

**COMMONWEALTH OF KENTUCKY
PUBLIC PROTECTION CABINET
DEPARTMENT OF FINANCIAL INSTITUTIONS
ADMINISTRATIVE ACTION NO. 2025-DFI-0074**



KENTUCKY DEPARTMENT OF FINANCIAL INSTITUTIONS

COMPLAINANT

v.

VANGUARD MARKETING CORPORATION (CRD #7452)

and

THE VANGUARD GROUP, INC. (CRD #105958)

RESPONDENTS

CONSENT ORDER

Pursuant to the authority granted to The Kentucky Department of Financial Institutions, under Kentucky Revised Statutes Chapter 292 ("Securities Law"), and after investigation, careful review, and due consideration of the facts and statutory provisions set forth below, the Kentucky Department of Financial Institutions hereby finds that there is good cause and it is in the public interest to enter into a Consent Order (the "Consent Order") with Vanguard Marketing Corporation and The Vanguard Group, Inc. (together, "Vanguard" or "Respondents"), which hereby agree to resolve any and all issues in controversy regarding the specific conduct described herein under the terms set forth in this Consent Order.

WHEREAS, The Vanguard Group Inc. ("VGI") (CRD No. 105958) is registered with the United States Securities and Exchange Commission (the "SEC") as an investment adviser. VGI is one of the largest investment advisers in the world, is owned by its U.S. mutual funds, and provides services to the funds at Vanguard's cost of operations;

WHEREAS, Vanguard Marketing Corporation ("VMC") (CRD No.7452), with a main address of 100 Vanguard Blvd., Malvern, Pennsylvania 19355, has been registered with Kentucky as a broker-dealer since July 16, 1982. As an institutional brokerage firm, VMC offers portfolio

management, financial planning and advisory services. VMC is a wholly owned subsidiary of VGI;

WHEREAS, parallel to a concurrent investigation conducted by the SEC, the North American Securities Administrators Association (“NASAA”), with Connecticut, New Jersey, and New York among five other states, conducted an investigation into the circumstances surrounding the recommendation of VGI to the Vanguard Chester Funds (the “Trust”) to lower the investment minimum of its Institutional Target Retirement Funds (“TRFs”), effective December 11, 2020, and the resulting capital gains tax distributions in December 2021 to shareholders of Investor TRFs (“Investor TRFs”) who held the funds in taxable accounts;

WHEREAS, Vanguard has agreed to resolve the Investigation upon the terms specified in the Settlement Term Sheet executed as of January 15, 2025, between Vanguard and the participating NASAA jurisdictions, with all participating states and territories identified in Appendix A to the Settlement Term Sheet (each, a “Jurisdiction” and collectively, the “Jurisdictions”);

WHEREAS, Vanguard consents to the form, content, and entry of this Consent Order; and

WHEREAS, Vanguard neither admits nor denies the findings of fact contained herein;

NOW, THEREFORE, the Commissioner, as administrator of KRS Chapter 292, hereby enters this Consent Order:

FINDINGS OF FACT

1. The Trust has been organized as a Delaware statutory trust since 1998. The Trust is registered with the SEC under the Investment Company Act as an open-end management investment company.

2. Except as otherwise expressly stated, the conduct described herein occurred during the approximate time period of December 1, 2019, to December 31, 2021 (the “Relevant Time

Period”).

A. Reduction of the Institutional TRF Investment Minimum

3. Vanguard markets and distributes the TRFs to investors who hold TRF shares in qualified accounts that offer special tax treatment, including deferred taxes, as well as to investors who hold TRF shares in taxable accounts.

4. The TRFs are mutual fund investments designed for investors who plan to retire close to the target year indicated in the fund’s name. As an investor approaches the target retirement age, the TRFs’ asset allocation strategy moves toward more conservative investments.

5. During the Relevant Time Period, Vanguard marketed and distributed two suites of TRFs on behalf of the Trust: Institutional TRFs and Investor TRFs. Each suite offered 12 vintages of TRFs with different target retirement years. Each vintage of the Institutional and Investor TRFs distributed to shareholders virtually all of its net short-term and long-term capital gains realized from the sale of its holdings or received from the TRFs’ underlying funds.

