UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT COMPANY ACT OF 1940
Release No. 33919 / July 2, 2020

INVESTMENT ADVISERS ACT OF 1940
Release No. 5531 / July 2, 2020

ADMINISTRATIVE PROCEEDING
File No. 3-19854

In the Matter of **FRANKLIN ADVISERS, INC., and FRANKLIN TEMPLETON INVESTMENTS CORP.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, PURSUANT TO SECTION 9(f) OF THE INVESTMENT COMPANY ACT OF 1940 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 9(f) of the Investment Company Act of 1940 ("Investment Company Act"), and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") against Franklin Advisers, Inc. ("FAV") and Franklin Templeton Investments Corp. ("FTIC," together with FAV, "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the "Offers") 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 them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Section 9(f) of the Investment Company Act of 1940 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 Respondents' Offers, the Commission finds[1] that:

SUMMARY

1. These proceedings arise out of FAV and FTIC causing certain funds they managed to violate Section 12(d)(1)(A) of the Investment Company Act ("Section 12(d)(1)(A)"), which limits an investment company's ownership interests in other investment companies. First, from October 2013 to November 2015, both FAV and FTIC purchased certain ETFs for client funds, ultimately causing the funds to exceed the limits of Section 12(d)(1)(A). FAV was responsible for implementing certain of the funds' policies and procedures designed to prevent such violations, but did not do so. Second, FAV failed to communicate material facts regarding the violations to the funds' boards. In particular, in November 2015, FAV, as adviser to the funds, sold shares of certain ETFs in order for the funds to come into compliance with Section 12(d)(1)(A). Certain FAV-advised funds realized losses on one of these ETF investments. FAV did not reimburse the funds for these losses despite its stated policy, previously provided to the boards, that FAV would normally reimburse the funds for losses due to trade errors. FAV did not disclose to the boards of directors of the impacted funds the losses incurred, FAV's decision not to reimburse the losses, the associated conflict of interest, or the deviation from FAV's trade error policy.

RESPONDENTS

2. **FAV** is a corporation organized under the laws of California, and an investment adviser registered with the Commission since 1986 and headquartered in San Mateo, California. FAV had approximately $423 billion in assets under management as of September 2019.

3. **FTIC** is a corporation organized under the laws of Ontario, Canada and a wholly-owned subsidiary of Franklin Resources, Inc. FTIC is an investment adviser registered with the Commission since 2000 and headquartered in Toronto, Canada. FTIC had approximately $23 billion in assets under management as of September 2019.

OTHER RELEVANT ENTITIES

4. The **Franklin Conservative Allocation Fund, Franklin Moderate Allocation Fund** and **Franklin Growth Allocation Fund** (collectively, the "Allocation Funds") are series of the Franklin Fund Allocator Series, an open-end investment company organized in Delaware, registered with the Commission, and advised by FAV.

5. The **LifeSmart Retirement Target Date Funds** (collectively, the "LifeSmart Funds" and together with the Allocation Funds, the "Franklin Funds") are series of the Franklin

[1] The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

Fund Allocator Series, an open-end investment company organized in Delaware, registered with the Commission and advised by FAV.

6. The **Franklin Quotential Growth Portfolio, Franklin Quotential Diversified Equity Portfolio, Franklin Quotential Diversified Income Portfolio, Franklin Quotential Balanced Income Portfolio, Franklin Quotential Balanced Growth Portfolio, Franklin Quotential Diversified Income Corporate Class Portfolio, Franklin Quotential Balanced Income Corporate Class Portfolio and Franklin Quotential Balanced Growth Corporate Class Portfolio** (collectively, the "Quotential Funds") are open-end investment companies formed under Canadian law and are managed by FTIC. The Quotential Funds are not registered with the Commission.

