

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 88976 / June 1, 2020

INVESTMENT ADVISERS ACT OF 1940
Release No. 5513 / June 1, 2020

ADMINISTRATIVE PROCEEDING
File No. 3-19818

In the Matter of

U.S. BANCORP
INVESTMENTS, 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 U.S. Bancorp Investments, Inc. (“USBI” 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 finds that:

Summary

1. These proceedings arise from breaches of fiduciary duties by USBI, a dually-registered investment adviser and broker-dealer, in connection with its mutual fund share class selection practices and its receipt of fees for shareholder servicing ("shareholder servicing fees") and fees pursuant to Rule 12b-1 under the Investment Company Act of 1940 ("12b-1 fees"). From October 2012 through November 2017, USBI purchased, recommended, and held for advisory clients mutual fund share classes that charged 12b-1 fees and shareholder servicing fees instead of lower-cost share classes of the same funds which were available to the clients. USBI failed to adequately disclose a conflict of interest related to these fees to its clients. In addition, by causing certain advisory clients to invest in fund share classes that charged 12b-1 fees and shareholder servicing fees when 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, Respondent violated its duty to seek best execution for those transactions. USBI 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. As a result, USBI willfully violated Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

RESPONDENT

2. **U.S. Bancorp Investments, Inc.**, incorporated in Delaware and headquartered in St. Paul, Minnesota, has been registered with the Commission as an investment adviser since July 23, 2007, and as a broker-dealer since 1986. In its Form ADV dated March 27, 2019, USBI reported regulatory assets under management of approximately \$8.5 billion.

FACTS

3. USBI offered asset management services to its advisory clients through various wrap fee programs managed on a discretionary and non-discretionary basis, in which clients paid an all-inclusive fee for asset management and trade execution ("Wrap Fee Programs").

Mutual Fund Share Class Selection

4. 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 various share classes is their fee structure.

5. Class A shares were the most prevalent of the mutual fund share classes that USBI purchased for advisory clients in its Wrap Fee Programs during the relevant 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 may continue to charge what is known as a 12b-1 fee to cover certain costs of fund distribution and shareholder services. These recurring fees, which are included in a mutual fund’s total annual fund operating expenses and vary by share class, typically are 25 basis points for class A shares. These recurring fees 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.

6. In addition to load-waived Class A shares or equivalent “no load” fund shares,¹ many mutual funds also offer share classes that do not charge 12b-1 fees (such as “Institutional Class” or “Class I” shares)² to fee-based advisory accounts. The terms and eligibility requirements for any particular share class are described in a mutual fund’s prospectus. 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 almost always 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 generally is better for the investor to purchase or hold the Class I share.

7. Between approximately October 2012 and November 2017, USBI received 12b-1 fees and shareholder servicing fees under a clearing agreement with a large nationwide clearing firm (“the Clearing Firm”) through which the Clearing Firm provided clearing and custody services for USBI’s advisory clients. The clearing agreement provided that the Clearing Firm would pay to USBI all 12b-1 fees and shareholder servicing fees received from mutual funds based on the amount of USBI client assets invested in no-transaction-fee share (“NTF”) classes of those funds. However, the Clearing Firm was not required under the clearing agreement to pay USBI any 12b-1 fees or shareholder servicing fees on transaction-fee (“TF”) share classes for the same mutual funds. The Clearing Firm’s payment of 12b-1 fees and shareholder servicing fees gave USBI the financial incentive to favor NTF load-waived Class A shares and similar NTF share classes over other lower-cost share classes.

8. During the relevant time period, USBI had a policy under which it limited its clients’ purchases of mutual fund shares to NTF load-waived Class A shares (and similar NTF share classes when Class A shares were unavailable) that paid 12b-1 fees and shareholder servicing fees to USBI. Through this policy, USBI primarily purchased and held NTF load-waived Class A shares or other similar share classes that charged 12b-1 fees and shareholder servicing fees for

¹ 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.

² Share classes that do not charge 12b-1 fees go by a variety of other names in the mutual fund industry, such as “Advisory Class,” “Class F2,” “Class Y,” and “Class Z” shares. The term “Class I shares” in this Order refers generically to share classes that do not charge 12b-1 fees.

clients in its Wrap Fee Programs – even when lower-cost share classes of those same funds were available to such clients.

9. As a result, USBI received 12b-1 fees and shareholder servicing fees that it would not have collected had those clients been invested in lower-cost share classes of those same funds.

10. During the relevant time period, USBI received approximately \$7.944 million in 12b-1 fees and approximately \$6.034 million in shareholder servicing fees. USBI kept all of the shareholder servicing fees and shared a portion of the 12b-1 fees with its registered representatives, who also were investment adviser representatives.

