March 23, 2012

By Electronic Delivery (*rule-comments@sec.gov*)

Ms. Elizabeth Murphy
Secretary
Securities and Exchange Commission
100 F Street N.E.
Washington, DC 20549-1090

RE: Request for Comment to Inform Study Regarding Financial Literacy Among Investors (Release No. 34 - 66164; File No. 4 - 645)

Dear Ms. Murphy:

The Association for Advanced Life Underwriting (the "AALU") appreciates the opportunity to provide comments to the Securities and Exchange Commission ("Commission" or the "SEC") in response to the request for public comment to inform the study regarding the financial literacy of investors, as required under §917 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act").

The AALU is a nationwide organization of approximately 2,200 life insurance agents and financial professionals who are primarily engaged in the sale of life insurance products for estate, charitable, retirement, deferred compensation, and employee benefit planning services. A variety of statutory and regulatory disclosure rules apply to the interactions between AALU members and their clients in the provision of these services.[1]

The above-referenced study is intended to address issues raised in §917(a)(2)-(4) of the Dodd-Frank Act. Accordingly, the Commission has specifically sought public comment on:

> (2) methods to improve the timing, content, and format of disclosures to investors with respect to financial intermediaries, investment products, and investment services; (3) the most useful and understandable relevant information that retail investors need to make informed financial decisions before engaging a financial intermediary or purchasing an investment product or service that is typically sold to retail investors…; and (4) methods to increase

[1] *See infra* at 2-3.

> the transparency of expenses and conflicts of interest in transactions involving investment services and products…[2]

We applaud the Commission's focus on the issues outlined in its release. For seventy-five years, the central mission of the SEC has been the protection of investors through disclosure. We believe disclosure requirements should be designed with the goal of promoting informed investment decisions by providing investors with salient information about the products and services offered by financial professionals. That information should include: the material features of product offerings; the scope of available products given the role of the financial professional and the investor's current financial situation, risk tolerance, and future needs; the nature of the services rendered; and information about the obligations of the financial professional in providing those services.

We believe disclosure should be concise and in "plain English" if it is to have any benefit for the vast majority of investors, who have neither the time nor the willingness to wade through lengthy disclosure documents that have too often failed to focus on the needs of retail investors, but unfortunately have become commonplace as a result of regulatory requirements and a myriad of marketplace developments.

Discussion

General Overview of the Regulation of AALU Members. AALU members—primarily licensed life insurance agents engaged in the sale life insurance products for estate, charitable, retirement, deferred compensation, and employee benefit planning services—are subject to a variety of disclosure requirements under Federal securities laws and State insurance and securities laws. For example, many of our members serve their clients as registered representatives of an insurance company or independent broker-dealers, entities that are themselves subject to an array of statutory, SEC, and FINRA consumer protection rules.[3]

In addition to rigorous market conduct and due diligence requirements, our members are generally subject to the disclosure requirements of numerous regulators. Many states in which our members are licensed have adopted model disclosure regulations for the sale of specific insurance products.[4]

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[2] The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, §917(a)(2)-(4), Pub. L. 111-203, 124 Stat. 1376 (2010) (12 U.S.C. §5301).

[3] *See generally* Securities Exchange Act of 1934, §§10(b), 15(c) (hereinafter "Exchange Act") (prohibiting misstatements or use of manipulative or deceptive devices in connection with the purchase or sale of securities). *See also* NASD Conduct Rule 2310, Recommendations to Customers (Suitability) (requiring that broker-dealers have a reasonable basis for concluding that a recommended securities transaction is "suitable" for the client based upon specific and detailed personal and financial information about the retail customer).

[4] *See, e.g.*, Annuity Disclosure Model Regulation, NAIC Model Regulation Service—April 1999, at II-245-1 (providing standards for customer disclosures to ensure a minimum level of education regarding annuity contracts).

