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August 7, 2018

Submitted electronically through http://www.regulations.gov

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: **Regulation Best Interest [File Number S7-07-18]; Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the Use of Certain Names or Titles [File Number S7-08-18]; Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation [File Number S7-09-18][1]**

Dear Mr. Fields:

PFS Investments Inc. ("PFSI" or "we"), a broker-dealer and investment adviser registered with the Securities and Exchange Commission ("SEC"), is an indirect wholly-owned subsidiary of Primerica, Inc. ("Primerica"). We focus on helping middle-income families become financially independent. Our customers earn, on average, between $30,000 and $100,000 in annual household income, a category that represents approximately 50% of all U.S. households.[2] We have one of the largest and most diverse sales forces in North America with approximately 24,300 brokerage licensed representatives helping over two million middle-income customers with their investment accounts.[3] Additional information about who we are, how we help middle-income families, and

[1] Because we view the three proposed rulemakings and interpretations as interrelated, we believe it is appropriate to address our comments on the three proposals in a single, unified letter. As such, we are filing this letter in each of the three rulemaking dockets referenced above.
[2] U.S. Census Bureau, Census Population Survey 2016 Annual Social and Economic Supplement, last revised August 26, 2016. Based upon 125.8 mm households.
[3] As of December 31, 2017 (including 18,000 in the United States and 6,000 in Canada); 40% of licensed representatives are millennials, 30% of Regional Vice Presidents (RVPs) are women, 19% of RVPs are African-American and 13% of RVPs are Hispanic as of December 31, 2016. Our securities representatives generally hold Series 6 and 63 FINRA registrations, and approximately 3,400 of our registered representatives are also registered as Investment Adviser Representatives.

the importance of preserving access to financial professionals for the middle market is provided in **Appendix A** to this letter.

We commend the SEC's efforts to address the important issue of what standards should apply to broker-dealers and investment advisers when they provide investment advice and recommendations to retail investors.

We appreciate the opportunity to comment on the SEC's proposed package of regulations and interpretations that would define these standards ("Proposals"), and we share the SEC's goals of enhancing transparency, while preserving choice and access to a variety of investment products and services, including through the brokerage advice model.[4]

Primerica has commented extensively on this topic over the past several years, including to both the SEC and the Department of Labor ("DOL").[5] We have consistently requested that the SEC, as the primary federal regulator of broker-dealers and investment advisers, take the lead in addressing this issue for retail investors and savers. Over the past decade, we have seen various other regulators, including the states, insurance regulators, and most significantly the DOL, put forth their own standards purporting to address the perception that retail investors lack appropriate consumer protections. We believe this fragmented approach to regulation has resulted in significant and observable harm to investors by having the effect of reduced access and choice and increased costs for middle-income families. With the DOL "fiduciary rule" now vacated ("DOL Fiduciary Rule"),[6] the SEC has an opening to harmonize the standards across securities statutes

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[4] *See* Regulation Best Interest, 90 Fed. Reg. 21574 (proposed May 9, 2018) (to be codified at 17 C.F.R. pt. 240) (hereinafter, "Reg BI Proposal"); Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the Use of Certain Names or Titles, 90 Fed. Reg. 21416 (proposed May 9, 2018) (to be codified at 17 C.F.R. pts. 240, 249, 275 and 279) (hereinafter, "Form CRS Proposal"); Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation, 90 Fed. Reg. 21203 (proposed May 9, 2018) (to be codified at 17 C.F.R. pt. 275).

[5] We incorporate by reference our previously filed comment letters to the SEC and DOL. *See*, Letter to The Honorable Jay Clayton Re: Comment on the Standards of Conduct for Investment Advisers and Broker-Dealers (Dec. 10, 2017) (available at https://www.sec.gov/comments/ia-bd-conduct-standards/cll4-2782348-161672.pdf) (hereinafter, "SEC Comment Letter (2017)"); Letter to the Employee Benefits Security Administration Re: Request for Information Regarding DOL's Regulation Defining the Term "Fiduciary" and Related Prohibited Transaction Exemptions (Sept. 6, 2017) (available at https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00648.pdf) (hereinafter, "DOL Comment Letter (2017)"); Letter to Secretary Elizabeth M. Murphy Re: SEC Release No. 34-69013; IA-3558; File No. 4-606 (Duties of Brokers, Dealers and Investment Advisers): Request for data and other information (July 5, 2013) (available at https://www.sec.gov/comments/4-606/4606-3133.pdf) (hereinafter, "SEC Comment Letter (2013)"); Letter to Office of Regulations and Interpretations Re: Conflicts of Interest Proposed Rule (July 21, 2015) (available at https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00615.pdf) (hereinafter, "DOL Comment Letter (2015)"); Letter to the Employee Benefits Security Administration Re: Conflicts of Interest Proposed Rule (July 5, 2013) (available at https://www.sec.gov/comments/4-606/4606-3133.pdf) (hereinafter, DOL Comment Letter (2013)").

[6] Definition of the Term "Fiduciary"; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. 20946 (Apr. 8, 2016); Best Interest Contract Exemption, 68 Fed. Reg. 21002 (Apr. 8, 2016), *vacated*; *U.S. Chamber of Commerce v. DOL*, No. 3:16-cv-01476-M (N.D. Tex., Feb. 8, 2018).

that apply to all retail investor accounts and avoid the unnecessary complexities and expense that result from different standards and rulesets for individual retirement and taxable savings.

We have always advocated that the interests of investors should be put first.[7] In fact, we believe that acting in the customer's best interests is critical to our business's long-term success. Of course, the contours and details of the applicable standard, and how it is enforced by regulators or the trial bar, will have a profound impact on whether it is workable and preserves access to help middle-income Americans. The pull back from the middle-income market by many in the financial services industry as a result of the DOL Fiduciary Rule has left no doubt that regulation in this space risks severe and unintended consequences.[8]

We also have always made financial education our priority. In the communities we serve, we often teach the "how to's" of investing and encourage individuals to save for the first time. We agree that an introductory piece similar to the concept of Form CRS, layered with the disclosure obligation in Regulation Best Interest ("Reg BI"), with some important modifications detailed below, have the potential to better-educate investors to help them make important informed decisions related to achieving their financial goals.

However, our years of experience tells us that the SEC should refine the Proposals in certain key respects to avoid unnecessary complexity and uncertainty in the regulatory scheme that will not markedly assist investors and may instead encourage further abandonment by the financial services industry of middle-income investors. Our purpose is to ensure that any final regulations preserve our ability, and the ability of others, to serve middle-income Americans who tend to have smaller amounts to invest and who need and deserve access to help.

To create a workable rule that achieves our shared goals, we respectfully recommend that the SEC:

Part I: Regulation Best Interest

- Clarify the approach to addressing "financial incentives" to provide greater certainty as to how to comply with the requirements, recognizing that certainty will be necessary to dissuade the flight from the brokerage advice model.
  - Recognize that incentives are critical to motivating positive behavior such as to encourage financial representatives to help middle-income consumers with smaller amounts to invest, and clarify that there is no *per se* requirement to eliminate financial incentives so long as firms adopt reasonably designed policies and procedures to ensure recommendations are consistent with an investor's best interest.
  - Confirm that the Proposals do not prohibit or restrict broker-dealers from offering investment products that pay third-party compensation to the firm, so long as resulting conflicts are appropriately disclosed.

[7] *See, e.g.,* SEC Comment Letter (2017); DOL Comment Letter (2015).
[8] *Id.*

- Clarify and expand, with specificity, the SEC's examples of acceptable conflict mitigation techniques.

- Rationalize the SEC's preamble statements suggesting enhanced requirements may apply where an investor is "less sophisticated."

- Confirm that the care obligation for broker-dealers is consistent with current obligations under Financial Industry Regulatory Authority ("FINRA") Rule 2111.

  - Clarify how to appropriately weigh the costs and expenses of investment options when making a recommendation to a retail investor.

  - Confirm that the required level of customer diligence is consistent with current requirements under the federal securities laws.

- Revise Reg BI's recordkeeping requirements to be more workable and consistent with consumer privacy and cybersecurity laws.

Part II: Form CRS Relationship Summary and Disclosures

- Ensure that the Proposals, and particularly Form CRS, do not unintentionally create a private right of action.

- Revamp the approach to disclosure to more effectively arm investors with meaningful information and education about the differences between brokerage and advisory services without creating unnecessary legal risks and barriers for broker-dealers and investment advisers, as suggested in the concept disclosure drafts attached as **Exhibit B** to this letter.

- Restyle the Form CRS "Key Questions to Ask," so as to not incidentally expand current disclosure and other obligations.

- Modify the delivery and recordkeeping requirements for Form CRS.

Part III: Interpretation Regarding Standard of Conduct for Investment Advisors

- Refrain from adding new licensing and continuing education requirements for investment advisers.

Our experience in serving middle-income Americans has shown us that the real issue is not that their investment choices are negatively affected by conflicts, but rather that far too many have simply failed to take the steps necessary to accumulate meaningful savings. This conclusion, that there is a lack of personal savings by middle-income Americans, is borne out by research that confirms what we know anecdotally - savings is ***heavily*** skewed to higher net worth families, and everybody else needs to save more. Those families with a net worth in the bottom 50%, which would be most middle-income families, are in real financial trouble and need help.

Americans' lack of savings and poor financial literacy are inextricably intertwined with the Proposals. Research, which we present in more detail in the Appendix A to this letter, has

consistently shown that those who work with a financial representative save more than those who do not receive personal investment help. At issue here is whether a new standard will incentivize one-on-one help for these currently underserved families or instead disincentive it. We are concerned that, without the changes we suggest in this letter, the Proposals could make financial education and investment recommendations harder to obtain for these already struggling middle-income families, making a bad situation worse.