FACTS

Statutory Limits on Fund of Funds Investments

7. Section 12(d)(1) of the Investment Company Act sets forth certain limits and conditions on investments made by investment companies that invest in the securities of other investment companies. Section 12(d)(1) prevents pyramiding, in which investors in the acquiring fund could control the assets of the acquired fund and thereby enrich themselves at the expense of the acquired fund shareholders, unduly complex structures, and excessive cost to fund investors. An acquiring fund may exercise control over an acquired fund through a controlling interest of the acquired fund's voting securities or through the threat of large-scale redemptions. In 1970, Section 12(d)(1) was amended to prevent similar abuses by investors in unregistered acquiring funds.

8. Section 12(d)(1)(A) prohibits registered and unregistered investment companies (each, the "acquiring company") from: (i) acquiring more than 3% of the outstanding voting stock of a registered investment company; (ii) acquiring securities issued by another registered investment company (the "acquired company") when such acquisitions result in the acquired company having an aggregate value of more than 5% of the total assets of the acquiring company; or (iii) acquiring securities issued by another registered investment company (the "acquired company") when such acquisitions result in the acquired company and all other investment companies having an aggregate value of more than 10% of the total assets of the acquiring company.

9. Section 12(d)(1)(F) of the Investment Company Act allows a registered investment company (the "acquiring company") to invest in unaffiliated investment companies in excess of limits imposed in Section 12(d)(1)(A), provided, among other things, that the acquiring company and its affiliates do not own, in the aggregate, more than 3% of the outstanding shares of the acquired company.

FAV Caused Certain Funds to Purchase Interests in Other Investment Companies That Exceeded the Limits in Section 12(d)(1)(A)

10. From December 2014 to November 2015 ("Relevant Time Period 1"), the Allocation Funds and eight LifeSmart Retirement Target Date Funds purchased shares of three

ETFs ("ETF No. 1," "ETF No. 2," and "ETF No. 3"), all registered, unaffiliated investment companies. At the time of these purchases by the Allocation Funds and LifeSmart Funds, each fund's holdings of investment companies in the aggregate exceeded 10% of its assets. FAV attempted to rely on Section 12(d)(1)(F) to permit the Franklin Funds to hold shares of investment companies in excess of the Section 12(d)(1)(A)(iii) limit, i.e., each of the Franklin Fund's holdings of other investment companies, including the shares of ETF Nos. 1 through 3 and all other registered investment companies, could have an aggregate value of more than 10% of the fund's total assets. However, as reflected in the table below, during Relevant Time Period 1, FAV's aggregate purchases of ETF Nos. 1, 2, and 3 caused the Franklin Funds to exceed the firm-wide 3% ownership limits of Section 12(d)(1)(F) for each ETF.

ETF	ETF Shares Outstanding	Date Franklin Funds breached the 3% limit under 12(d)(1)(F)	Shares Held by Franklin Funds as of November 24, 2015	Franklin Funds Ownership % as of November 24, 2015
No. 1	28,600,000	12/16/2014	1,647,976	5.76%
No. 2	83,452,000	7/17/2015	4,968,222	5.95%
No. 3	46,701,000	10/6/2015	2,990,445	6.40%

Because firm-wide ownership of ETF Nos. 1 through 3 each exceeded 3%, the Franklin Funds could not rely on the exemption of Section 12(d)(1)(F), and FAV caused the Franklin Funds that had purchased those ETFs to violate Section 12(d)(1)(A)(iii).

11. During Relevant Time Period 1, the Franklin Funds had written policies and procedures designed to comply with Section 12(d)(1)(A), including compliance with the conditions of the exemption in Section 12(d)(1)(F). FAV was responsible for implementing the Franklin Funds' written policies and procedures. FAV, however, failed to implement a pre-trade screening process with regard to Section 12(d)(1)(F) set forth in those written policies and procedures. As a result, certain of the Franklin Funds' purchases of ETF Nos. 1 through 3 exceeded the 3% complex-wide ownership limit with respect to holdings in the three ETFs.

12. On November 24, 2015, FAV's compliance department discovered the breaches of the limits in Section 12(d)(1)(A). Because of such breaches, on November 25, November 27 and November 30, 2015, FAV reduced its clients' positions in the ETFs to bring complex-wide ownership within the 3% limit of Section 12(d)(1)(F). As a result, the Allocation Funds realized losses of $2,184,031 for ETF No. 1 and gains of $3,723,124 and $4,747,560 from selling their holdings in ETF Nos. 2 and 3, respectively.

