receipt of 12b-1 or other service fees from mutual funds held in the Account. This practice is a conflict of interest as it provides [Cascade] an incentive to recommend mutual funds based on the additional compensation received rather than the Client needs. [Cascade] seeks to discount the management fee by the amount or more than the service fees received.”

14. During the Relevant Period, Cascade’s Forms ADV disclosed: “Additional compensation may be received by ... the receipt of 12b-1 service fees from the sale of mutual funds. This practice may present a conflict of interest and does give your registered investment advisor an incentive to recommend investment products based on the additional compensation received.”

15. Cascade did not adequately disclose all material facts regarding the conflict of interest that arose when it purchased, recommended, or held for its clients a share class that would generate 12b-1 fee revenue for Cascade while a share class of the same fund was available that would not provide Cascade with that additional compensation.

16. Further, Cascade’s revised PFA disclosure that Cascade “seeks to discount the management fee by the amount or more than” the 12b-1 fees it received was misleading because Cascade’s IARs separately negotiated advisory fees with each client, and Cascade’s IARs did not consistently discount fees by an amount equal to or more than the firm’s receipt of 12b-1 fees.

Best Execution Failures

17. An investment adviser’s fiduciary duty includes, among other things, an obligation to seek best execution for client transactions.⁵

18. By causing certain advisory clients to invest in fund share classes that charged 12b-1 fees when share classes of the same funds were available to the clients that presented a more favorable value under the particular circumstances in place at the time of the transactions, Cascade violated its duty to seek best execution for those transactions.

Compliance Deficiencies

19. During the Relevant Period, Cascade failed to adopt and to 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

⁵ See, e.g., Interpretive Release Concerning the Scope of Section 28(e) of the Securities Exchange Act of 1934 and Related Matters, Exchange Act Rel. No. 23170 (Apr. 28, 1986).

class selection practices, or in connection with making recommendations of mutual fund share classes that were in the best interests of its advisory clients.

Violations

20. As a result of the conduct described above, Respondent willfully⁶ violated Section 206(2) of the Advisers Act, which makes it unlawful for any investment adviser, directly or indirectly, to “engage in any transaction, practice or course of business which operates as a fraud or deceit upon any client or prospective client.” Scierter is not required to establish a violation of Section 206(2), but rather a violation may rest on a finding of 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. 180,194-95 (1963)).

21. As a result of the conduct described above, Respondent willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, which require a registered investment adviser to adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder.

Cascade’s Remedial Efforts

22. Although Cascade did not self-report pursuant to the SCSD Initiative even though it was eligible to do so, in determining to accept the Offer, the Commission considered other remedial acts promptly undertaken by Cascade (including reimbursement to its clients) and cooperation afforded the Commission staff.

Undertakings

23. Respondent has undertaken to:

- a. Within 45 days of the entry of this Order, review and correct as necessary all relevant disclosure documents concerning mutual fund share class selection and 12b-1 fees.
- b. Within 45 days of the entry of this Order, evaluate whether existing clients should be moved to a lower-cost share class and move clients as necessary.
- c. Within 45 days of the entry of this Order, evaluate, update (if necessary), and review for the effectiveness of their implementation, Respondent’s policies and procedures so that they are reasonably designed to prevent violations of the Advisers Act and rules thereunder in connection with disclosures regarding mutual

⁶ “Willfully,” for purposes of imposing relief under Section 15(b) of the Exchange 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[ted]” material information from a required disclosure in violation of Section 207 of the Advisers Act).

fund share class selection and in connection with making recommendations of mutual funds and mutual fund share classes that are in the best interests of Respondent's advisory clients.

d. Within 45 days of the entry of this Order, notify affected investors (*i.e.*, those former and current clients who, during the Relevant Period of inadequate disclosure, purchased or held 12b-1 fee paying share class mutual funds when a lower-cost share class of the same fund was available to the client (hereinafter, "affected investors")) of the settlement terms of this Order by sending a copy of this Order to each affected investor via mail, email, or such other method not unacceptable to the Commission staff, together with a cover letter in a form not unacceptable to the Commission staff. Cascade will also comply with all disclosure obligations under the Advisers Act concerning this Order, including providing a notification of this Order in the Item 2 "Material Changes Since Last Annual Update" section of any brochure required under Rule 204-3 of the Advisers Act.

e. Within 60 days of the entry of this Order, certify, in writing, compliance with the undertaking(s), provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The certification and supporting material shall be submitted to Ian S. Karpel, Assistant Regional Director, Denver Regional Office, Securities and Exchange Commission, Byron G. Rogers Federal Building, 1961 Stout Street, Suite 1700, Denver, CO 80294-1961, or such other address as the Commission staff may provide, with a copy to the Office of Chief Counsel of the Division of Enforcement, Securities and Exchange Commission, 100 F. Street, NE, Washington, DC 20549.

f. For good cause shown, the Commission staff may extend any of the procedural dates relating to these undertakings. Deadlines for procedural dates shall be counted in calendar days, except that if the last day falls on a weekend or federal holiday, the next business day shall be considered the last day.

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 Section 15(b) of the Exchange Act and Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

A. Respondent 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)-7 promulgated thereunder.

B. Respondent is censured.

C. Respondent shall, within ten (10) days of the entry of this Order, pay a civil money penalty in the amount of \$125,000 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) 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 Cascade 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 Ian S. Karpel, Assistant Regional Director, Denver Regional Office, Securities and Exchange Commission, Byron G. Rogers Federal Building, 1961 Stout Street, Suite 1700, Denver, CO 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.

E. Respondent shall comply with the undertakings enumerated in Paragraph 23(a)-(e) above.

By the Commission.

Vanessa A. Countryman
Secretary