Part I

Regulation Best Interest

A. The SEC Should Refine Its Approach to Addressing Broker-Dealers' Conflicts of Interest to Provide Greater Certainty as to How Firms Can Comply

While we agree that broker-dealers should not allow their financial interests to adversely influence the recommendations they provide to their customers, we are concerned that as proposed, Reg BI's Conflicts Obligation[9] creates significant uncertainty. In particular, we are concerned with the uncertainty as to the specific conflicts a broker-dealer must mitigate or eliminate under the Proposal, the types of conflict mitigation techniques that may be effective, and at what point in time a conflict has been sufficiently mitigated. Faced with these regulatory uncertainties, and resulting enforcement risks, we are concerned that many broker-dealers, similarly to how they approached such risks under the DOL Fiduciary Rule, will merely curtail access to brokerage services in favor of the advisory model, particularly for low balance accounts. We believe that this is a material, although unintended, risk of this rule that will disproportionately harm middle-income American families.

We urge the SEC to address these concerns in the final rule, to create a more workable approach to addressing conflicts by providing predictability and certainty.

1. *The Requirement to Disclose and Mitigate or Eliminate Conflicts Arising from "Financial Incentives" Goes Beyond the Standard that Applies to Investment Advisers and Thus Results in a Preference for Advisory Models over Brokerage*

Issue: The current formulation of the conflicts obligation inappropriately, and we believe unintentionally, produces a DOL Fiduciary Rule-like outcome where advisory models will be favored over brokerage models.

Proposed Solution: To avoid further harming these middle-income investors, we urge the SEC to clarify that broker-dealers can effectively address all material conflicts, including those that arise from "financial incentives," by providing a full and fair disclosure and obtaining customer consent to the conflicts.

Comment: By requiring broker-dealers to disclose and *mitigate or eliminate* conflicts resulting from "financial incentives," the SEC has proposed a standard that is ***actually higher*** than the standard that applies under the Advisers Act. The SEC's current formulation of the conflicts

[9] *See* Proposed Sec. Exch. Act Rule 15l-1(a)(2)(i).

obligation thus inappropriately, and we believe unintentionally, preferences advisory models over brokerage models.

We note, first, that the consumers we serve often do not have enough financial resources to meet the minimum account sizes required of most advisory programs. More importantly, advisory programs are generally not appropriate for investors who are typically buy-and-hold investors. Understanding that it is not the intent of the SEC to incent, for regulatory purposes, a movement of accounts from brokerage to advisory, we would emphasize that if the SEC does not apply a business model neutral conflicts standard, the Proposal is likely to have this effect. Specifically, if not neutralized, the Proposal is likely to have the same consequences as the DOL Fiduciary Rule – a favoring of, and an accelerated migration of, assets to advisory models.[10] Our proposed solution, that conflicts can be addressed through disclosure and consent, is a long-standing principle of the common law of agency and trusts, as well as the federal securities laws.

Broker-dealers are already subject to numerous rules and obligations that are specifically intended to address the potential that a conflict could result in "bad" recommendations being provided to investors. For example, broker-dealers and their registered personnel are subject to rigorous registration, testing, continuing education, and recordkeeping requirements.[11] Most importantly, FINRA rules and the federal securities laws require broker-dealers to closely supervise their representatives for compliance with the federal securities laws, including the anti-fraud provisions of the Securities Exchange Act of 1934, among other rules.[12] Additionally, under current law,

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[10] *See*, Michael Wursthorn, *Merrill Lynch to End Commission-Based Options for Retirement Savers*, Wall St. J., Oct. 6, 2016, https://www.wsj.com/articles/merrill-lynch-to-end-commission-based-options-for-retirement-savers-1475784928; Michael Wursthorn, *Merrill's Fiduciary Alternative Would Affect Limited Number of Clients*, Wall St. J., Mar. 10, 2017 ("While Merrill Lynch is considering offering an alternative product, such a product would "carry heavy restrictions. … The people familiar added that there is no guarantee an alternative product will be created."); Michael Wursthorn, *Edward Jones Shakes Up Retirement Offerings Ahead of Fiduciary Rule*, Wall St. J., Aug. 17, 2016, http://www.wsj.com/articles/edward-jones-shakes-up-retirement-offerings-ahead-of-fiduciary-rule-1471469692; Greg Iacurci, *State Farm, citing DOL fiduciary rule, cuts agents from mutual fund and variable annuity sales*, Investment News, Sept. 12, 2016, http://www.investmentnews.com/article/20160912/FREE/160919992/state-farm-citing-dol-fiduciary-rule-cuts-agents-from-mutual-fund?AID=%2F20160912%2FFREE%2F160919992; Michael Wursthorn, *J.P. Morgan Moves Ahead With Plan to Drop Commissions in IRAs*, Wall St. J., Mar. 13, 2017, https://www.wsj.com/articles/j-p-morgan-moves-ahead-with-plan-to-drop-commissions-in-iras-1489420979; Grete Suarez, *Capital One will eliminate commissions on IRAs*, Investment News, Nov. 16, 2016, http://www.investmentnews.com/article/20161116/FREE/161119951/capital-one-will-eliminate-commissions-on-iras; Investment News Staff, *Commonwealth Financial eliminates commission-based retirement products in wake of DOL rule*, Investment News, Oct. 24, 2016, http://www.investmentnews.com/article/20161024/FREE/161029956/commonwealth-financial-eliminates-commission-based-retirement; Kenneth Corbin, *Stifel's fiduciary solution for commissions*, OnWallStreet, Nov. 3, 2016, https://www.onwallstreet.com/news/stifels-fiduciary-solution-for-commissions.

[11] *See*, *e.g.*, NASD Rules 1031 and 1021 (requiring "representatives" and "principals," respectively, to register with FINRA and pass the corresponding qualification examinations); FINRA Rule 1250 (requiring firms to design and administer firm-element continuing education programs for their registered personnel and to ensure their registered personnel satisfy applicable regulatory-element continuing education requirements); FINRA Rule 4511 (requiring FINRA members to make and preserve books and records as required under various FINRA rules, the Exchange Act, and applicable Exchange Act rules, including in a format and media that complies with Exchange Act Rule 17a-4); FINRA Rule 4513 (requiring firms to keep and preserve written customer complaints); FINRA Rule 4530 (requiring reporting to FINRA of written customer complaints).

[12] *See*, *e.g.*, FINRA Rule 3110 (regarding a FINRA member's supervisory obligations, which include, among others, requirements to review certain correspondence and internal communications; to review all of the member's securities

customers have recourse if they have received recommendations falling short of applicable standards that result in losses—they can pursue class actions and seek redress through arbitration.[13] Moreover, the SEC and FINRA can, through enforcement actions, sanction broker-dealers for providing advice that is not appropriate for the investor.[14] These are powerful motivating factors that currently encourage firms to continually review and modify their compliance and supervision programs and identify and address potential bad actors. To comply with the assemblage of these laws and regulations, and to mitigate litigation risks, firms such as ours have in place well-functioning and rigorous policies, procedures, and technological tools to see that products offered are carefully vetted as suitable for clients and transactions can be monitored and supervised for variances.

To this, Reg BI would add yet another level of protection for investors that also weighs in favor of a disclosure and consent-based approach to conflicts. Specifically, under Reg BI, broker-dealers would be subject to an SEC-articulated and SEC-enforceable duty of care.

We understand that the SEC's intention is to address broker-dealer conduct that is particularly egregious, but we believe concerns here may be overstated and are largely based on anecdotal evidence of misconduct as opposed to empirical data and facts.

We are also concerned that the SEC's approach to addressing conflicts as presented in the Proposal was influenced by the DOL's rulemaking, which prior to being vacated, materially affected retail brokerage, and by the fact that any SEC rule in this area would have needed to co-exist with the DOL's more restrictive approach. In any case, we believe the SEC can accomplish its goals by adopting an enhanced and more effective disclosure-based regime to addressing conflicts coupled with an SEC-defined care obligation. We believe this is critical to preserving the brokerage advice model and will provide firms with flexibility to adopt a risk-based approach to identifying what additional steps, if any, are needed to address particular conflicts inherent in their particular business model. To do otherwise is to create an uneven playing field tilted in favor of investment

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transactions (including procedures reasonably designed to identify trades that may violate the provisions of the Exchange Act, Exchange Act rules, and FINRA rules prohibiting insider trading and other manipulative and deceptive devices); to capture, acknowledge, and respond to all written customer complaints; and to conduct internal inspections of the member's offices); FINRA Rule 2010 (requiring members to "observe high standards of commercial honor and just and equitable principles of trade"); FINRA Rule 2020 (prohibiting members from effecting transactions in, or inducing the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance); FINRA Rule 2121 (acknowledging that firms are "entitled to a profit" when trading with customers as principal, so long as prices are "fair" considering the relevant circumstances," and requiring that commissions charged by firms for agency transactions be "fair," taking into account all relevant circumstances); Sec. Exch. Act § 15(b)(4)(E) (authorizing the SEC to take disciplinary action against broker-dealers for certain failures to reasonably supervise with a view to preventing violations of the various federal securities laws).

[13] *See*, *e.g.*, FINRA Rule 12000 Series (the Customer Code of Arbitration, which governs arbitrations between investors and broker-dealers or their representatives); Sec. Act § 12(a)(2) (providing a cause of action for damages or rescission as a result of material misstatements or omissions made by any person (i) who offers or sells a security by means of a prospectus or oral communication that includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and (ii) who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission); Sec. Exch. Act § 10(b); 17 C.F.R. 240.10b-5.