FAV Breached Its Fiduciary Duty to the Allocation Funds and Failed to Follow Its Own Policies and Procedures

13. As an investment adviser, FAV had a fiduciary duty to act in its clients' best interests. FAV also owed a duty of loyalty to clients, which required it to fully and fairly disclose all material facts that could affect the advisory relationship, including any conflicts of interest that

arose between itself and its clients. In addition, FAV's trade error policy, which had previously been provided to the funds' board, normally required that FAV reimburse losses incurred by clients for a security bought or sold in contravention of regulatory investment restrictions.

14. However, FAV ultimately concluded, as a result of offsetting gains that the Allocation Funds earned from selling two different securities—shares in ETF Nos. 2 and 3— that FAV would not reimburse the Allocation Funds' losses in ETF No. 1.

15. FAV's decision not to reimburse the Allocation Funds created a conflict of interest due to FAV's financial incentive to avoid having to reimburse the Allocation Funds for the losses resulting from the corrective sales of ETF No. 1. FAV did not disclose this conflict of interest to the Allocation Funds' board.

16. The manner in which FAV determined not to reimburse the Allocation Funds for the losses also contravened FAV's own policies and procedures. Under normal circumstances, FAV's trade error policy required FAV to reimburse for client losses on trade errors. The FAV trade error policy provided for an alternative method of correcting a trade error, but only under certain circumstances and with the approvals of designated FAV officers. However, FAV did not conduct an analysis under any alternative method and compliance never obtained the requisite approvals. Moreover, FAV's policies and procedures required FAV to document all trade errors, circulate the documentation to senior officers in the affected departments, and report the errors and corrective action to the board of trustees. But FAV failed to follow these policies or procedures.

17. In a memorandum dated June 30, 2016, FAV first reported the Section 12(d)(1)(A) violations by the Allocation Funds and LifeSmart Funds to these funds' board of trustees. FAV orally communicated the violations of Section 12(d)(1)(A) at a board meeting on July 13, 2016. In those communications to the board, FAV omitted any reference to the Allocation Funds' realized losses as the result of the corrective sales of ETF No. 1, that FAV would not be reimbursing the Allocation Funds for the losses, the associated conflict of interests, or that FAV had not followed its policies and procedures in making its determinations.

18. In February 2018, after the commencement of the Commission's investigation, FAV first disclosed to the Franklin Funds' board the losses that the Allocation Funds incurred on the corrective sales of ETF No. 1. In December 2018, FAV fully reimbursed the Allocation Funds for these losses, including interest.

FTIC Caused Certain Funds to Purchase Interests in Other Investment Companies That Exceeded the Limits in Section 12(d)(1)(A)

19. From approximately February 2015 to September 2016 ("Relevant Time Period 2"), six Quotential Funds, managed by FTIC, acquired shares of ETF No. 4, an unaffiliated, registered investment company, in excess of the 3% limit in Section 12(d)(1)(A)(i). The six Quotential Funds each purchased the shares in amounts ranging from 3.309% to 24.635% of the outstanding shares of ETF No. 4. In the aggregate, the Quotential Funds acquired between 64.59% to 90.65% of ETF No. 4 during Relevant Time Period 2.

20. In approximately October 2015, when the Quotential Funds had acquired approximately 78% of the outstanding shares of ETF No. 4, the Quotential Funds' portfolio managers proposed to the investment adviser of ETF No. 4 that FTIC would increase their clients' investments in the ETF in exchange for a reduction in the management fee and absent such a fee waiver, would redeem their entire existing investment. The ETF's adviser agreed and, after informing the board of ETF No. 4, reduced the management fee by 15 basis points for all shareholders. The Quotential Funds proceeded to purchase an additional 12% of the ETF's shares. The Quotential Funds' ownership levels of ETF No. 4 peaked in February 2016 when their holdings totaled 90.65% of the ETF's shares.

