

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 83004 / April 6, 2018

INVESTMENT ADVISERS ACT OF 1940
Release No. 4878 / April 6, 2018

ADMINISTRATIVE PROCEEDING
File No. 3-18426

In the Matter of

PNC INVESTMENTS LLC,

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 PNC Investments LLC (“PNCI” 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 improper mutual fund share class selection and billing practices by PNCI, a registered investment adviser and broker-dealer. First, from at least 2012 to 2016 (the "Relevant Period"), PNCI invested 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. PNCI financially benefitted from investing advisory clients in mutual fund share classes with 12b-1 fees, which created a conflict of interest that PNCI failed adequately to disclose in its Forms ADV or otherwise. In addition, PNCI 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 Period, PNCI received over \$5.129 million in 12b-1 fees for investing clients in higher-cost share classes.

2. Second, during the Relevant Period, PNCI received marketing support payments from three mutual fund complexes. The mutual fund complexes paid PNCI over \$497,000 in marketing support payments, which were due only when PNCI invested its advisory clients in mutual fund share classes that charged 12b-1 fees. PNCI did not receive such fees when it invested advisory clients in share classes that did not charge 12b-1 fees. PNCI never disclosed this conflict of interest in its Forms ADV or otherwise.

3. Third, during the Relevant Period, PNCI improperly charged over \$105,000 in advisory fees to client accounts whose investment adviser representative had departed the firm ("Orphaned Accounts") and for which PNCI had failed to assign a new investment adviser representative within thirty days thereafter.

4. Finally, PNCI 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 and treatment of Orphaned Accounts. As a result of this conduct, PNCI willfully violated Sections 206(2), 206(4) and 207 of the Advisers Act and Rule 206(4)-7 thereunder.

RESPONDENT

5. **PNC Investments LLC** ("PNCI"), a Delaware limited liability company, is a dual-registered broker-dealer and investment adviser with its principal place of business in Pittsburgh, Pennsylvania. PNCI has been registered with the Commission as an investment adviser and a broker-dealer since 2003. On its Form ADV dated November 8, 2017, PNCI reported that it had approximately \$14 billion in regulatory assets under management and provides investment advisory services to over 90,000 client accounts.

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.

FACTS

6. PNCI provides advisory services through certain programs, including the Capital Directions and Portfolio Solutions programs, which are wrap account programs for which PNCI is the program sponsor. In the Capital Directions program, advisory clients select from a variety of model-driven portfolios, which PNCI recommends based on clients' answers to an investor questionnaire and a consultation. In the Portfolio Solutions program, rather than using model-driven portfolios, holdings for advisory clients are managed by the clients' investment adviser representative ("IAR"). The IAR selects investments for the client from an approved list of mutual funds that PNCI maintains.

Mutual Fund Share Class Selection

7. PNCI offers its advisory clients the opportunity to invest in a broad selection of mutual funds across numerous mutual fund complexes. 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.

8. Class A shares were one of the more common mutual fund share classes that PNCI and its IARs purchased for advisory clients during 2012 to 2016. 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 generally are waived by prospectus 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.

9. 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, such as PNCI's Capital Directions and Portfolio Solutions accounts. The terms and eligibility requirements for any particular share class are described in a mutual fund's prospectus.

10. When an advisory client in a fee-based program like Capital Directions or Portfolio Solutions is eligible for a non-12b-1 fee share class, it generally is in the client's best interest to

² 12b-1 fees are paid to the fund's distributor or underwriter, which, in turn, generally remits the fees to intermediaries that distribute or "sell" the fund's shares. In its capacity as broker-dealer, PNCI received 12b-1 fees from mutual funds it sold to 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.

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.

11. From 2012 to 2016, PNCI and its IARs invested certain of its advisory clients 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, PNCI received \$5,129,340 in 12b-1 fees that it would not have collected had it invested those advisory clients in available lower-cost share classes.

Marketing Support Payments to PNCI

12. During the Relevant Period, PNCI received payments (other than 12b-1 fees) from three mutual fund complexes to support the marketing and distribution of fund shares to PNCI's advisory clients.⁴ PNCI received the marketing support payments pursuant to separate marketing support agreements ("MSAs") that it entered into with each of the three mutual fund complexes. PNCI agreed in the MSAs to provide the mutual fund complexes with fund sales data as well as certain information about PNCI and its IARs that could assist in marketing efforts.

13. Each of the MSAs specified the method for calculating the fees paid to PNCI for marketing support. Pursuant to the terms of the MSAs, the fund complexes paid fees to PNCI based either on the total assets invested by PNCI's advisory clients or the total sales of the mutual fund shares sold to PNCI's advisory clients. The MSAs specified that fees would be paid only on the share classes that charged 12b-1 fees. No MSA fees would be paid on shares that did not pay 12b-1 fees.

14. Each of the MSAs presented a conflict of interest for PNCI because each gave PNCI an additional economic incentive to sell advisory clients more expensive share classes so that PNCI could receive marketing support payments. From 2012 through 2016, PNCI received \$497,144 in marketing support payments under the terms of the three MSAs as a result of the share classes purchased or owned by its advisory clients.