[14] *See*, *e.g.*, Sec. Act § 17(a); Sec. Exch. Act § 10(b); 17 C.F.R. 240.10b-5; FINRA Rule 2111; FINRA Rule 2010.

advisers and against broker-dealers, an outcome the DOL Fiduciary Rule was clearly driving towards. As brokerage has historically been a preferable and cost-effective way of providing middle-income Americans access to financial education and investments, we fear that changes here could harm these small balance account investors who are the most in need of access to the brokerage model.

2. *What Is a "Financial Incentive" Conflict?*

Alternative Solution: If the SEC determines to reject our proposed solution above, then we urge the SEC to clarify, with specificity, the Conflicts Obligation framework so that firms have greater certainty about what specific conflicts are required to be disclosed, what conflicts must be mitigated and what conflicts must be eliminated entirely.

Comment: In particular, the SEC should expressly define "financial incentive" in the rule, and provide a series of examples of conflicts that ***do*** and ***do not*** arise from financial incentives.[15] But, as not all firms serve the same market segments, their particular fees, compensation programs, registered representative compensation, incentive programs, and product mixes will differ, and we ask that the SEC be mindful and not apply an overly prescriptive one-size fits all approach. Again, we note that broad reaching prescriptive rules like the DOL's Fiduciary Rule resulted in reductions and restrictions for the retail market in general, and a material pull back from the small account market in particular.

As proposed, Reg BI does not expressly define "financial incentive," and the Proposal makes numerous conflicting statements about particular financial incentive conflicts that serve to add to the uncertainty.[16] Broker-dealers need to know the rules of the road so that they can design and maintain effective compliance programs that appropriately address the conflicts inherent in their particular business models consistent with Reg BI. Without this certainty, Reg BI's conflicts obligation will serve as a potential enforcement booby-trap for firms and (unless the potential for a private right of action under Form CRS is addressed as discussed in Section II.A. below) will open the door for the plaintiff's bar to file class actions based on these unclear standards. This also runs the risk that state courts could define 50 different standards. Alternatively, faced with these potential uncontrollable risks, firms may, as they did in response to the DOL Fiduciary Rule,

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[15] Furthermore, the SEC should clarify how a broker-dealer might satisfy its written disclosure obligation where its associated persons may be "unconsciously" inclined to make a particular conflicted recommendation. The SEC's citation to *SEC v. Capital Gains Research Bureau, Inc.* on this point does little to provide meaningful guidance in a proposed disclosure regime that we believe differs from that under the Advisers Act. *See* Reg BI Proposal, n. 198 at 21602 (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191-92, 194 (1963)).

[16] As an example, with respect to differential compensation, the Reg BI Proposal makes potentially inconsistent statements, stating that the conflicts obligation:

- requires that the broker-dealer's financial incentives not be the "predominant motivating factor behind the recommendation" (*i.e.*, self-enrichment, self-dealing, or self-promotion), which suggests a firm's financial incentives can be a secondary factor (*i.e.*, no need to eliminate or mitigate a conflict just because of a financial incentive).
- does not prohibit differential compensation per se.
- views differential compensation as a material conflict arising from financial incentives that a broker-dealer must eliminate or mitigate.

This results in three inconsistent approaches for differential compensation: (1) differential compensation is permitted, subject to disclosure; (2) differential compensation is permitted, but incentives must be structured to mitigate the conflicts; or (3) differential compensation is not permitted and must be eliminated.

simply view the advisory model, with its more established rules and more flexible approach to addressing conflicts, as a safer place to serve their customers—again at the expense of small balance account customers.

When defining "financial incentive," the SEC should keep in mind that requiring a broker-dealer to do ***more than*** disclose the conflict puts broker-dealers at a disadvantage vis-à-vis investment advisers, particularly as compared to non-discretionary advice models. As such, we believe the SEC should focus on the types of financial incentives that have been proven to harm (rather than benefit) investors, and the SEC should support its approach with evidence. Additionally, the SEC should keep in mind the current protections already built into the brokerage regulatory regime (see Section I.A.1 above) and take into account that these protections are *already* calibrated to mitigate brokerage conflicts and to prevent the types of activities that have proven to be harmful to retail investors in the past.

Issue: The lack of clarity around whether and how the Conflict Obligations apply at the firm level puts the brokerage model at risk.

Proposed Solution: Expressly limit the definition of "financial incentives" to conflicts that operate on financial professionals, rather than at the firm level, recognizing that a broad definition that extends to the firm level would be harmful to the brokerage model without adding meaningful investor protections.

Comment: We believe a workable approach would be for the SEC to define "financial incentive" to be limited to financial incentives for registered representatives that, without appropriate mitigation, would reasonably be expected to incline the registered representative to make a recommendation that is harmful to the customer. Though we do not believe the SEC is beholden to concepts from the vacated DOL Fiduciary Rule in crafting its standards, we note that even the DOL limited its requirement to mitigate conflicts in the Best Interest Contract Exemption to conflicts that operate on financial professionals, providing financial institutions with flexibility as to how to address conflicts at the firm level.

We are concerned that defining "financial incentives" in an overly broad fashion to include those that operate at the firm level would be unnecessarily harmful to the current brokerage model. Given the transaction-based nature of brokerage compensation structures and market pressures on current commission rates, broker-dealers depend on compensation and support from third parties, including investment product sponsors, to support their platforms and current business models. Compensation and support come in different forms, including revenue sharing, sub-TA and omnibus recordkeeping fees for administrative services provided to investment products, and conference and training program sponsorship and support. This compensation is not only fair compensation, but also recognizes the different types of services provided to customers and services provided to the investment products available on the platform. These relationships and compensation streams are critical for firms to be able to maintain their current business models, including the ability to train and appropriately motivate their sales forces. As shown by the partial implementation of the DOL Fiduciary Rule, changes here will have a material, and most likely adverse, effect on the current brokerage model. We ask that the SEC study and fully understand the effects that an overly broad rule will have on current operations before finalizing this rule.

In this regard, as shown from our experience implementing the DOL Fiduciary Rule, it just was not feasible to level these payments across all product sponsor and types or even to bring third-party compensation to the firm within narrow ranges. To do so would require much greater coordination among the product manufactures (*i.e.*, the mutual fund and insurance companies, in our case), which we believe would have material implications on compliance with anti-trust rules. Moreover, we do not believe we, nor most other distributors, have the negotiating leverage to demand the same firm level compensation structure and rates – nor wholesaler commitments – across product sponsors on their platforms. At the same time, as this compensation is not shared with their representatives, who thus have no direct financial incentive to sell one product over another as a result of the third-party payments we receive, we do not believe that these types of arrangements are likely to result in harmful recommendations to investors.

Accordingly, we are pleased that the SEC recognizes that compensation arrangements with third parties are important for many broker-dealers.[17] But the SEC also suggested that "heightened mitigation measures, including enhanced supervision, may be appropriate in situations … where the compensation is less transparent (for example, a payment received from a third party or built into the price of the product or a transaction versus a straight commission payment) …."[18] We believe the SEC should clarify that, so long as this compensation is adequately disclosed in accordance with FINRA rules, there is no additional requirement for firms to mitigate these firm-level conflicts where registered representatives do not directly receive any portion of the third-party payments.

3. *The SEC Should Recognize That Sales Contests, Trips, Prizes, Awards, and Similar Bonuses Can Be Used to Incentivize Positive Behavior and Clarify There Is No Per Se Requirement to Eliminate Such Incentives*

Issue: The Reg BI Proposal undermines the public policy goal to increase financial education and savings by casting doubt on whether bonuses, awards, and non-cash compensation incentive programs can be properly managed.

Proposed Solution: Expressly clarify that Reg BI does not require bonuses, awards, non-cash compensation incentives, or any particular financial incentives, to be eliminated, but rather permit them where the incentives are not tied to a particular investment product and the firm appropriately supervises registered representatives as they approach thresholds for award eligibility.[19]

Comment: The Reg BI Proposal states that sales contests, trips, prizes, and other similar bonuses that are based on sales of certain securities or accumulation of assets under management "may be more appropriately avoided in their entirety for retail customers or for certain categories of retail customers (*e.g.*, less sophisticated retail customers)."[20] While we generally agree that sales contests and non-cash compensation programs should not improperly differentiate among different specific investment products, we do not believe the SEC intended to prohibit incentives to

[17] Reg BI Proposal at 21620.
[18] *Id.* at 21620-21.
[19] This approach would appropriately align Reg BI with FINRA's rules permitting the use of non-cash compensation. *See, e.g.*, FINRA Rule 2341(l)(5)(d) (for investment company securities); FINRA Rule 2320(g)(4)(D) (for variable insurance contracts).
[20] *Id.* at 21621.

encourage registered representatives to engage in positive behaviors, such as seeking (and reaching out to) potential new customers and encouraging customers to save and invest more assets.