6. During the Relevant Time Period, the Institutional TRFs had lower expense ratios than the Investor TRFs. Prior to December 2020, the investment minimum for the Institutional TRFs was \$100 million and the investment minimum for the Investor TRFs was \$1,000.

7. VGI recoups the expenses it incurs for its investment advisory services to the Trust from the expense ratios paid by TRF shareholders. VGI monitors the TRFs’ expense ratios to ensure that any difference between the expense ratios and the costs VGI incurs to service the funds does not exceed certain guidelines.

8. By the middle of 2019, due in part to increased investments by small-sized and medium-sized retirement plans, Investor TRF assets had grown substantially. The growth in assets resulted in economies of scale that lowered VGI’s expenses in servicing the Investor TRFs, creating a gap

between the expense ratios and VGI's expenses. As a result, in early 2020 Vanguard formed a Pricing Working Group to reduce the gap between the expense ratios and VGI's expenses for the Investor TRFs, and to return value to shareholders.

9. VGI tasked the Pricing Working Group with analyzing various options to return value to shareholders and to recommend solutions to VGI's Global Investment Committee, which would in turn make a recommendation to the Trust's Board of Trustees. The Pricing Working Group concluded its analysis in March 2020. At the time the Pricing Working Group performed its analysis, the financial markets had suffered substantial losses due to the Covid-19 pandemic.

10. The Pricing Working Group considered several options, but in October 2020 ultimately recommended to the Global Investment Committee lowering the minimum investment of the Institutional TRFs from \$100 million to \$5 million, and also to lower the Investor TRFs' expense ratios by 0.01% to 0.02%. In November 2020, the Global Investment Committee recommended the investment minimum reduction to the Trust's Board of Trustees, which approved the change.

11. The Pricing Working Group failed to update its March 2020 analysis regarding potential capital gains impacts or consider whether significant market appreciation could impact its evaluation of potential capital gains or tax consequences from investors redeeming Investor TRF shares in 2021, when it made its recommendation to the Global Investment Committee in October 2020. Thus, the Global Investment Committee and the Board of Trustees relied on outdated data in approving the lowering of the Institutional TRF investment minimum. Accordingly, in making its recommendation to the Global Investment Committee and ultimately to the Board of Trustees, the Pricing Working Group failed to account for the significant market rebound that occurred between March and October 2020, and the potential for continued market appreciation, in its analysis of potential capital gains impacts to the Investor TRFs. As a result, the size of the capital

gains distributions from the Investor TRFs in December 2021 was significantly larger than the Pricing Working Group anticipated it would be based on market conditions in March 2020.

12. On December 11, 2020, Vanguard announced, via press release and Institutional TRF prospectus supplement, the lowering of the investment minimum in Institutional TRFs from \$100 million to \$5 million, effective immediately.

13. After the December 11, 2020, announcement, and through the first half of 2021, a substantial number of small- and medium-sized retirement plan investors in the Investor TRFs redeemed fund shares to switch to the Institutional TRFs due to the lower expense ratio. To meet these redemptions, the Investor TRFs had to sell underlying assets at elevated prices due to the rising financial markets that had rebounded from pandemic lows and reached new highs. As compared to prior years, the redemptions resulted in large capital gains distributions to investors holding the Investor TRFs in taxable accounts in December 2021.

14. In 2020, Investor TRF shareholders holding the funds in taxable accounts at Vanguard received long-term and short-term capital gains distributions of approximately \$290 million. At the end of 2021, after VGI lowered the investment minimum for Institutional TRFs, Investor TRF shareholders holding the funds in taxable accounts at Vanguard received approximately \$2.5 billion in long-term and short-term capital gains distributions. The TRFs distributed long and short-term capital gains to more than 1,050 Kentucky accounts.

15. In February 2022, the Trust merged the Investor and Institutional TRFs.

B. VMC's Supervisory System During the Relevant Time Period

16. The members of the Pricing Working Group comprised individuals from various business groups within Vanguard, including certain FINRA registered VMC agents. Among the options explored by the Pricing Working Group was reducing the investment minimum of the Institutional

TRFs, expense reductions, and merging the Institutional and Investor TRFs.

