

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 4764 / September 8, 2017

ADMINISTRATIVE PROCEEDING
File No. 3-18164

In the Matter of

Envoy Advisory, Inc.,

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 Envoy Advisory, Inc. (“Envoy” 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 purposes 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 Advisers Act, 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, inadequate disclosures, and compliance deficiencies by registered investment adviser Envoy. Envoy's clients are primarily small to medium sized non-profit, faith-based organizations that sponsor Employee Retirement Income Security Act of 1974 ("ERISA") Section 403(b) retirement plans for the benefit of the organizations' employees ("Plan Sponsors").² Envoy's remaining clients (approximately 13% of assets under management) are individuals that hold individual retirement accounts ("IRAs") or Roth IRAs directly with Envoy ("IRA Holders"). Envoy offers to both Plan Sponsors and IRA Holders (collectively, "Advisory Clients") a menu of mutual funds and ETFs screened and selected by Envoy ("Basic Menu").

2. From January 2013 through March 2017 (the "Relevant Period"), Envoy recommended, and plan participants and IRA Holders held, Class A mutual fund shares when less expensive institutional share classes of the same mutual funds were available. In contrast to institutional shares, Class A shares may charge investors marketing and distribution fees, typically 25 basis points per year, pursuant to Section 12(b) of the Investment Company Act of 1940 and Rule 12b-1 thereunder ("12b-1 fees"). The 12b-1 fees (also commonly known as "trail" or "trailer" fees) are paid out of the assets of the fund. Here, the 12b-1 fees paid by mutual funds held by plan participants and IRA Holders went to Envoy's affiliated broker-dealer, Envoy Securities, LLC ("Envoy Securities"). During the Relevant Period, Envoy Securities received at least \$24,893.26 in 12b-1 fees in connection with investments in higher-fee share classes by plan participants and IRA Holders.

3. Envoy's disclosures did not adequately inform its Advisory Clients of the conflict of interest presented by its recommendations to purchase Class A mutual fund shares. Envoy's Form ADV disclosures to Plan Sponsors during the Relevant Period disclosed that certain mutual funds "may" pay a "dealer" 12b-1 fees, but failed to disclose that the "dealer" receiving the 12b-1 fees was Envoy's affiliate. Envoy's Form ADV disclosures to IRA Holders during the Relevant Period failed to make any mention at all of 12b-1 fees, or the actual conflict of interest associated with its affiliated broker-dealer's receipt of those fees. In addition, Envoy's investor handbook, which was provided to IRA Holders during the Relevant Period, stated that Envoy or the account custodian "may" receive 12b-1 fees as a result of investments in certain mutual funds. Envoy's general disclosures regarding the potential receipt of 12b-1 fees were inadequate to put Advisory Clients on notice that its affiliated broker-dealer, Envoy Securities, would, and

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 These plans include Section 403(b) tax-advantaged retirement savings plans available to public education organizations, non-profits employers, cooperative hospital organizations, and self-employed ministers, and some Section 401(k) retirement savings plans.

did, receive additional compensation by Envoy recommending investments in more expensive share classes of a mutual fund.

4. In addition, during the Relevant Period Envoy failed to adopt and implement written compliance policies and procedures governing mutual fund share class selection and throughout the Relevant Period failed to implement its compliance policy and procedure regarding conflicts of interest.

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

Respondent

6. **Envoy Advisory, Inc. (“Envoy”)**, a Colorado corporation based in Colorado Springs, Colorado, has been registered as an investment adviser with the Commission since 2011. Envoy has six investment adviser representatives (“IARs”). As of March 29, 2016, Envoy reported approximately 1,800 advisory clients with approximately \$225 million in assets. Envoy is affiliated, through common ownership, with a registered broker-dealer, Envoy Securities, LLC.

Relevant Party

7. **Envoy Securities, LLC (“Envoy Securities”)**, a New Hampshire limited liability company based in Colorado Springs, Colorado, has been registered with the Commission as a broker-dealer since 2005 and is affiliated with Envoy through common ownership. Envoy’s IARs are also registered representatives of Envoy Securities. Throughout the Relevant Period, Envoy Securities acted as the broker-dealer for Envoy’s clients.

Background

8. During the Relevant Period, Envoy’s clients were primarily Plan Sponsors. Envoy’s remaining clients during the Relevant Period were IRA Holders. Envoy offered its Basic Menu (a menu of mutual funds and ETFs screened and selected by Envoy) to both Plan Sponsors and IRA Holders. While Envoy’s Investment Committee created and maintained the Basic Menu, Plan Sponsors and plan participants (in the case of 403(b) plans) and IRA Holders (in the case of separately held IRAs) retained ultimate decision-making authority for choosing the funds and ETFs for the plans and their accounts, respectively (“Basic Client Portfolio”).