It should not be presumed that all such incentives drive negative behavior. To the contrary, we believe that these incentives are critical to ensuring access to education and investments for middle-income investors. Numerous studies suggest that non-cash compensation programs and performance-based bonus programs are a valuable and powerful tool to motivate individuals to engage in positive behavior in various industries.[21] They also are widely used across industries and well-accepted. One study indicates that over 74% of U.S. businesses use non-cash incentives and 46% of those businesses offer travel as rewards.[22] The positive motivational impact of these types of non-cash incentives has been shown to be more effective than cash awards.[23] Incentive travel, in particular, has been shown to foster a strong sense of corporate culture within an organization.[24] Consistent with our experience, another study shows that the reward of travel is not simply the extrinsic reward of the trip itself, but also the networking and learning opportunities and intrinsic rewards such as feelings of accomplishment and public recognition.[25] Moreover, incentives have been shown to improve results—not just for the firms that use them, but also for the customers they serve. For example, in the field of medicine, one study showed that financial incentives provided to physicians to improve patient experience resulted in significant improvement of communication, care coordination, staff interaction and patient care experiences, particularly for physicians that had low base line performance.[26]

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[21] *See, e.g.,* Jeanie Casion, *The Right Remedy: A Sales Incentive Case Study*, Incentive Mag., June 7, 2011, http://www.incentivemag.com/article.aspx?id=7268 ("Incentive programs are the primary way that our company is able to encourage the behaviors that are essential to not only successfully launching a product but also sustaining its market share trajectory"); Scott A. Jeffrey, *Justifiability and the Motivational Power of Tangible Noncash Incentives*, Mar. 31, 2009, https://www.researchgate.net/publication/232963008_Justifiability_and_the_Motivational_Power_of_Tangible_Noncash_Incentives (concluding that non-cash rewards were more powerful motivators than equivalent cash rewards).

[22] *See* Steve Bova & Kevin M. Hinton, *FICP and SITE Weigh In on Proposed DOL Fiduciary Rule*, INCENTIVEWISE BLOG (Apr. 6, 2016, 2:17 PM), https://www.siteglobal.com/blog/ficp-and-site-weigh-in-on-proposed-dol-fiduciary-rule-impact ("Any reduction in incentive travel opportunities may also reduce the number of face-to-face meetings where financial services employees can receive in-person education to develop advanced skills, learn about new regulations, and develop professionally.").

[23] *See Conscious and Unconscious Reward Preference & Choice: A Biometric Experiment*, INCENTIVE RESEARCH FOUNDATION (Nov. 28, 2017), http://theirf.org/research/conscious-and-unconscious-reward-preference-choice-a-biometric-experiment/2328/. *See also* Bill Hastings, Julia Kiely & Trevor Watkins, *Sales Force Motivation Using Travel Incentives: Some Empirical Evidence*, JOURNAL OF PERSONAL SELLING & SALES MANAGEMENT (Oct. 24, 2013), https://www.tandfonline.com/doi/abs/10.1080/08853134.1988.10754490; Scott Jeffrey, *Justifiability and the Motivational Power of Tangible Noncash Incentives*, HUMAN PERFORMANCE (Mar. 2009), https://www.researchgate.net/publication/232963008_Justifiability_and_the_Motivational_Power_of_Tangible_Noncash_Incentives.

[24] Pauline J. Sheldon, *The Demand for Incentive Travel: An Empircal Study*, JOURNAL OF TRAVEL RESEARCH (April 1995), http://journals.sagepub.com/doi/abs/10.1177/004728759503300404.

[25] *Id.*

[26] *See* Hector P. Rodriguez, PhD, MPH, Ted von Glahn, MS, Marc N. Elliott, PhD, William H. Rogers, PhD & Dana Gelb Safran, ScD, The Effect of Performance-Based Financial Incentives *on Improving Patient Care Experiences: A Statewide Evaluation*, FINANCIAL INCENTIVES AND PATIENT CARE EXPERIENCES (Oct. 14, 2009), https://link.springer.com/content/pdf/10.1007%2Fs11606-009-1122-6.pdf.

PFSI currently sponsors programs that reward our representatives with cash and non-cash compensation to incentivize them to reach out to potential and existing customers and encourage them to save and invest more assets, which we believe should be viewed as a necessary policy objective to address the savings crisis. This is in large part a material aspect of our mission to help educate and "nudge[27]" middle-income Americans to make the right choices for their financial futures. We note that our programs are not tied to sales of any particular product, but rather are based on the amount and growth of customer assets for which our representative is responsible. We firmly believe that with the proper alignment of the interests of the customer and the representative, everyone benefits.

In our experience, incentive programs are essential to encourage and recognize legitimate business conduct that, in many ways, is essential to providing access to financial services for middle-income Americans. Specifically, these programs encourage representatives to reach out to prospective customers to encourage them to open an account and start saving and investing for their futures. We have found that the best way to get middle-income Americans to save is for our representatives to actively reach out to them and in many cases sit at their kitchen table to educate them on the benefits of saving for their futures. Otherwise, the distractions and competing priorities they face in their daily lives will result in them never taking that initial step towards their financial security, which seems to elude so many. As our experience shows, in-person outreach is by far more effective than over the phone or via computer, at helping families make positive decisions about managing their own money. Too often middle-income families have "too much month at the end of the money," and our sales force needs to be incentivized and recognized for helping these families improve their financial well-being. Programs that encourage the dissemination of financial education and savings are important and powerful means to produce positive financial outcomes for these families.

Additionally, firms, including us, rely on these types of programs to advance team-building and to incent training. These are critical to both driving business success and ensuring that representatives have the tools and knowledge to deliver appropriate levels of service to retail customers. Moreover, FINRA, the SEC, and the North American Securities Administrators Association ("NASAA") have each demonstrated their support of these programs. FINRA even proposed a new rule, as recently as 2016, to expand the availability of such programs, subject to certain conditions.[28]

[27] Richard H. Thaler and Cass R. Sunstein, *Nudge: Improving Decisions About Health, Wealth, and Happiness*, Penguin Bks. (2009).

[28] *See*, *e.g.*, Proposed FINRA Rule 3221 (proposing to eliminate the current non-cash compensation rules that apply in the context of investment company securities, variable insurance contracts, direct participation programs, and public offerings, and to replace them with a similar framework that would apply in connection with the sale of *any* security, such that, *e.g.*, sales contests would be permitted if: (1) based on the total production of associated persons with respect to *all* securities distributed by the member and not only product-specific contests; and (2) not based on conditions that would encourage an associated person to recommend particular securities or categories of securities) (also codifying existing guidance regarding the permissibility of certain travel for training and education); FINRA Reg. Notice 16-29 (Aug. 2016) (regarding proposed FINRA Rule 3221); Letter to Marcia E. Asquith Re: FINRA Regulatory Notice 16-29 Gifts, Gratuities and Non-Cash Compensation Rules, NASAA, Sept. 30, 2016, http://www.finra.org/sites/default/files/16-29_NASAA_comment.pdf (supporting FINRA's proposed Rule 3221). The SEC approved each FINRA rule that currently permits non-cash compensation, thereby finding the rules to be sufficient for the protection of investors.

We recognize that, though our incentives motivate positive behavior that advantages the middle-income communities we serve, at the same time they are susceptible to creating conflicts that can cause negative behavior. To mitigate conflicts, our incentive programs are not contingent on sales of any particular product or the product of any particular product sponsors. We focus on total production. To address the concern that incentives could encourage unnecessary trading in an account, we have structured our supervision program to aggressively identify and address potential instances of churning or recommendations for non-suitable investments. We also implement heightened supervision and surveillance procedures as a representative nears an incentive threshold to help determine if the incentive is causing the representative to provide advice that is harmful to the customer. Unfortunately, Reg BI, as proposed, leaves us uncertain as to what would be required to satisfy its requirement to "mitigate" these conflicts, and even as to whether Reg BI prescribes elimination of them entirely.

We believe the types of incentive programs we provide, structured as they are to mitigate conflicts, are entirely consistent with Reg BI's goal of improving the quality of advice investors receive through the brokerage channel and that they do not introduce any additional conflicts, beyond those already inherent in the transaction-based brokerage model. We therefore urge the SEC to clarify that, with proper supervision and disclosure consistent with FINRA requirements, bonuses, awards, non-cash compensation incentives, and other appropriate financial incentive programs are expressly permitted under Reg BI.

If the SEC effectively prohibits or materially restricts these types of programs, firms like ours may have less ability to motivate and incentivize their representatives to provide face-to-face personal services to the middle-income America and small balance investors. Without this change, the middle-income market segment may ultimately be abandoned to passive execution only platforms and robo-advice without human interaction, materially reducing the likelihood that their resources will be shifted from spending today towards savings for the future.

4. The SEC Should Not Differentiate "Less Sophisticated" Retail Customers from Other Retail Customers

Issue: The SEC's statements in the Proposals regarding the additional protections broker-dealers should afford "less sophisticated" retail customers could create a sub-class of retail customers that broker-dealers would have to identify based on subjective and poorly defined criteria, and potentially further restrict access to help with saving and investing for customers who need it most.

Proposed Solution: Avoid creating this differentiation as the potential customer harms seem to clearly outweigh any articulated benefit or effective customer protection.

<u>Comment</u>: Specifically, the SEC suggests that "heightened mitigation measures, including enhanced supervision, may be appropriate in situations where the retail customer displays a *less sophisticated* understanding of securities investing generally or the conflicts associated with particular products involved,"[29] and that certain financial incentives "may be more difficult to mitigate for categories of retail customers (*e.g.*, *less sophisticated* retail customers)."[30]

First, it is unclear what "less sophisticated" means and whether the intent is that sophistication be judged on an objective or subjective standard. We assume the SEC is referring to retail customers who have little investment experience or would be incapable of independently evaluating the risks of recommended transactions or investment strategies. However, the SEC has not stated this to be the case and it is unclear how this is to be measured in practice and where to set the threshold for sophistication. We note that FINRA has provided guidance consistent with our assumption in discussing the suitability obligations of broker-dealers recommending certain complex products,[31] but FINRA's guidance is not entirely clear in terms of practical application.