21. From approximately October 2013 to September 2016 ("Relevant Time Period 3"), five Quotential Funds acquired shares of ETF No.5, a registered, unaffiliated investment company, in excess of the 3% limit in Section 12(d)(1)(A)(i). The five Quotential Funds acquired the shares in amounts ranging from 3.038% to 20.72% of the then outstanding shares of ETF No. 5. In the aggregate, the Quotential Funds' acquisitions totaled between 24% to 29% of ETF No. 5 during Relevant Time Period 3.

22. As investment companies, the Quotential Funds' purchases of the shares of ETF Nos. 4 and 5—both registered investment companies—were subject to the 3% limit in Section 12(d)(1)(A)(i). The applications for exemptive relief from Section 12(d)(1)(A) filed by the issuers of ETF Nos. 4 and 5 with the Commission requested exemptive relief for "certain registered open-end management investment companies" to aquire the ETF's shares in excess of Section 12(d)(1) limits, subject to certain conditions and representations specified in each application. As unregistered investment companies, the Quotential Funds were ineligible to avail themselves of the relief from Section 12(d)(1)(A) granted by the Commission in connection with the applications.

23. FTIC, the manager of the Quotential Funds, caused the Quotential Funds to violate Section 12(d)(1)(A)(i).

FAV's and FTIC's Remedial Efforts

24. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by FAV and FTIC.

VIOLATIONS

25. As a result of the conduct described above, FAV caused certain Franklin Funds to violate Section 12(d)(1)(A)(iii) of the Investment Company Act, which prohibits registered investment companies from acquiring securities issued by another registered investment company (the "acquired company") when such acquisitions result in the acquired company and all other investment companies having an aggregate value of more than 10% of the total assets of the acquiring company.

26. As a result of the conduct described above, FTIC caused the Quotential Funds to violate Section 12(d)(1)(A)(i) of the Investment Company Act, which prohibits investment

companies from acquiring more than 3% of the outstanding voting stock of a registered investment company.

27. As a result of the conduct described above, FAV willfully 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."[2] Scienter is not required to establish a violation of Section 206(2), which may rest on a finding of simple 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)).

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

29. As a result of the conduct described above, FAV caused the Franklin Funds' violations of Rule 38a-1(a) of the Investment Company Act, which requires that registered investment companies, among other things, adopt and implement written policies and procedures reasonably designed to prevent violation of the federal securities laws by the fund, including policies and procedures that provide for the oversight of compliance by the fund's investment adviser.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest, to impose the sanctions agreed to in Respondents' Offers.

Accordingly, pursuant to Section 9(f) of the Investment Company Act and Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

A. Respondent FAV cease and desist from committing or causing any violations and any future violations of Section 12(d)(1)(A) of the Investment Company Act and Rule 38a-1 promulgated thereunder and Sections 206(2) and 206(4) of the Advisers Act and Rule 206-4(7), promulgated thereunder.

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[2] "Willfully," for purposes of imposing relief under Section 9(b) of the Investment Company Act and Sections 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).

B. Respondent FTIC cease and desist from committing or causing any violations and any future violations of Section 12(d)(1)(A) of the Investment Company Act.

C. Respondent FAV is censured.

D. Respondent FAV shall, within 30 days of the entry of this Order, pay a civil money penalty in the amount of $250,000 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.

E. Respondent FTIC shall, within 30 days of the entry of this Order, pay a civil money penalty in the amount of $75,000 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.

F. Payment must be made in one of the following ways:

(1) Respondents may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondents 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) Respondents 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 Franklin Advisers, Inc. or Franklin Templeton Investments Corp. 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 simultaneously sent to C. Dabney O'Riordan, Co-Chief, Asset Management Unit, Securities and Exchange Commission, Los Angeles Regional Office, 444 South Flower Street, Suite 900, Los Angeles, CA 90071, or such other person or address as the Commission staff may provide.

G. 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, Respondents agree that in any Related Investor Action, they shall not argue that they are entitled to, nor shall they benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondents' payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondents agree that they 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 Respondents 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.

Vanessa A. Countryman
Secretary