Mutual Fund Share Class Selection

9. 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. The Basic Menu that Envoy explicitly recommended to Advisory Clients included a broad selection of mutual funds and ETFs across various fund complexes, which was periodically updated according to criteria applied by Envoy’s Investment Committee. In many instances, Envoy

recommended specific share classes within the funds.

10. During the Relevant Period, Envoy recommended to its Advisory Clients various iterations of the Basic Menu that included Class A shares of two funds. 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 often sold with front-end sales charges or sales “loads” in retail brokerage accounts based on the dollar amount of the investment, but the sales charges are generally waived when purchased in fee-based advisory accounts. However, even these “load-waived”³ Class A shares purchased in fee-based advisory accounts continue to pay 12b-1 fees, which are paid by a mutual fund on an ongoing basis from its assets for shareholder services, distribution, and marketing expenses.⁴ The 12b-1 fee for Class A shares is typically 25 basis points per year.

11. In addition to load-waived Class A shares or equivalent “no load” fund shares, many mutual funds in recent years have begun to offer “institutional” or “advisory” share classes, which are available only to investors who meet certain criteria (*e.g.*, minimum investment amount or eligible investment program) and do not carry 12b-1 fees.⁵ Many of these mutual funds offer institutional share classes with high minimum investment thresholds, and many such funds waive or substantially reduce that amount for purchases in fee-only advisory accounts (such as Envoy’s Basic Client Portfolio). An investor who holds institutional share classes of a mutual fund will pay lower fees over time – and earn higher investment returns – than an investor who holds Class A shares of the same fund. Therefore, if a mutual fund offers an institutional share class, and an investor is eligible to own it, it is almost invariably in the investor’s best interests to select the institutional share class.

12. During the Relevant Period, Envoy recommended Basic Menus to Advisory Clients that included Class A shares of two funds with 12b-1 fees when plan participants and IRA Holders were eligible to purchase or hold share classes without 12b-1 fees of those same funds. As a result, Envoy’s affiliated broker-dealer, Envoy Securities, received approximately \$24,893.26 in 12b-1 fees that it would not have collected had plan participants and IRA Holders been invested in lower-cost share classes for which they were eligible.

Envoy’s Inadequate Disclosures Concerning Mutual Fund Share Class Selection

13. As an investment adviser, Envoy was obligated to fully disclose, among other things, all material conflicts of interest between itself and its clients that could affect the advisory

³ Certain mutual funds known as “no load” funds can be purchased in advisory accounts but may also have 12b-1 fees. These no load funds are equivalent to “load-waived” Class A shares in advisory accounts.

⁴ 12b-1 fees are paid to the fund’s distributor or principal underwriter, which, in turn, generally remits the fees to the broker-dealer (such as Envoy Securities) that distributes or sells the fund’s shares. Here, Envoy Securities retained the 12b-1 fees.

⁵ “Institutional” shares go by a variety of names in the mutual fund industry. As used in this Order, the term refers to share classes that carry neither front-end sales charges nor 12b-1 fees.

relationship. To accomplish this disclosure obligation, Envoy was required to provide its clients with sufficient information to understand the conflicts of interest that Envoy had, enabling clients to give informed consent to such conflicts or practices or reject them.

14. Throughout the Relevant Period, Envoy filed two Forms ADV: one with respect to its Plan Sponsor advisory program related to Section 403(b) plans, and another with respect to its advisory program related to IRA Holders. During the Relevant Period, Envoy's 403(b) Forms ADV disclosed to Plan Sponsors that "funds on [Envoy's] platform have a Distribution Plan (Rule 7 12b-1 Plan) [sic] that may pay the dealer an annual distribution fee equal to 0.25% on the value of the assets." The term "dealer" is not defined in the ADV. In addition, it was not accurate that all of the funds offered had 12b-1 plans. Envoy's IRA Forms ADV filed during the Relevant Period failed to make any mention at all of 12b-1 fees or the actual conflict of interest associated with its affiliated broker-dealer's receipt of 12b-1 fees. Envoy's investor handbook, which was provided to IRA Holders, stated that Envoy or the account custodian "may" receive 12b-1 fees as a result of investments in certain mutual funds.

15. Throughout the Relevant Period, Envoy failed to adequately disclose in its Forms ADV or otherwise the conflict of interest presented by its recommendation of mutual fund share classes that charged 12b-1 fees that were paid to its affiliated broker-dealer, Envoy Securities. In addition, Envoy failed to disclose to Advisory Clients that two of the mutual funds it recommended offered a variety of share classes, including some that did not charge 12b-1 fees and were, therefore, less expensive. By omitting any mention of share class distinctions, Envoy's disclosures were inadequate, as the disclosures provided insufficient information from which a client could understand that Envoy would recommend a share class that bears a 12b-1 fee when a less costly share class of the same fund was available to the client.

Envoy's Compliance Deficiencies

16. In July 2013, Envoy adopted written compliance policies and procedures for selecting and monitoring recommended mutual funds for inclusion on the Basic Menu (the "Advisory Selection Criteria"). The Advisory Selection Criteria adopted in July 2013, however, provided no reference to how (or even if) mutual fund share class might impact this selection.