Seemingly easy proxies for investment sophistication are wealth and education, but a few examples may illustrate why that approach does not work well:

- ***Professional athletes.*** In 2009, Sports Illustrated reported that 78% of NFL players declare bankruptcy within two years of leaving the game.[32] Later studies indicate this percentage may be much lower—1.9% after two years, and 15.7% after twelve years. Examples of players with multi-million dollar contracts who lose it all abound in other sports as well. For example, Antoine Walker earned $108 million while playing for the NBA, but declared bankruptcy with net liabilities of $7 million (thanks in part to bad real estate investments). Sheryl Swoopes, who earned an estimated $50 million playing basketball, also declared bankruptcy and admitted, "I didn't surround myself with the right people. I got in a position where it was like, 'Oh, wow, what happened?[33]'" Jack Clark filed for bankruptcy in the middle of his $8.7-million-dollar contract with the Red Sox. These stories show that income does not always correlate with financial acumen and investment sophistication.

- ***Doctors and lawyers.*** Doctors and lawyers are well-educated with advanced degrees and are typically high-income earners compared to other professions. But, here, education and income do not always translate to investment sophistication. A *New York Times* article highlighted this suggesting that, in some cases, education and intelligence in their profession lead lawyers and doctors to think they will have the same success in investing

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[29] Reg BI Proposal at 21620-21.

[30] *Id.* at 21621.

[31] *See*, *e.g.*, FINRA Reg. Notice 12-03 (Complex Products), at 8 (Jan. 2012) ("In recommending complex products, firms are encouraged to adopt the approach mandated for options trading accounts, which requires that a registered representative have 'a reasonable basis for believing, at the time of making the recommendation, that the customer has such knowledge and experience in financial matters that he may reasonably be expected to be capable of evaluating the risks of the recommended transaction, and is financially able to bear the risks of the recommended position in the' complex product.").

[32] *See* Pablo S. Torre, *How (And Why) Athletes Go Broke*, SPORTS ILLUSTRATED, Mar. 23, 2009, https://www.si.com/vault/2009/03/23/105789480/chow-and-why-athletes-go-broke.

[33] Liz Robbins, *Swoopes Says She Is Gay, and Exhales*, N.Y. Times, Oct. 27, 2005.

and saving with mixed results.[34] Thus, formal education may not always correlate with financial acumen and investment sophistication.

- ***Financial advisors.*** All of our representatives have taken extensive courses and training on investment products and strategies and hold various FINRA series licenses. At the same time, many do not have college degrees and as they start to build their careers with us are themselves middle-income Americans. Again, formal education and income may not always correlate with financial acumen and investment sophistication.

These examples show the challenges broker-dealers (and the financial services industry, as a whole) face when assessing a customer's investment sophistication. Requiring this differentiation, particularly without clarification on how to assess sophistication, thus creates significant compliance uncertainty and risk.

Second, differentiating customers based on investment sophistication could harm less sophisticated investors by curtailing their access to certain types of advice, products, strategies, and transactions. Many middle-income Americans engage with firms like us for the specific purpose of leveraging our representatives' knowledge and understanding of the financial markets and the products that would serve their financial needs. This is even more the case for investors with less understanding of investments, as they are less likely to be able to effectively structure their investment program without help.

The SEC's positions on "less sophisticated" retail customers would effectively create a new sub-class of retail customers to whom broker-dealers would have to implement "heightened mitigation measures, including enhanced supervision." Of course, regulatory requirements for heightened mitigation and other special procedures means heightened costs—and legal risk—for the firms tasked with implementing them.

As most recently experienced with the DOL Fiduciary Rule, these uncontrolled risks generally lead firms to cut off or severely restrict access to services and product choices for their customers. We urge the SEC to avoid creating this differentiation as the potential customer harms seem to clearly outweigh any articulated benefit or effective customer protection.

5. The SEC Should Clarify and Expand Its Examples of Conflict Mitigation Techniques

<u>Issue</u>: Reg BI's construct to "mitigate or eliminate" financial incentives is vague and inconsistent, leaving too much uncertainty as to how to comply.

<u>Proposed Solution</u>: Provide greater certainty on how firms can comply with the requirement to "mitigate or eliminate" financial incentives by providing clear examples and expressly stating conflicts that need to be addressed and how the mechanism in an example accomplishes this.

<u>Comment</u>: We appreciate that the SEC sought to adopt a principles-based approach that would permit firms flexibility to design conflicts mitigation programs that are adapted to their particular

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[34] *See* Paul Sullivan, *Money Advice for Doctors and Lawyers and the Rest of Us*, N.Y. Times, Mar. 29, 2013, https://www.nytimes.com/2013/03/30/your-money/money-advice-for-doctors-and-lawyers.html.

business models, and we are pleased that the SEC provided some examples of conflicts mitigation techniques that could be acceptable under the Proposals. However, we note that firms, due to the risks of regulatory enforcement, put a lot of weight on "examples" when designing regulatory compliance programs. In many instances, regulatory examples are viewed as "safe harbors" and deviations from them are generally discouraged by firms' risk management. Applying our proposed solution would go a long way toward helping firms develop their individual programs without being tied to the specific facts of the example.

Below, we provide excerpts from Reg BI's examples and discuss how they might be clarified.

- ***"avoid compensation thresholds that disproportionately increase compensation through incremental increases in sales"*** – The SEC should clarify what it means by "disproportionately increase compensation," and state what is the specific issue that this is tied to. The SEC should confirm that increases in compensation due to commission-based sales (*e.g.*, traditional compensation grids) are permitted, subject to disclosure. Also, the SEC should confirm that enhanced supervision tied to material increases in compensation could satisfy the mitigation requirement as it could be used to ensure that recommendations are not adversely affected by the compensation arrangement.

- ***"minimize compensation incentives for employees to favor one type of product over another, proprietary or preferred provider products, or comparable products sold on a principal basis – for example, establishing differential compensation criteria based on <u>neutral factors</u> (e.g., the time and complexity of the work involved)"*** – It is unclear how this could be implemented in a way that provides meaningful certainty. In particular, it is unclear how fee differences could be supported by "neutral factors," and there is no ability to anticipate what the SEC, or state courts, may consider, from time to time, to be a valid "neutral factor," particularly when prices are set by third-party manufacturers based on market factors. We also note that, in attempting to design policies and procedures to comply with the DOL Fiduciary Rule, many firms spent significant resources on analyzing "neutral factors" that could justify differences in compensation for different investment products. These so-called "time and motion" studies considered the time and effort to sell a product, licensing requirements and other relevant criteria that could support differences in compensation. However, many firms remained concerned that, whatever approach they adopted, and no matter how rigorous an analysis they conducted, a regulator or private litigant could later challenge them for failing to sufficiently mitigate their conflicts. We also understand that certain members of the DOL staff have informally questioned the viability of such time and motion studies in meeting the neutral factors analysis, leaving uncertainty on how to effectively implement the approach at all.

  To avoid confusion, we urge the SEC to remove "neutral factors" from its examples of conflict mitigation techniques.

- ***"eliminating compensation incentives within comparable product lines (e.g., one mutual fund over another)"*** – The SEC should clarify that product category is not necessarily an appropriate distinguishing factor for representative compensation differentials. For example, mutual funds may fall within different asset classes or strategies that justify greater or lesser compensation (*e.g.*, equities vs. fixed income; active vs. passive; domestic

vs. international). Firms should be permitted to adopt reasonably designed supervisory procedures to prevent these incentives from resulting in recommendations that are not appropriate for investors, so long as the related conflicts are disclosed.

- ***"implement supervisory procedures to monitor recommendations that involve the rollover or transfer of assets from one type of account to another (such as recommendations to rollover or transfer assets in an ERISA account to an IRA, when the recommendation involves a securities transaction)"*** – The SEC should confirm that the Reg BI conflict obligation for rollovers and account transfers are consistent with, and no broader than, current requirements under the securities laws, including FINRA Notice 13-45 and SEC positions on churning and anti-churning. Noting that "rollovers" and IRA transfers have garnered much attention in recent years, we request clarification as to whether the SEC has identified special or additional concerns with these types of transactions or accounts. Middle-income America relies on these types of accounts for a large part of their retirement saving. Although we note the importance of these types of accounts, we believe all individual customer assets are essential and should all be subject to the same standards and protections. We urge the SEC to not differentiate the treatment of individual retirement assets and taxable assets, but rather to treat them all under a single ruleset for retail investors.

  We think there is ample support for harmonizing the rules for individual retirement assets and taxable accounts after the disconnected approaches resulting from the DOL Fiduciary Rule. The result of partially implementing that rule resulted in much investor confusion and client irritation as firms tried to explain why different rules applied to different accounts.

- ***"adjusting compensation for registered representatives who fail to adequately manage conflicts of interest"*** – Most broker-dealers already have policies and procedures to address misconduct of their registered representatives, including for failing to meet applicable standards of conduct. Disciplinary procedures include ineligibility for recognition clubs and non-cash awards, mandatory training, and enhanced supervision. We request that the SEC provide additional color as to what specific issues they intend to address and how current arrangements may not be sufficient. We are further concerned that compensation clawbacks can raise irreconcilable conflicts with state wage and hour laws and request that the SEC study these potential types of employment law issues prior to providing examples that could be interpreted as requiring such adjustments.

- ***"limiting types of retail customers to whom a product, transaction or strategy may be recommended (e.g., certain products with conflicts associated with complex compensation structures)"*** – It is unclear what the SEC means by a "complex compensation structure." We urge the SEC to confirm that this is not intended to encompass traditional compensation structures associated with mutual funds and variable annuities. We are also concerned that focusing on what types of products can be sold to particular classes or types of customers raises the same issue we discussed above regarding dealings with "less sophisticated" customers.