At the Federal level, whether expressly[5] or through interpretation,[6] disclosure obligations regarding details such as product features, tax implications, fees, and market risks are imposed when our members are providing advice regarding any transactions involving insurance or annuity products registered as securities under Federal or State law.

In their totality, the disclosure and suitability requirements applicable to our members—particularly when considered in conjunction with the mandated internal supervisory procedures and rigorous inspection of broker-dealers by the Commission and FINRA—afford investors a considerable amount of protection. However, the level of investor understanding about the specific roles and responsibilities of financial professionals can be improved upon. Similarly, the level of investor knowledge around investment types, product choices, the costs and benefits of their own individual transactions, overall market risk and their own risk tolerance, and the differences between short and long-term financial objectives can be enhanced. Moreover, the methods in which this information is disclosed can be simplified.

Subjects for Consideration by the Commission. AALU members work closely with their clients and these relationships typically involve a meaningful degree of care and attention. Much of the interaction of our members with their clients takes place orally, over time, in one-to-one conversations. These relationships are set out and documented in written materials. We believe it is important that retail customers receiving services from financial professionals are provided with the information necessary to properly inform their decisions, but it must be delivered in a way that is concise, productive, and educational—and supports the development of quality working relationships.

We believe the Commission should obtain the input of investors regarding the information they believe to be most relevant to their decision-making processes. The Commission should assess how best to cultivate increased financial literacy and a deeper understanding of the products and services that investors are receiving, and not simply attempt to add to an already complex regime of disclosure regulation.

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[5] *See, e.g.*, FINRA Rule 2330 (formerly NASD Rule 2821) (establishing sales practice standards regarding recommended purchases and exchanges of variable annuities).

[6] In an April 2010 notice to its members, FINRA indicated that a broker-dealer who recommends a security to a customer possesses a duty to conduct a "reasonable investigation" concerning the security and the issuer's representations about it. Failure to adhere to this duty can be construed as a violation of the antifraud provisions of Federal securities laws, including, *e.g.*, Exchange Act §10(b) and Rule 10b-5, promulgated thereunder, as well as FINRA Rule 2010 (requiring adherence to just and equitable principles of trade) and FINRA Rule 2020 (prohibiting manipulative and fraudulent devices), among others. *See* FINRA Regulatory Notice 10-22, *available at* http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p121304.pdf (last visited Mar. 22, 2012).

Investor Testing. The presence of confusion among retail investors has been documented by the Commission on prior occasions,[7] but we believe (a) additional investor testing is needed to confirm the scope of and reasons for this confusion, and (b) the solutions proffered to date to address this problem—such as imposing a uniform standard of conduct for all financial professionals providing retail investment advice under the assumption that investors will never understand the differences among financial professionals—have insufficient empirical support and reflect a lack of appreciation for consumer preferences and needs. For example, the frequently cited RAND report[8] found that investors typically "failed to distinguish broker-dealers and investment advisers along the lines that federal regulations define," but did not reach the conclusion that investor harm resulted from any such confusion. In fact, survey findings indicated that investors were highly satisfied with services provided by their financial services professionals.[9] Nonetheless, the SEC staff has recommended sweeping changes to the broker-dealer and investment adviser regulatory regimes, such as the above mentioned uniform standard of conduct for those providing investment advice about securities, partially based on the incomplete data proffered by the above report and other limited surveys.

We therefore believe the Commission must commit to extensive investor testing to gain a detailed, objective perspective on how to protect investors and best position these individuals to make sound investment decisions.[10] In doing so, the Commission should seek the input of a variety of stakeholders, including not only investors and prospective investors, but service

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[7] In January 2011, the Commission published a study examining the legal and regulatory duties of broker-dealers and investment advisers, as required under §913 of the Dodd-Frank Act. Several prior studies were cited therein regarding the level of understanding of the duties and obligations owed by financial professionals to their retail clients. These included a 2004 Siegel & Gale, LLC and Gelb Consulting Group focus group survey of "a few dozen investors," a 2008 SEC-commissioned report by the RAND Institute for Civil Justice (hereinafter "RAND report" or "RAND survey"), and a 2010 telephone survey conducted by the Consumer Federation of America. *See* SEC Staff, *Study on Investment Advisers and Broker-Dealers* at 95-101 (Jan. 2011).