Orphaned Accounts

15. PNCI advisory clients entered into investment management agreements with PNCI which provided, among other things, that the clients would pay fees in exchange for advisory services. As part of the advisory services that PNCI agreed to provide, PNCI assigned an IAR to each advisory client account.

16. During the Relevant Period, certain IARs departed from, or were terminated by, PNCI, leaving the respective advisory client accounts without an assigned IAR. During that time period, PNCI had adopted a policy that required a new IAR to be assigned to such Orphaned Accounts within thirty days of the departure or termination of the IAR originally assigned to the accounts. However, PNCI failed to establish procedures reasonably designed to ensure that Orphaned Accounts actually would be assigned a new IAR within thirty days and would not be charged an advisory fee without receiving IAR services.

⁴ The marketing support payments at issue here are paid by the fund's adviser or distributor, unlike 12b-1 fees, which are paid by the fund.

17. As a result, from 2012 through 2016, numerous PNCI Orphaned Accounts were not assigned a new IAR for periods of more than thirty days, and PNCI improperly charged these accounts \$105,516 in advisory fees.

Disclosure and Best Execution Failures

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

19. During the Relevant Period, PNCI disclosed in its Forms ADV that it received 12b-1 fees from mutual fund investments of its clients. However, PNCI did not disclose in its Forms ADV or otherwise that it had a conflict of interest concerning mutual fund share classes and that it would select share classes that charged 12b-1 fees even when its clients were eligible for lower-cost share classes of the same fund. PNCI also failed to disclose in its Forms ADV or otherwise that it had a conflict of interest due to a financial incentive to invest client assets in higher-cost share classes of mutual funds subject to the MSAs.

20. 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.⁵ 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, PNCI violated its duty to seek best execution for those transactions.

Compliance Deficiencies

21. In addition, from 2012 until 2016, PNCI 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 its mutual fund share class selection practices and treatment of Orphaned Accounts. PNCI did not adopt policies and procedures reasonably designed to ensure that advisory clients would be invested in the lowest-cost available share class of mutual funds when doing so would be in the clients' best interests. Also, PNCI failed to establish procedures

⁵ See, e.g., *In the Matter of SunTrust Investment Services, Inc.*, Advisers Act Rel. No. 4769 (Sept. 14, 2017) (settled order) (collecting cases).

reasonably designed to ensure that Orphaned Accounts would be assigned a new IAR on a timely basis and would not be charged an advisory fee without receiving IAR services.

VIOLATIONS

22. As a result of the conduct described above, PNCI willfully⁶ 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.*

23. As a result of the conduct described above, PNCI 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.

24. As a result of the conduct described above, PNCI 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

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

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 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.

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)).

B. Respondent is censured.

C. Respondent shall pay disgorgement and prejudgment interest, totaling \$5,847,200, to compensate advisory clients that were affected by the conduct detailed in Paragraphs 7 through 11 and 15 through 21 of this Order, as follows:

- (i) Respondent shall pay disgorgement of \$5,234,856 and prejudgment interest of \$612,344, consistent with the provisions of this Subsection C.
- (ii) Within ten (10) days of the entry of this Order, Respondent shall deposit \$5,847,200 (the "Distribution Fund") into an escrow account acceptable to the Commission staff and shall provide the Commission staff with evidence of such deposit in a form acceptable to the Commission staff. If timely payment 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 affected by the above conduct described herein, 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 Respondent or its past or present officers or directors.
- (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. 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) The distribution of the Distribution Fund shall be made in the next fiscal quarter immediately following the staff's approval of the Calculation but no later than within ninety (90) days of the staff's approval of the Calculation. If Respondent

does not distribute any portion of the Distribution Fund for any reason, including factors beyond Respondent's control, Respondent shall transfer any such undistributed funds to the Commission for transmittal to the United States Treasury. Any such payment shall be made in accordance with Paragraph x below.

- (vi) Respondent agrees to be responsible for all tax compliance responsibilities associated with distribution of the Distribution Fund and may retain any professional services necessary. The costs and expenses of any such professional services shall be borne by Respondent and shall not be paid by any of Respondent's past or present clients.
- (vii) Within 120 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. 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 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 PNC Investments 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.
- (viii) After Respondent has submitted the final accounting to the Commission staff, the staff shall submit the final accounting to the Commission for approval and shall request Commission approval to send any undistributed amount to the United States Treasury.
- (ix) The Commission staff may extend any of the procedural dates set forth in Paragraphs iv through vii 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.

- (x) If Respondent is unable to distribute or return any portion of the Distribution Fund for any reason, Respondent shall transfer any such undistributed funds to the Commission for transmittal to the United States Treasury, in accordance with Exchange Act Section 21(F)(g)(3), after the final accounting provided for in Paragraph vii of Subsection C is submitted to the Commission staff.

D. Respondents shall, within ten (10) days of the entry of this Order, pay, in addition to the amounts referenced in Subsection C, disgorgement of \$497,144 and prejudgment interest of \$63,426 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 \$900,000 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 PNC Investments 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