In addition, the SEC should confirm that the references cited herein to the preamble of Reg BI regarding mitigating conflicts apply to representative level conflicts, and are not intended to address firm level conflicts. As we discussed at Section I.A.2. of this letter, these requirements applied to firm level conflicts would unnecessarily be harmful to the current brokerage model.

The SEC also should confirm that guidance provided by FINRA in its Report on Conflicts of Interest relating to these types of conflicts would apply for purposes of Reg BI and that the examples of effective supervision and surveillance techniques provided in that report could also be deemed effective for purposes of conflict mitigation under Reg BI, if reasonably designed and implemented. For example, in the Report on Conflicts of Interest, FINRA highlighted, as possibly effective mitigation techniques, that some firms perform specialized surveillance as their registered representatives approach thresholds that move the representative to a higher payout percentage in a firm's compensation grid, qualify a representative to receive a back-end bonus, or qualify a representative to participate in a recognition club, such as a President's Club.

B. The SEC Should More Closely Align the Care Obligation with Securities Law Concepts and Standards

We appreciate the SEC's efforts to adopt a principles-based approach to the Care Obligation, and, in particular, its commitment to permitting firms to continue to balance cost (including fees, compensation, and other financial incentives) with other factors (including, among others, the product's or strategy's investment objectives, characteristics (including any special or unusual features), liquidity, risks and potential benefits, and volatility) in determining whether a broker-dealer meets its care obligation. We also agree that conducting a proper evaluation of any recommendation prior to making it is of fundamental importance to retail investors. However, we believe that FINRA's standards are well-established and already meet these objectives. We urge the SEC to view and build its Care Obligation on the current foundation of established brokerage requirements.

1. The SEC Should Not Import ERISA Concepts of "Prudence" into the Broker-Dealer Regulatory Regime

Issue: Incorporating ERISA prudence into securities law unnecessarily creates legal uncertainty that may have the effect of incenting the flow of assets from brokerage to advisory models.

Proposed Solution: Eliminate the word "prudence" from the Reg BI Proposal and clarify that the reasonableness standard is consistent with FINRA's guidance under Rule 2111.

Comment: The SEC has introduced an ostensibly new concept in the Care Obligation that would require broker-dealers and their representatives to exercise "reasonable diligence, care, skill, and ***prudence***" to determine whether an investment is in the customer's best interest.[35] The SEC's use of the term "prudence" is concerning because it suggests that a new, ERISA-type standard, will be

[35] Proposed Sec. Exch. Act Rule 15l-1(a)(2)(ii) (emphasis added).

applied in brokerage, notwithstanding that the SEC goes on to describe the term as effectively being a "reasonableness" standard.[36]

While some may view ERISA prudence (the highest standard for relationships of trust) as an appropriate standard for broker-dealers who should provide advice in their customers' best interest, the term raises numerous interpretive issues and compliance risks. Regulatory and judicial interpretations of ERISA "prudence" and its requirements abound, but these are exclusive to employee benefit plan duties and do not address duties with respect to retail accounts for individual customers. Additionally, because broker-dealers have historically not generally been viewed as ERISA "fiduciaries" subject to the ERISA prudence standard, there are virtually no cases or guidance interpreting how the standard should be applied in a transactional brokerage model. The SEC has emphasized in its proposal that, unlike investment advisers, broker-dealers are generally not "fiduciaries"[37] . Consistent with this concept, the SEC should not apply a fiduciary-like standard to broker-dealers. Moreover, it is unclear whether including a concept Congress expressly delegated to the DOL under a separate statutory regime, is within the scope of the SEC's interpretive and enforcement authority under.

As the SEC noted, the Care Obligation largely incorporates existing obligations broker-dealers have under FINRA Rule 2111 (Suitability) and FINRA Rule 2090 (Know Your Customer).[38] We agree that reasonableness is an appropriate standard and believe that FINRA Rule 2111 already captures that standard. We ask the SEC clarify that the reasonableness standard is consistent with FINRA's guidance under Rule 2111. We further request that the SEC remove the word "prudence" so as not to confuse Reg BI's standard with fiduciary standards and guidance developed under ERISA and other laws.

<u>Issue</u>: Reg BI creates uncertainty as to when a recommendation may be made when a broker-dealer may not have been able to obtain certain "customer investment profile information" notwithstanding its reasonable diligence.

<u>Proposed Solution</u>: Clarify how much "customer investment profile information" is enough to have a reasonable basis for a recommendation.

<u>Comment</u>: The SEC should clarify when a broker-dealer may not have been able to obtain certain customer investment profile information, notwithstanding its reasonable diligence, yet a recommendation might nonetheless be appropriate. This could be done in the form of examples in the final rule. We agree that broker-dealers should be obligated to use "reasonable diligence" to ascertain customers' investment profiles before making recommendations. However, the SEC noted in the Proposals that it would consider a broker-dealer that makes a recommendation to a retail customer, for whom it lacks sufficient information to have a reasonable basis to believe that

[36] *See* Reg BI Proposal at 21609.
[37] *See*, *e.g.*, *id.* at 21662-63.
[38] "FINRA Rule 2111 requires FINRA member firms to "have a *reasonable basis* to believe that a recommended transaction or investment strategy … is suitable for the customer, based on the information obtained through the *reasonable diligence* of the member or associated person to ascertain the customer's investment profile." FINRA Rule 2111(a) (emphasis added). FINRA Rule 2090 requires "[e]very member [to] use *reasonable diligence*, in regard to the opening and maintenance of every account, to know (and retain) the essential facts concerning every customer and concerning the authority of each person acting on behalf of such customer." FINRA Rule 2090 (emphasis added).

the recommendation is in the best interest of that retail customer, to have failed to meet its obligations under Reg BI. This, coupled with uncertainty as to how "prudence" would be interpreted in the brokerage construct, leaves open how much information a broker-dealer has to collect and consider before making a recommendation. Clarity here is necessary.

2. *The SEC Should Clarify How Cost and Likely Performance Should Be Considered When Recommending Investments*

Issue: The SEC's articulation of its Care Obligation with respect to what is an "identical security" and how to support recommendations that may not be to the "best," "least expensive," "least remunerative" or "high performance" options is unworkable without further clarification.

Proposed Solution: Remove the language in the preamble with respect to "identical" securities or strategies and clarify that Reg BI does not require recommendations be made to the "best," "least expensive," or "least remunerative" options or the options with the highest likelihood of performance.

Comment: We agree that the cost associated with a recommended investment is an important factor when evaluating whether to recommend an investment to a retail customer – and it already is.[39] Specifically, the SEC states that "a broker-dealer could not have a reasonable basis to believe that a recommended security is in the best interest of a retail customer if it is more costly than a reasonably available alternative offered by the broker-dealer and the characteristics of the securities are otherwise identical."[40]

Our proposed solution recognizes that some differences will inevitably exist that could justify a higher cost. For example, these differences might relate to credit quality of an issuer, tenure of a portfolio manager, whether one mutual fund has experienced more "style drift" than another, brand perception, and many other difficult-to-quantify metrics. Imposing a strict obligation to consider *any* cost differential, however immaterial, between products or strategies that will inevitably have *some* difference is unnecessary and costly.

From a practical perspective, broker-dealers and their representatives simply do not have access to the real-time information that would be required to precisely compare all investments' features and benefits to their costs to determine which investment is the "best" for the investor. Moreover, the SEC should recognize that broker-dealers should be able to construct investment platforms with the share classes they choose to make available and that broker-dealers are not obligated to make all share classes available. This is critical to a broker-dealer's economics and ability to operate its platform profitably.

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[39] *See* FINRA Rule 2111 (Suitability) (requiring, among other things, that broker-dealers deal fairly with their customers and make recommendations that are intended to satisfy customers' investment objectives, are consistent with customer's investment profiles, and are within customers' financial ability to undertake). *See also* FINRA Reg. Notice 12-25, at 3-4 (dedicating an entire segment to "Acting in a Customer's Best Interests," which discussed in various ways the import of cost, for example: "Examples of instances where FINRA and the SEC have found brokers in violation of the suitability rule by placing their interests ahead of customers' interests include … [a] broker whose motivation for recommending one product over another was to receive larger commissions.").

[40] Reg BI Proposal at 21589.

The SEC should at minimum consider clarifying the whether a broker-dealer has met its Care Obligation in this regard incorporates a "materiality" factor and that "a reasonable basis to believe that the higher cost is justified" should be judged both on objective factors and the subjective factors actually considered by a particular representative. Thus, we note that the objective to identify the "best," "least expensive," or "least remunerative" products is a worthy goal, but it is an unworkable standard to apply to a transactional-based brokerage business.

The SEC should also clarify its statements regarding consideration of the "likely performance" of a recommended product or strategy from the analysis. The SEC appears to have borrowed this concept from FAQ1 in FINRA Regulatory Notice 12-25, in which FINRA interpreted its suitability rule to require firms to make recommendations consistent with their customers' best interests:

> The customer's investment profile, for example, is critical to the assessment, as are a host of product- or strategy-related factors in addition to cost, such as the product's or strategy's … likely performance in a variety of market and economic conditions.

However, instead of "likely performance of a security in a variety of market and economic conditions"), the SEC states that "likely performance of market and economic conditions,"[41] which is a consideration distinct from what FINRA contemplated. We request that the SEC clarifies this point.