17. By March 2020, the Pricing Working Group had identified that lowering the investment minimum of the Institutional TRFs could potentially result in capital gains and tax consequences for shareholders holding the Investor TRFs in taxable accounts. The Pricing Working Group estimated that approximately 5.79% or \$17 billion of Investor TRF assets were held by investors in taxable accounts at Vanguard. The Pricing Working Group further estimated that approximately 40% of total Investor TRF assets were held by investors in non-Vanguard brokerage accounts. Additionally, the Pricing Working Group assumed that redemptions from the Investor TRFs would be staggered over time, potentially reducing the sale of assets to meet redemptions and related capital gains.

18. Merging the Institutional and Investor TRFs would have eliminated the gap between the Investor TRFs' expense ratios and Vanguard's expenses, and could have been achieved with no capital gains or tax consequences for taxable investors, but the Pricing Working Group decided not to recommend this option to the Global Investment Committee because it would result in an immediate reduction in Vanguard's revenues that was significantly larger than the other options considered, and would impair Vanguard's ability to make expense reductions in other products. The Pricing Working Group determined that the potential capital gains and tax consequences to investors holding the Investor TRFs in taxable accounts did not "present a hindrance" to lowering the investment minimum of the Institutional TRFs.

19. In March 2020, the Pricing Working Group, including the FINRA registered VMC agents, settled on the recommendation to reduce the Institutional TRF investment minimum from \$100 million to \$5 million and to also lower the Investor TRFs' expense ratios.

20. On October 5, 2020, the Pricing Working Group recommended to the Global Investment

Committee to lower the investment minimum of the Institutional TRFs from \$100 million to \$5 million and to lower the Investor TRF expense ratios by 0.01% to 0.02%. The VMC agents who served on the Pricing Working Group, however, failed to disclose to the Global Investment Committee the risk that reducing the investment minimum of the Institutional TRFs could cause significant redemptions from the Investor TRFs, potentially resulting in high capital gains distributions and tax consequences for investors who held the Investor TRFs in taxable accounts.

21. VMC, through its registered agents, knew or should have known that reducing the investment minimum for the Institutional TRFs could result in significant redemptions of shares from the Investor TRFs, and potential tax impacts in the form of historically large capital gains distributions to Investor TRF shareholders who held the funds in taxable accounts.

22. VMC's supervisory system was not reasonably designed to ensure that the registered VMC agents who served on the Pricing Working Group would disclose to the Global Investment Committee the risk that Investor TRF shareholders holding the funds in taxable accounts could potentially receive higher than usual capital gains distributions as a result of lowering the investment minimum for Institutional TRFs.

C. VGI's Failure to Disclose the Potential Capital Gains Tax Consequences

23. VGI prepared the prospectuses for the Investor and Institutional TRFs and distributed the prospectuses to investors.

24. In the TRF prospectuses, VGI represented to investors that "[c]apital gains distributions may vary considerably from year to year as a result of the Fund's normal investment activities and cash flows," and that "funds with high turnover rates may be more likely to generate capital gains."

25. However, VGI recommended lowering the Institutional TRF investment minimum in order to reduce expenses for a substantial number of small- and medium-sized retirement plans that

would redeem Investor TRF shares to move to lower-cost Institutional TRFs. The resulting surge of redemptions in Investor TRFs, and historically high capital gains distributions, were not “normal investment activities and cash flows.”

26. Despite VGI’s knowledge that retail investors holding approximately 5.79% of Investor TRF assets could potentially experience substantially higher than normal capital gains distributions and taxes on those distributions, Vanguard failed to disclose this risk to investors, including in the Investor TRFs’ prospectuses and the December 11, 2020, press release.

CONCLUSIONS OF LAW

27. Pursuant to KRS 292.337(2)(k) and 808 KAR 10:030, Section 3, it is a violation of the Securities Law for a registered broker-dealer firm to fail to establish and maintain a system to reasonably supervise its agents.

28. Pursuant to KRS 292.330(3), certain members of the Pricing Working Group were registered agents of VMC. The VMC registered agents knew or should have known of the risk that reducing the investment minimum for the Institutional TRFs could potentially result in higher than usual capital gains distributions to investors holding the Investor TRFs in taxable accounts and potentially cause adverse tax impacts on those investors.

29. VMC failed to have an adequate supervisory system to ensure that its agents sufficiently communicated to the Global Investment Committee the risk that investors holding the Investor TRFs in taxable accounts could potentially receive significant capital gains distributions and related tax obligations.

30. These failures by VMC constitute a failure to enforce a reasonably designed supervisory system, in violation of 808 KAR 10:030, Section 3.