17. In September 2016, Envoy revised the Advisory Selection Criteria to require that mutual fund share classes be considered (by ranking the performance and fees of the fund based on share class) before inclusion on the Basic Menu.

18. As such, from January 2013 through August 2016, Envoy failed to adopt and implement compliance policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder in connection with its share class recommendations.

19. In addition, throughout the Relevant Period, Envoy had a written compliance policy and procedure for identifying and disclosing all actual or apparent conflicts of interest between it and its clients and disclosing or resolving those conflicts in a way that favored clients over Envoy. However, Envoy did not adequately implement this compliance policy and procedure to identify and disclose the conflict of interest arising from Envoy Securities' receipt

of 12b-1 fees when less expensive share classes were available for purchase.

Violations

20. Section 206(2) of the Advisers Act makes it unlawful for an adviser directly or indirectly to engage in any transaction, practice, or course of business that operates as a fraud or deceit upon any client or prospective client. Scienter is not required to establish a violation of Section 206(2), but rather 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)). As a result of the conduct described above, Envoy willfully⁶ violated Section 206(2).

21. Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder require a registered investment adviser to, among other things, “[a]dopt and implement written policies and procedures reasonably designed to prevent violation” of the Advisers Act and its rules. As a result of the conduct described above, Envoy willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

22. Section 207 of the Advisers Act 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.” As a result of the conduct described above, Envoy willfully violated Section 207 of the Advisers Act.

Respondent’s Remedial Efforts and Cooperation

23. In determining to accept the Offer, the Commission considered the remedial acts undertaken by the Respondent and the cooperation afforded by it to the Commission staff.

24. Beginning in October 2016, Envoy stopped recommending investments in share classes that pay 12b-1 fees and began transitioning legacy and existing advisory clients’ holdings of higher-fee share classes to institutional share classes. Envoy has also made arrangements to credit or rebate Plan Sponsors and IRA Holders with any 12b-1 fees that it may continue to receive from legacy holdings.

25. Envoy has also engaged a compliance consultant who is conducting a comprehensive review of Envoy’s written compliance policies and procedures, Forms ADV, investment advisory agreement, and disclosure documents.

26. After the Commission’s Division of Enforcement began its investigation in this matter, Envoy voluntarily began rebating the avoidable 12b-1 fees incurred during the Relevant Period. The rebates identified for processing total \$24,893.26 in avoidable 12b-1 fees. As of

⁶ 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)).

June 22, 2017, Envoy has confirmed to the Commission staff that \$2,646.82 in rebates have been sent to 50 IRA Holders through credits to client accounts and \$22,246.44 in rebates have been sent to 40 Plan Sponsors through checks ("Paid Rebates").

27. For Plan Sponsors who have not deposited or cashed a check within ninety (90) days of the check's issuance, Envoy will follow up with such clients and remind them of the outstanding checks. Funds owed to clients for whom Envoy has been unable, within 180 days after entry of this Order, to process a rebate ("Unprocessed Rebates") will be disgorged by Envoy pursuant to the terms of Section V.C. of this Order.

V.

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 thereunder.
- B. Respondent is censured.
- C. Subject to the offset provisions of Section V.D., below, Envoy shall, within two hundred (200) days after entry of this Order, pay total disgorgement of \$24,893.26 and prejudgment interest of \$2,106 to the United States 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 of disgorgement and prejudgment interest is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. 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 Envoy Advisory, Inc. 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 Jason J. Burt, Assistant Regional Director, U.S. Securities and Exchange Commission, 1961 Stout Street, Suite 1700, Denver, Colorado 80294-1961.

D. No later than two hundred (200) days following the date of this Order, Envoy will provide to the Commission staff an accounting of rebates to affected clients, the accuracy of which must be certified by the appropriate officer at Envoy (the "Accounting"). The Accounting must include: (i) the amount credited or paid to each affected client; (ii) the date of each credit or payment; (iii) the check number or other identifier of money credited or paid; (iv) the date and amount of any returned payment; and (v) the amount of all Unprocessed Rebates. If Unprocessed Rebates are processed subsequent to two hundred (200) days following the date of this Order, Envoy shall provide to the Commission staff a verified supplement to the Accounting. The amount of Paid Rebates to affected clients, prior to the lapse of one hundred and eighty (180) days following the date of this Order, as accepted by the Commission staff in writing, will dollar for dollar offset the disgorgement payable to the Commission pursuant to paragraph V.C.

E. Envoy shall, within ten (10) days after entry of this Order, pay a civil monetary penalty in the amount of \$24,893 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury in accordance with 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 Envoy Advisory, Inc. 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 Jason J. Burt, Assistant Regional Director, U.S. Securities and Exchange Commission, 1961 Stout Street, Suite 1700, Denver, Colorado 80294-1961.

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