Additionally, we ask that the SEC clarify that consideration of "likely performance" or "expected returns" of a security for purposes of the Care Obligation (and FINRA suitability) should not be interpreted as impacting the regulatory status quo surrounding FINRA Rule 2210 and communications with the public involving hypothetical or projected performance.[42] In other words, a retail customer should expect that his or her registered representative is considering those two characteristics of a security the as part of the Care Obligation and suitability analysis. But, that is not to say the representative must then make disclosures to the retail customer regarding the likely performance or expected returns that the representative analyzed, which FINRA has considered to be possibly misleading, particularly in dealing with retail customers (other than as might be provided by the terms of the security itself (*e.g.*, a bond coupon)).

C. The SEC Should Revise Reg BI's Recordkeeping Requirements So That They Do Not Result in Undue Compliance Costs and Are Consistent with Privacy and Cybersecurity Laws

Issue: Significant obstacles, including increased privacy and cybersecurity risks, will likely result from implementing proposed Rule 17a-3(a)(25), in particular with respect to the "all information collected from … the retail customer" requirement.

Proposed Solution: Clarify Reg BI's recordkeeping requirements apply to each account, among other solutions discussed below.

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[41] *Id.* at 21610.

[42] *See* FINRA Rule 2210(d)(1) (Communications with the Public). *See also* Interpretive Letter to Bradley J. Swenson, ALPS Distributors, Inc. (Apr. 22, 2013); Interpretive Letter to Edward P. Macdonald, Hartford Funds Distributors, LLC (May 12, 2015); Interpretive Letter to Clair Pagnano, K&L Gates LLP (June 9, 2017).

Comment: Reg BI would create new record retention requirements that would require, "for each retail customer to whom a recommendation of any securities transaction or investment strategy involving securities is or will be provided, a record of all information collected from and provided to the retail customer pursuant to Regulation Best Interest, as well as the identity of each natural person who is an associated person of a broker or dealer, if any, responsible for the account."[43] This differs from Exchange Act Rule 17a-3(a)(17), which requires broker-dealers to create and periodically update certain customer account information, because Rule 17a-3(a)(17) applies to *each account*, whereas proposed Rule 17a-3(a)(25) imposes recordkeeping obligations in respect of *each recommendation*.

For example, compliance with the Rule 17a-3(a)(25) requirement would likely require broker-dealers to substantially enhance their technology expenditures in order to build internal IT infrastructure and policies and procedures surrounding the collection of highly sensitive personally identifiable information and other sensitive documents (*e.g.*, a Form W-2 and other documents with Social Security numbers). In addition, firms would be required to invest substantial sums in representative- and customer-friendly technological tools that can be used during in-person meetings with retail customers. This would be particularly impactful to firms like us because our representatives often meet with retail customers in the customers' homes or in public spaces where our institutional technology is unavailable. We would thus need to build (at considerable costs) a suite of new tools that might be able to securely image or otherwise record "all information collected" in those meetings in compliance with applicable cybersecurity and privacy laws.

Remarkably, the Proposals do not acknowledge or even once reference cybersecurity or privacy laws that might be implicated by broker-dealers complying with proposed Rule 17a-3(a)(25), and it is also not clear that the Proposals quantify the technology costs associated with this recordkeeping requirement.

With respect to written materials collected from retail customers for purposes of complying with proposed Rule 17a-3(a)(25), when our representative meets with a retail customer at his or her home or other space (which as we discussed above, is at the core of what we do for our customers), what is the proper course to be taken when the customer hands the representative written materials that the customer does not want removed from the home (or shared over insecure technology)?

Pursuant to the Proposals, we would be excused from obtaining those materials for recordkeeping purposes upon the "neglect, refusal, or inability" of the customer to provide or update such information.[44] Does this mean, however, that the representative would then be required to photocopy the materials or otherwise document that the customer's refusal to permit the representative to take the materials? In addition, much information our representatives obtain from retail customers is information conveyed orally to the representative in face-to-face meetings. Is information that is conveyed orally subject to the requirement that PFSI make a record of "all information collected from" retail customers? The SEC should clarify these obligations.

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[43] Reg BI Proposal at 21625.
[44] *Id.*

Part II:

Form CRS and Disclosures

A. The SEC Should Revamp the Proposals' Approach to Disclosure to More Effectively Arm Investors with Information They Need to Make Informed Investment and Savings Decisions Without Creating Unnecessary Legal Risks for Broker-Dealers and Investment Advisers That Shift Resources Away Individual Investors

The SEC has an important rulemaking opportunity to improve the content, format, delivery, and general approach of disclosures broker-dealers and investment advisers use to communicate with, educate, and inform retail investors. The time is ripe to arm investors with meaningful information so that they can make well-informed decisions about the investment products, advice models, and compensation structures best suited to meeting their personal investment and savings goals.

To this end, we support the SEC's concept of "layered disclosure" and believe this approach can have a meaningful impact on how investors receive and process information. The SEC's Form CRS, when paired with Reg BI's Disclosure Obligation for broker-dealers, and the current disclosure regime for investment advisers (including disclosure obligations under the fiduciary standard of care, as well as Form ADV's disclosure requirements) can form the starting point for a robust layered disclosure regime. But, as proposed, Form CRS introduces unnecessary and potentially harmful complexity, legal risks and compliance burdens that could both fall short of enhancing financial literacy, and also cause firms to restrict or even end access to brokerage advice for middle-income Americans.

To address these issues, Form CRS, as the first layer of disclosure, should be a single industry-wide, SEC-created document that is focused on educating investors about the general marketplace for financial services models, rather than the specifics of any particular firm. The SEC can then require firms to create subsequent disclosure layers geared to summarize the specific relationships they offer to their customers, including general descriptions of services offered, compensation structures, and related conflicts of interest, with the focus on helping customers choose the appropriate account type for their personal circumstances. These subsequent disclosure layers would be subject to the investment adviser's or broker-dealer's general disclosure obligations under the Investment Advisers Act of 1940 ("Advisers Act") and Reg BI (as applicable).

The sections that follow outline our concerns with the Form CRS Proposal and provide more details on our suggested approach to more effective disclosures.

1. *Form CRS Should Not Create a Private Right of Action*

<u>Issue</u>: The required language in Form CRS may form the basis for a private right of action or a rescission right.

<u>Proposed Solution</u>: The SEC should expressly state that Form CRS is not intended to create a private right of action, as it did for Reg BI, each of which Proposals may be enforced alone, *and* make Form CRS (what we view as the first layer of disclosure in a multilayered disclosure approach) a generic, standardized investor education piece created and maintained by the SEC.[45]

<u>Comment</u>: The fear of an unrestricted private right of action was a fundamental flaw of the DOL Fiduciary Rule—one that indisputably drove many firms to limit choice, restrict access to the brokerage advice model, and abandon investors with small accounts (*i.e.*, middle-income Americans).[46] This will undoubtedly harm investors who are already struggling to save and invest for the future by cutting off access to the professional investment services they need.

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[45] This approach would be similar to the manner in which some states have addressed educating their citizens in relation to the insurance products that they regulate. For example, some states' insurance laws require that insurance companies or producers provide prospective purchasers of variable annuities with a "buyer's guide" prior to accepting initial premiums for the variable annuities. *See*, *e.g.*, FLA. STAT. § 626.99(4) ("The insurer shall provide to each prospective purchaser a buyer's guide and a policy summary prior to accepting the applicant's initial premium or premium deposit, unless the policy for which application is made provides an unconditional refund for at least 14 days, or unless the policy summary contains an offer of such an unconditional refund. In these instances, the buyer's guide and policy summary must be delivered with the policy or before delivery of the policy. … For variable annuities, a policy summary may be used, which may be contained in a prospectus, until such time as a buyer's guide is developed by NAIC or the department, at which time one of those guides must be used."); *See also* IOWA ADMIN. CODE § 191-15.64(507B) (requiring the National Association of Insurance Commissioner's ("NAIC's") approved buyer's guide to be delivered in various contexts). These buyer's guides are intended to help prospective contract owners understand common features of variable annuities and include, among other things, discussion of fees and other charges, how annuities make payments, and questions a prospective purchaser should ask the insurance company issuer or insurance producer. State insurance departments may adopt the guide developed by the NAIC or may develop their own guides. *See*, *e.g.*, NAIC Buyer's Guide for Deferred Annuities, https://www.naic.org/documents/prod_serv_consumer_anb_la.pdf.

[46] *See*, Michael Wursthorn, *Merrill Lynch to End Commission-Based Options for Retirement Savers*, Wall St. J., Oct. 6, 2016, https://www.wsj.com/articles/merrill-lynch-to-end-commission-based-options-for-retirement-savers-1475784928; Michael Wursthorn, *Merrill's Fiduciary Alternative Would Affect Limited Number of Clients*, Wall St. J., Mar. 10, 2017 (While Merrill Lynch is considering offering an alternative product, such a product would "carry heavy restrictions. … The people familiar added that there is no guarantee an alternative product will be created."); Michael Wursthorn, *Edward Jones Shakes Up Retirement Offerings Ahead of Fiduciary Rule*, Wall St. J., Aug. 17, 2016, http://www.wsj.com/articles/edward-jones-shakes-up-retirement-offerings-ahead-of-fiduciary-rule-1471469692; Greg Iacurci, *State Farm, citing DOL fiduciary rule, cuts agents from mutual fund and variable annuity sales*, Investment News, Sept. 12, 2016, http://www.investmentnews.com/article/20160912/FREE/160919992/state-farm-citing-dol-fiduciary-rule-cuts-agents-from-mutual-fund?AID=%2F20160912%2FFREE%2F160919992; Michael Wursthorn, *J.P. Morgan Moves Ahead With Plan to Drop Commissions in IRAs*, Wall St. J., Mar. 13; Grete Suarez, *Capital One will eliminate commissions on IRAs*, Investment News, Nov. 16, 2016, http://www.investmentnews.com/article/20161116/FREE/161119951/capital-one-will-eliminate-commissions-on-iras; Investment News Staff, *Commonwealth Financial eliminates commission-based retirement products in wake of DOL rule*, Investment News, Oct. 24, 2016, http://www.investmentnews.com/article/20161024/FREE/161029956/commonwealth-financial-eliminates-

Our primary concerns for the Form CRS Proposal are centered on the statements required in the "Our Obligations to You" section of the Form CRS disclosure, which we believe could be viewed as creating state law contractual liability. Specifically, Form CRS would require firms to make the following affirmative statements:

- ***For broker-dealers—***
  - "We must act in your best interest and not place our interests ahead of yours when we recommend an investment…. When we provide any service to you, we must treat you fairly and comply with a number of specific obligations."
  - "When we provide any service to you, we *must* treat you fairly and comply with a number of specific obligations"; and "When we provide recommendations, we *must* eliminate these conflicts or tell you about them and in some cases reduce them."
- ***For investment advisers—*** "We are held to a fiduciary standard that covers our entire investment advisory relationship."[47]

Although these statements are included in a disclosure (rather than in the customer agreement), we believe a court could mistakenly view them as a unilateral contract obligation from the financial institution forming a broad basis of a breach of contract claim under state law.