31. VGI's decision to lower the investment minimum of the Institutional TRFs and the resulting surge of redemptions from the Investor TRFs, and historically high capital gains distributions to shareholders of the Investor TRFs, were not normal investment activities and cash flows of the TRFs. VGI's failure to disclose the potential for higher capital gains distributions from lowering the investment minimum of the Institutional TRFs was materially misleading to investors holding Investor TRFs in taxable accounts.

32. Pursuant to KRS 292.320(1)(b), it is a violation to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading.

ORDER

On the basis of the Findings of Fact, Conclusions of Law, and Vanguard's consent to the entry of this Order, IT IS HEREBY ORDERED:

33. Vanguard shall permanently cease and desist from conduct in violation of KRS 292.320 as described herein;

34. On about January 15, 2025, Vanguard entered into the following settlement agreements: (i) the Settlement Term Sheet; (ii) the Order Instituting Administrative and Cease-and-Desist Proceedings against Vanguard Group, Inc., Admin. Proc. File No. 3-22435 with the SEC (the "SEC Order"); and (iii) the Assurance of Discontinuance, No. 25-003, with the Attorney General of the State of New York (together, the "Settlement Agreements").

35. Under the Settlement Agreements, Vanguard agreed to pay \$135 million in remediation to the SEC Fair Fund for the benefit of Harmed Investors (the "Remediation Payment"). "Harmed Investors" includes certain shareholders who held Investor TRFs as of December 28, 2021, in a taxable brokerage account at VMC, a taxable account directly through the VGI, or a taxable

account through a third-party broker-dealer, and who received taxable capital gains distributions in 2021 attributable to the Investor TRFs.¹ Under the Settlement Agreements, Vanguard is entitled to receive the following offsets to the Remediation Payment:

- i. The amount of \$40 million for Vanguard's and/or its affiliates' settlement of a class action against VGI and certain related parties pending in the U.S. District Court for the Eastern District of Pennsylvania captioned, *In re Vanguard Chester Funds Lit.*, Case No. 2:22-cv-955-JFM, under a Stipulation of Settlement submitted by plaintiffs for preliminary and final Court approval ("Class Action Settlement"), and
- ii. The amount of \$2.09 million for Vanguard's settlement of certain individual investor arbitration claims filed or threatened to be filed against Vanguard or its affiliates before FINRA.

36. The total amount of remediation inclusive of the offsets in paragraph 35 is \$92.91 million, which Vanguard paid into the Fair Fund on or about January 24, 2025.

37. In the event Vanguard does not pay the \$40 million under the Class Action Settlement, as a result of the termination or withdrawal of the Stipulation of Settlement or the Court's rejection of the Class Action Settlement, Vanguard shall pay the \$40 million into the Fair Fund within ten (10) days of such termination or rejection.

38. On or about January 24, 2025, Vanguard paid an administrative penalty of \$13,500,000 into the SEC Fair Fund for distribution to Harmed Investors (the "Penalty").

¹ On July 6, 2022, the Massachusetts Securities Division and VMC entered into the Agreement and Acknowledgment of Undertakings (the "Agreement"), where the parties agreed to conclude and resolve, with prejudice, Massachusetts's investigation into VMC's "marketing practices in connection with investment minimum changes to Institutional Vanguard Target-date Retirement Mutual Funds." Under the terms of the Agreement, VMC agreed, in part, to "establish a non-reversionary escrow account" to make restitution payments to Massachusetts Investor TRF shareholders "with a primary address of record in Massachusetts who held [Investor TRFs] as of December 28, 2021, either in taxable brokerage accounts at VMC or directly through the Vanguard Group, Inc." The Agreement does not preclude Massachusetts investors who purchased through a broker dealer other than VMC from submitting claims to the SEC Fair Fund for the benefit of Harmed Investors and consistent with the SEC Order.

39. Pursuant to the terms of the SEC Order, Vanguard will pay disgorgement in the amount of \$14,700,000, plus prejudgment interest in the amount of \$3,500,000 into the SEC Fair Fund for distribution to Harmed Investors. The amounts in this paragraph will be deemed satisfied by Vanguard's payment of the amounts in paragraphs 34 through 38 above.

