CARLTON FIELDS

DC Circuit: Willful Means Intentional Under the Advisers Act – Negligent Conduct Cannot Be Willful Conduct

July 11, 2019

In *Robare Group v. SEC*, the court clarified the meaning of "willfully" under Section 207 of the Investment Advisers Act of 1940. A willful omission requires that a person "subjectively intended to omit material information."

So, when the SEC alleges inadequate financial disclosure — for example, Form ADV disclosure that does not address receipt of "revenue sharing" payments (e.g., shareholder servicing fees paid when clients invest in certain eligible funds on an online platform) or the potential conflict of interest to clients created by those payments — an investment adviser cannot be held liable for willful violations of the Advisers Act if the adviser's conduct was merely negligent.

Importantly, however, not all of the Advisers Act's anti-fraud provisions are predicated on "willful" misconduct. Thus, courts have held that a violation of Section 206(1) requires proof of scienter (i.e., an intent to deceive, manipulate, or defraud) and a violation of Section 206(2) requires proof only of simple negligence. But, prior to Robare, the courts had not addressed the meaning of "willfully" in Section 207, which makes it unlawful for any person to willfully make any untrue statement of material fact, or omit to state any material fact, in Form ADV or reports filed with the SEC.

Robare is important for several reasons. In addition to clarifying that negligent conduct (failure to exercise reasonable care under all circumstances) is not sufficient to establish a willful violation under Section 207, the court:

- reinforced the importance of disclosure (in Form ADV) of "revenue sharing" arrangements;

- emphasized the importance of full and fair disclosure of potential conflicts of interest created by "revenue sharing" arrangements; and
- confirmed that the "everyone else does it this way" defense is not sufficient to overcome a negligence allegation. Rather, the fact that an adviser's disclosure is consistent with industry practice does not mean that the adviser acted reasonably.

It also is possible that *Robare*'s interpretation of "willful" will be followed by other circuits or where that term appears in federal securities law provisions other than Section 207 of the Advisers Act. This could greatly amplify the decision's relevance for advisers and their counsel in defending against allegations of willful misconduct.

Authored By

Ann Began Furman

Related Practices

Financial Services Regulatory

Related Industries

Life, Annuity, and Retirement Solutions
Securities & Investment Companies