Disclosure Failures

11. As an investment adviser, USBI was obligated to disclose all material facts to its advisory clients, including conflicts of interest between itself, its investment adviser representatives, and its clients that could affect the advisory relationship and how those conflicts could affect the advice USBI provided to its clients. To meet this fiduciary obligation, USBI was required to provide its advisory clients with full and fair disclosure that is sufficiently specific so that they could understand the conflicts of interest concerning USBI's advice about investing in different classes of mutual funds and have an informed basis for consenting to or rejecting conflicted transactions.

12. During the relevant period, USBI did not disclose adequately to its advisory clients the conflicts of interest related to (a) its receipt of 12b-1 fees and shareholder servicing fees, and (b) its selection of mutual fund share classes that pay such fees.

Best Execution Failures

13. An investment adviser's fiduciary duty includes, among other things, an obligation to seek best execution for client transactions.³

14. During the relevant time period, USBI caused certain advisory clients to invest in fund share classes that charged 12b-1 fees and shareholder servicing 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. As a result, USBI violated its duty to seek best execution for those transactions between at least October 2012 and November 2017.

Compliance Deficiencies

15. During the relevant time period, USBI failed to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules

³ 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).

thereunder in connection with disclosure of conflicts of interest presented by its mutual fund share class selection practices, or making recommendations of mutual fund share classes that were in the best interests of its advisory clients in its Wrap Fee Programs.

VIOLATIONS

16. As a result of the conduct described above, USBI willfully⁴ 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 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)).

17. As a result of the conduct described above, USBI 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.

REMEDIAL EFFORTS

18. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent USBI and cooperation afforded the Commission staff. Starting in February 2016, USBI began rebating 12b-1 fees to all clients. In December 2017, USBI initiated the process of converting existing mutual fund investments in NTF Class A shares (or comparable classes) held by its advisory clients to the lowest-cost share classes available for the same funds on the Clearing Firm’s platform, subject to eligibility restrictions imposed by the funds.

UNDERTAKING

19. Respondent has undertaken to:

A. Within 30 days of the entry of the Order, notify affected investors (i.e., those former and current clients who, during the period from October 2012 through November 2017, purchased or held 12b-1 fee or shareholder servicing fee paying share class mutual funds when a

⁴ “Willfully,” for purposes of imposing relief under Section 203(e) of the Advisers Act and Section 15(b) of the Exchange 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).

lower-cost share class of the same fund was available to the client) of the settlement terms of the Order in a clear and conspicuous fashion.

B. Certify, in writing, compliance with the undertaking set forth above. The certification shall identify the undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to Anne C. McKinley Assistant Regional Director, Chicago Regional Office, Securities and Exchange Commission, 175 W. Jackson Blvd., Suite 1450, Chicago, IL 60604, with a copy to the Office of Chief Counsel of the Enforcement Division, no later than ten (10) days from the date of the completion of the undertaking.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent USBI'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 USBI shall 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 USBI is censured.

C. Respondent USBI shall pay disgorgement and prejudgment interest, totaling \$15,992,441, to compensate past and present advisory clients that were affected by the 12b-1 fee- and shareholder servicing fee -related conduct detailed in this Order, as follows:

- (i) Respondent shall pay disgorgement of \$13,977,908 and prejudgment interest of \$2,014,533, consistent with the provisions of this Subsection C.
- (ii) Within ten (10) days of the entry of this Order, Respondent shall deposit \$15,992,441 (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 Wrap Fee Programs, who from October 2012 through November 2017 incurred 12b-1 fees and shareholder servicing 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 or with lesser 12b-1 fees and shareholder servicing 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 shall make its employees available and shall require any third parties or professionals retained by Respondent to assist in formulating the methodology for its Calculation and/or administration of the Distribution to be 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 U.S Bancorp Investments, Inc. 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 Anne C. McKinley, Assistant Regional Director, Chicago Regional Office, Securities and Exchange Commission, 175 W. Jackson Blvd., Suite 1450, Chicago, IL 60604.

- (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 210 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 U.S. Bancorp Investments, Inc. as the Respondent in these proceedings and the file number of these proceedings to Anne C. McKinley, Assistant Regional Director, Chicago Regional Office, Securities and Exchange Commission, 175 W. Jackson Blvd., Suite 1450, Chicago, IL 60604, 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 USBI shall, within ten (10) days of the entry of this Order, pay a civil money penalty in the amount of \$2.4 million 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 U.S Bancorp Investments, Inc. 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 Anne C. McKinley, Assistant Regional Director, Chicago Regional Office, Securities and Exchange Commission, 175 W. Jackson Blvd., Suite 1450, Chicago, IL 60604.

E. 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.

F. USBI shall comply with the undertakings enumerated in Section III. above.

By the Commission.

Vanessa A. Countryman
Secretary