40. Payment of the full Remediation Payment and the Penalty by Vanguard, less any offsets or credits to which Vanguard is entitled, concludes the investigation by the Kentucky Department of Financial Institutions into any other action that the Kentucky Department of Financial Institutions could commence against Vanguard and its officers, directors, and present or former employees under applicable Kentucky Securities Law on behalf of the Kentucky Department of Financial Institutions as it relates to the Findings of Fact and Conclusions of Law herein, provided however, that excluded from and not covered by this paragraph are any claims by the Kentucky Department of Financial Institutions arising from or relating to Respondents' failures to comply with the undertakings contained herein.

41. If Respondents fail to comply materially with any of the terms set forth in this Order, the Kentucky Department of Financial Institutions may institute an action to have this Order declared null and void. In the event that a Jurisdiction believes that Respondents have defaulted in the performance of any obligation set forth in this Settlement, the Jurisdiction will provide written notice of such default to the designated representative of Respondents. Respondents shall then have fourteen (14) days to respond and an additional thirty (30) days to certify that any default has been cured, which periods may be extended by the Jurisdiction ("Response and Cure Period"). Unless the Jurisdiction in its sole discretion determines that exigent circumstances exist, the Jurisdiction will not initiate any civil action or other proceeding to enforce or for violations of this Settlement until after the expiration of the Response and Cure Period. Upon issuance of an

appropriate order, after a fair hearing, a Jurisdiction may reinstitute the actions and investigations referenced in this Settlement Term Sheet.

CONSTRUCTION AND DEFAULT

42. This Order shall not (a) form the basis for any disqualifications of Respondent from registration as a broker-dealer, investment adviser, or issuer under the laws, rules, and regulations of any state, or for any disqualification from relying upon the securities registration exemptions or safe harbor provisions to which Respondent or any of its affiliates may be subject under the laws, rules, and regulations of the settling states; or (b) form the basis for any disqualifications of Respondents under the laws of any state, the District of Columbia, Puerto Rico, or the U.S. Virgin Islands; under the rules or regulations of any securities or commodities regulator or self-regulatory organizations; or under the federal securities laws or the Commodity Exchange Act, including but not limited to, § 3(a)(39) of the Securities Exchange Act of 1934, Rule 262 of Regulation A and Rules 504 and 506(d) of Regulation D under the Securities Act of 1933 and Rule 503 of Regulation CF or safe harbor provisions; this Order is not a final order of any court; or (c) form the basis for disqualification of Respondent under the FINRA rules prohibiting continuance in membership or disqualification under other SRO rules prohibiting continuance in membership.

43. Except in an action by the Kentucky Department of Financial Institutions to enforce the obligations in this Order, this Order is not intended to be deemed or used as (a) an admission of, or evidence of, the validity of any alleged wrongdoing, liability, or lack of any wrongdoing or liability; or (b) an admission of, or evidence of, any such alleged fault or omission of Respondents in any civil, criminal, arbitration, or administrative proceeding in any court, administrative agency, or other tribunal. Nothing in this Order affects Respondents' testimonial obligations or right to take legal positions in litigation in which the Kentucky Department of Financial Institutions is not

a party. Evidence of any compromise offers and negotiations of the parties related to the Order, including the Order and its terms and any conduct or statements made during compromise negotiations, should not be used as evidence against any Party in any proceeding to prove or disprove the validity or amount of a disputed claim except in an action or proceeding to interpret or enforce the Order.

44. This Order shall be binding upon Respondents and their successors and assigns, as well as to successors and assigns of relevant affiliates, with respect to all conduct subject to the provisions above and all future obligations, responsibilities, undertakings, commitments, limitations, restrictions, events, and conditions.


45. This Order and any dispute related thereto shall be construed and enforced in accordance with, and governed by, the laws of the Commonwealth of Kentucky without regard to any choice of law principles.

SIGNED AND ENTERED BY THE COMMISSIONER this 17th day of June, 2025.


Marni Rock Gibson
Commissioner

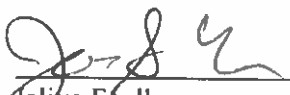
Agreed to by:

The Vanguard Group, Inc.

By: 
Jaliya Faulkner
Principal, Deputy General Counsel

Dated: 6/10/2025

Vanguard Marketing Corporation

By: 
Jaliya Faulkner
Authorized Signatory

Dated: 6/10/2025