[8] *See generally Study on Investment Advisers and Broker-Dealers*, *supra*, note 7.

[9] *See* Angela Hung, *et. al.*, Investor and Industry Perspectives on Investment Advisers and Broker-Dealers, RAND Institute for Civil Justice at xiv (2008), *available at* http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf (last visited Mar. 22, 2012).

[10] We note that the Commission examined in recent years several of these same concepts in attempting to require the provision of additional point of sale information and disclosures to investors, yet ultimately did not issue final regulations. Investor testing was a significant component of the Commission's underlying analysis, but the breadth of issues involved—particularly, as noted *infra*, with respect to disclosures associated with variable insurance products—underscores the need for additional, comprehensive testing to inform future regulatory efforts in this area. *See* Point of Sale Disclosure Requirements and Confirmation Requirements for Transactions in Mutual Funds, College Savings Plans, and Certain Other Securities, and Amendments to the Registration Form for Mutual Funds, 70 Fed. Reg. 10521, 10533-34 (Mar. 4, 2005).

providers, and legal and regulatory compliance professionals to ensure that the testing process itself adequately accounts for the totality of the information that must be considered.

In sum, we believe the Commission should not limit the focus of its inquiry to ascertaining an investor's understanding of the legal differences among financial professionals. Rather, the Commission should focus on determining the type of information an investor needs to make a sound choice regarding his or her professional financial representation. The Commission's goal for the investor should be that he or she understands the value and limits of a chosen financial professional. Investors should have the information necessary to make an informed choice.

Format and Content of Investor Disclosures. Since its inception in 1934, the Commission's fundamental mission has been to provide full and fair disclosure to investors, yet it appears that the struggle for clarity in disclosure regulation continues. The study mandated under §917 of the Dodd-Frank Act is evidence of the widely acknowledged need to depart from the practice of providing voluminous, overly complex disclosure statements to investors. SEC-commissioned studies have identified the challenges inherent in today's disclosure practices. For example, a majority of those interviewed in the RAND survey commented that "disclosures do not help protect or inform the investor, primarily because few investors actually read the disclosures," and "[t]he way that [disclosures] are written is not easily understandable to the average investor [or lack sufficient information]."[11] We do not believe this and other similar commentary undermines the utility of investor disclosure as a regulatory goal, but it does reflect the imperative of improving and simplifying the content, methods and delivery of disclosure.

Toward this end, we believe investors would benefit from a short and simple disclosure statement that is presented by financial professionals at the outset of a client relationship and clearly conveys the types of accounts and services provided, as well as the roles and responsibilities of the financial professional. This should include information about the nature of the services provided and the obligations of the service provider in his or her role, for example, any associated conflicts or contractual obligations that limit the suite of products he or she can offer. Similarly, under the rubric of product and account information, we believe that investors want and need to know basic fundamentals about their potential investment options and the pros and cons of certain products and/or investment decisions under consideration given their personal financial goals and risk tolerance.

With respect to format and delivery, the primary structural goal in the design of a disclosure statement should be to include key material information as succinctly and plainly as possible, making additional layers of information available to the investor as needed. The delivery of this information should be flexible. Retail customers should be able to access hard or electronic copies of disclosure statements and both should provide opportunities to access additional information as it is needed (through the use of hyperlinked documents or websites and/or other means).

[11] Hung, *et. al.*, *supra*, note 9, at 19-20.

