

# DC Circuit Opinion Reaffirms Fiduciary and Disclosure Obligations of Advisers While Rejecting SEC Finding of “Willful” Violations

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The [DC Circuit recently released an opinion](#) addressing the SEC’s administrative findings against registered investment adviser The Robare Group (TRG) for failure to disclose alleged conflicts of interest. Although the court affirmed the SEC’s finding of a violation of Section 206(2) of the Advisers Act, it held that Commission could not find willful violations under Section 207 based on the same negligent conduct.

The court’s analysis of 206(2) of the Advisers Act, the key negligence-based antifraud provision for investment advisers, is instructive. The court affirmed that, as a fiduciary to its clients, the adviser was required to make full and fair disclosure of all material facts, including conflicts of interest. However, the Commission also asserted that TRG violated Section 207 of the Advisers Act by willfully failing to disclose material conflicts of interest in its Form ADV Part 2 brochures. Yet because TRG acted negligently but not “intentionally or recklessly,” the DC Circuit disagreed that this factual basis could support a finding of willful misconduct. The holding appears to contradict the SEC’s traditional approach to alleging “willful” violations under the [Wonsover](#) analysis, which focuses on whether the actor intentionally (as opposed to involuntarily) committed the act constituting the violation.

Does the *Robare* decision mean that “willful” misconduct requires a finding of scienter? And does it shut the door on allegations of willful misconduct in negligence-based cases? Probably not. But it will make it more difficult for the Enforcement Division to allege willful violations in a litigated or settled context without more than negligence.

## I. Facts

The Robare Group (TRG) is a registered investment adviser that used a separate financial firm for execution, custody, and clearing services for its clients. In 2004, TRG entered into a revenue sharing arrangement with the custodial firm, whereby TRG received compensation when its clients invested in certain mutual funds offered on the firm's online platform. The Division of Enforcement at the SEC instituted an administrative proceeding in 2014 against TRG and its principals, alleging that they failed to disclose the revenue sharing agreement and the potential conflict of interest it created. Specifically, the Division alleged violations of Sections 206(1), 206(2), and 207 of the Advisers Act. Sections 206(1) and (2) govern disclosure to clients, while Section 207 addresses disclosures in filings with the Commission. A violation of Section 206(1) requires proof of scienter – an intent to defraud, but proof of simple negligence is sufficient to establish violation of Section 206(2). Section 207 proscribes willful untrue statements about, or omissions of, material facts.

In the initial administrative proceeding, the SEC's Administrative Law Judge had dismissed all charges brought by the Enforcement Division, at which point the Division sought review by the Commission. The [Commission conducted a de novo review](#), and concluded that TRG and its principals violated Section 206(2) by failing to adequately disclose material conflicts of interest to their clients, and Section 207 by willfully omitting material facts from TRG's ADVs filed with the Commission.

## **II. Key Holdings**

In appealing the Commission's determination, TRG argued it did not violate Section 206(2) because: (1) TRG's ADV brochures adequately disclosed the conflicts of interest arising from the revenue sharing arrangement; and (2) they were not negligent. After reviewing TRG's Forms ADV, the DC Circuit determined the statements made in the filings did not clearly and explicitly disclose the conflicts of interest arising from the payment arrangement "in a manner that would enable [TRG's] clients to understand the source and nature of the conflicts." The court also deemed TRG's arguments disputing its negligence "unpersuasive," finding that "[b]ecause a reasonable adviser with knowledge of the conflicts would not have committed such clear, repeated breaches of its fiduciary duty, TRG and its principals acted negligently."

In affirming the Commission's findings with respect to Section 206(2), it is important to note that the Commission's *de novo* review found that "TRG's disclosure that it may receive selling compensation...in no way revealed that TRG actually had an arrangement with [the custodial firm], that it received fees pursuant to the arrangement, and the arrangement presented at least a potential conflict of interest" Emphasis in original. In its recent [Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers](#), the Commission cited to its *de novo* review in support for the proposition that "an adviser disclosing that it 'may' have a conflict is not adequate disclosure when the conflict actually exists."

The court rejected TRG's claim that the SEC was required to call an expert to establish the relevant standard of care, finding that the fiduciary duty involved was "not so complex as to require expert testimony." According to the court, TRG was under a duty to fully reveal potential conflicts to their clients, and for a decade their disclosures made no reference to the payment arrangement at all. The court was not swayed by TRG's argument that their conduct conformed to that of most other investment advisers, stating "negligence is judged against a standard of reasonable prudence, whether that standard usually is complied with or not." (internal citation omitted). The court therefore affirmed the Commission's findings of negligent violations under Section 206(2).

TRG also disputed the Commission's finding of a willful violation of Section 207. The court acknowledged that it had yet to address the meaning of "willfully" as applied to Section 207, and proceeded to apply the standard set out in *Wonsover v. SEC*, 205 F.3d 408 (D.C. Cir. 2007) (addressing the definition of willfully in connection with Section 15(b)(4) of the Exchange Act). In *Wonsover*, the court determined that "willfully" in the context of a securities violation means "intentionally committing the act which constitutes the violation." 205 F.3d at 414. The DC Circuit rejected the SEC's position that TRG acted intentionally by choosing the language contained in the Forms ADV. Section 207, in the court's view, "does not proscribe willfully *completing or filing* a Form ADV that turns out to contain a material omission but instead makes it unlawful 'willfully *to omit . . . any material fact*' from a Form ADV." Thus, the court held that Section 207 requires a finding based on substantial evidence that one of TRG's principals subjectively intended to omit material information from TRG's Forms ADV.

Additionally, the court reiterated that negligence and intent are mutually exclusive concepts. Therefore, the Commission can't point to the same set of actions that it found to be negligent under 206(2) and claim they support a finding of willfulness under Section 207.

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