As stated above, AALU members serve their clients in a multitude of ways, often including the sale of variable life insurance and annuities—both registered securities under State and Federal securities laws. Variable life insurance policies are typically recommended to secure death benefit protection for the insured's beneficiaries. These transactions involve a high degree of agent-client interaction and require comprehensive "needs analysis" to determine an appropriate range of death benefit coverage. This entails accounting for the health of the potential insured, his or her assets, current expenses, future financial needs, investment time horizon, and risk tolerance, among other factors. Similarly, the sale of variable annuity contracts, which are an attractive means of securing future retirement income, involves a considerable amount of due diligence[12] and associated interaction with prospective clients. Both products require a significant amount of disclosure to retail customers in the form of a detailed prospectus that explains how these contracts work, highlights key product features, and provides detailed information regarding product fees and charges, as well as any additional costs that may be associated with the transaction. We believe that any disclosure statements to retail investors should continue to take into account the unique characteristics of and benefits provided by these products. However, disclosure of the above information should first be simplified, and subsequently layered with additional information to ensure that the investor possesses the appropriate information at the appropriate time and that it is delivered effectively and efficiently so as to maximize its utility and benefit to the investor.[13]

Conclusion. We support the effort to improve the format, delivery, and content of investor disclosure statements. We believe that doing so should be a collaborative exercise in which regulators and marketplace stakeholders share responsibility. Investors too must share in this responsibility, striving to evaluate and better understand their own financial circumstances so that they are more prepared in their dealings with their financial professionals and regarding the investment decisions and product choices they make. To this end, investors can both be further educated and protected through disclosure documents that clearly and concisely articulate the contours of the relationship they are entering into with a financial professional, the roles and duties of that service provider, any conflicts inherent in the provision of that service, the nature of any accounts or products under consideration, and the costs associated with these services and transactions.[14] We believe the Commission must undertake extensive investor testing, in

[12] *See generally* FINRA Rule 2330 (formerly NASD Rule 2821), *supra*, note 5.

[13] We note that the Commission, in prior consideration of point of sale disclosure regulations, has acknowledged this: "[following the proposal of Rule 15c2-3, in which a single set of disclosure requirements were drafted to apply to variable insurance products as well as other covered securities,] [c]ommenters stated that the proposed point of sale forms were not well suited to illustrating [material information about these contracts]. *To be effective, required point of sale disclosures for purchases of variable insurance products should take into account the unique characteristics of those products* (emphasis added). 70 Fed. Reg. 10521, *supra*, note 10, at 10533-34.

[14] We note that FINRA is considering, in concept, rules that would generally require broker-dealers to provide written statements at the beginning of a relationship with a retail investor that would explain the types of brokerage accounts provided, as well as any conflicts associated with these services. The AALU generally supports FINRA's effort for the same reasons articulated

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collaboration with all interested stakeholders, to obtain empirical data around the information that is material to investors' decision making processes and the methods in which that information should be presented. In so doing, the Commission should take note of and account for the existing preferences of investors and their utilization of current business models in any prospective disclosure regulation.[15] We believe that any purported confusion or insufficient financial education among retail investors can be significantly mitigated through a thoughtful, objective approach to disclosure regulation that incorporates the concepts discussed herein.

We again thank the Commission for the opportunity to provide comments on this important subject and we would appreciate future opportunities to further this dialogue.

Sincerely,

David J. Stertzer
Chief Executive Officer

Footnote continued from previous page
above. *See* FINRA Regulatory Notice 10-54 (Dec. 27, 2010), *available at* http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p122361.pdf (last visited Mar. 22, 2012).

[15] The RAND report identified the presence of some degree of investor confusion in transacting with broker-dealers and investment advisers, but also noted "[d]espite this confusion…respondents reported that they are largely satisfied with the services they currently receive from financial professionals." Hung, *et. al.*, *supra*, note 9, at 87. We note that this same report provided data around this level of customer satisfaction, establishing that 74.9% of respondents were "very satisfied" when considering all types of services provided (i.e., brokerage and advisory) and an even greater number, 79.3%, were "very satisfied" with respect to their brokerage services only. *Id.* at 98.