Reg BI and Form CRS could also potentially expand existing private rights of action under the federal securities laws, should the disclosures mandated by those provisions be interpreted as imposing a standard of care. For example, plaintiffs may sue a broker-dealer for a material omission under Exchange Act Rule 10b-5 and claim that Reg BI and Form CRS imposed a duty on the broker-dealer to disclose the omitted information. In other words, the standards in Reg BI and statements on Form CRS could reasonably be viewed as establishing a new and additional standard of conduct against which a broker-dealer's conduct could be judged, and enforced, under a private right of action. While this is not a novel issue,[48] there are refinements to the Proposals that the SEC could make to alleviate these concerns.

We appreciate the SEC stating that Reg BI is not ***intended*** to create a private right of action on the basis that it is being proposed, "in part," under the authority provided by Section 913(f) of Dodd-Frank Wall Street Reform and Consumer Protection Act and Section 15(l) of the Securities Exchange Act of 1934 ("Exchange Act"), neither of which create a new private right of action or right of rescission. However, at the same time, the SEC itself appears to recognize that its position here is uncertain at best, as under Reg BI it requests comment specifically on this point: "Do

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commission-based-retirement; Kenneth Corbin, *Stifel's fiduciary solution for commissions*, OnWallStreet, Nov. 3, 2016, available at https://www.onwallstreet.com/news/stifels-fiduciary-solution-for-commissions.

[47] Form CRS Proposal at 21429-30 (emphasis added).

[48] We are aware that Regulation S-K imposes disclosure obligations on public companies, including Item 303, which requires a public company to disclose in certain public filings "known trends and uncertainties" that the issuer reasonably expects will have a material impact on its financial performance. Although courts have long established that Item 303 does not create a private right of action, complaints commonly reference Item 303 as establishing a standard of disclosure.

commenters agree with the Commission's assessment that no new private right of action or right of rescission is created by Regulation Best Interest?"[49]

We also find it difficult to see how mandates of these types of consumer protection obligations will not ultimately find their way into state law actions, including breach of fiduciary duty claims under state laws. Agreeing that broker-dealers should be responsible for meeting their customer obligations, we question the potential enforcement mechanism by litigation claims brought by an extremely active and creative plaintiffs' bar. Our concerns are based not on the obligation to address customer issues, if or when, they occur, but on the extraordinary costs of addressing and responding to unsubstantiated and frivolous claims in state court actions.

We have no doubt that the plaintiffs' bar will seek to frame these contract claims as class actions. Even if a firm has reasonable arguments to substantiate its compliance with the applicable standard, due to the enormous costs of protracted litigation, the pressure to settle these cases, rather than to incur the cost to fight and prevail, will be enormous. Faced with this potential for exploitation, we believe that many firms will mitigate their risks and compliance costs by discontinuing services to middle-income Americans with small account balances.

We urge the SEC to clearly and structurally address this issue so that its rulemaking does not unintentionally expose firms to legal risks that are disproportionate to the perceived misconduct the SEC is seeking to address.

Under our proposed multilayered disclosure approach, the first layer of disclosure, Form CRS, could provide a simple plain-English explanation of brokerage and investment advisory advice models, with general service levels, applicable standards of conduct, types of compensation structures, and related conflicts of interest, incorporating and cross-referencing much of the existing SEC and FINRA investor educational materials. Adopting this approach would largely eliminate the risk that a plaintiff's lawyer could take the position that the statements in Form CRS constitute affirmative contractual representations from firms regarding their services or service obligations.

<u>Issue</u>: The current Form CRS will do little to address investor confusion, or help investors decide whether to get investment services from a broker-dealer, investment adviser, or both.

<u>Proposed Solution</u>: Building upon a standardized educational Form CRS, the SEC could then require firms to craft additional layers of disclosure that more specifically address the nuances of that firm's particular business model(s), and what investors should think about at various decision-points in the investment process.

<u>Comment</u>: As proposed, Form CRS would require individual firms to create customized Form CRS disclosures, subject to the strict length, format, and content limits set forth in the Form CRS Proposal. This mix of prescribed and flexible disclosure would ultimately result in a patchwork of new disclosures that fail to comprehensively describe a particular firm's business model in a way that is accessible and digestible by retail investors. Moreover, with three different Form CRS

[49] Reg BI Proposal at 21592.

models for registered investment advisers, broker-dealers, and dual registrants, investors will get different forms from different firms reducing their value as comparative documents.

The additional layers of disclosure under our multilayered disclosure approach, could again be in the form of simple, plain-English, executive summaries that cross-reference or link to other account documents for additional details. While we believe it is best if the SEC take a principles-based approach to these subsequent, firm-created layers of disclosure, and not prescribe specific content or page limits, we note that these disclosures would still be subject to the anti-fraud provisions under the securities laws, the disclosure obligation under Reg BI, and investment advisers' disclosure obligations (as applicable), which should provide an appropriate level of protections for investors. This would give firms flexibility to craft their own disclosures, while still protecting investors from misleading or insufficiently clear disclosure.

This approach will also improve the utility of Form CRS, and the disclosure regime generally, and reduce compliance costs. We have included an illustration of this layered disclosure approach, as well as concept drafts of disclosure layers 1-3 in **Appendix B** to this letter. These are merely samples for your consideration, and we welcome the opportunity to discuss the potential, content, style and approach of these disclosures with the SEC.

In the alternative, if the SEC rejects our preferred approach to create and require a first-layer standard educational Form CRS and subsequent firm-specific layers of disclosure, we urge the SEC to consider deleting from Form CRS the section entitled "Our Obligations to You," or to modify it to address the private right of action concern discussed above. The SEC should unequivocally state without qualification that none of the statutory authority under which Reg BI and Form CRS would be adopted empowers the SEC to create a private right of action. Regardless of whether plaintiffs and courts would agree in an actual controversy, it would be beneficial that the record clearly reflects the SEC's position, intentions and scope of authority in this regard.

Moreover, we believe the "Our Obligations to You" section should also be removed from Form CRS to avoid investor confusion. We appreciate the SEC's stated goal of clarifying the differences between the standards that apply to broker-dealers and investment advisers, but we do not believe retail investors can reasonably understand the difference between a "best interest" standard for broker-dealers and a "fiduciary" standard for investment advisers.[50] Thus, we believe this requirement not only increases litigation risks, but also, more importantly, risks confusing retail customers through casual use of undefined terms that seem clear on their face but lack clear meaning in practice (e.g., "best interest").

By eliminating this section of Form CRS, the purpose of the form would continue to be served – to give a summary of the types of services provided and how retail customers generally pay for such services, and to "help prompt a conversation between retail investors and their financial

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[50] *See* Commissioner Hester Peirce, *What's in a Name? Regulation Best Interest v. Fiduciary*, *statement at* Nat. Assn. of Plan Advisors D.C. Fly-In Forum (July 24, 2018), https://www.sec.gov/news/speech/speech-peirce-072418 (describing the varying meanings of "fiduciary," the inability of securities lawyers, financial professionals, and the Commission itself to be able to cohesively articulate the applicable standard across contexts, and the uncertainty that anybody fully understands what "best interest" actually means, notwithstanding "hundreds of pages" of the Commission attempting to describe it).

professionals about both the conflicts the firm and financial professional have and what steps the firm takes to reduce the conflicts."[51] The SEC should also permit firms to state on Form CRS that the customer agreement is the exclusive agreement of the parties, and that the disclosures provided pursuant to Form CRS do not create or modify the customer agreement, or create a separate private right of action under state or federal law.

2. The Form CRS "Key Questions to Ask" Should Not Expand Current Disclosure and Other Obligations

Issue: The proposed Form CRS section regarding "Key Questions to Ask" would impose substantial supervisory and compliance burdens on broker-dealers.

Proposed Solution: Consider restyling the "key questions" to be reflective back toward the retail investor.

Comment: In some cases, the questions simply cannot be answered with any degree of certainty or accuracy. In particular, consider Question 2:

2. Do the math for me. How much would I expect to pay per year for an advisory account? How much for a typical brokerage account? What would make those fees more or less? What services will I receive for those fees?"

The answers to these questions depend on multiple contingent inputs that cannot be known in advance. For example, what a client "pays" per year for an advisory account depends on:

- Assuming the fee is calculated a percentage of assets—
    - How much will the client invest over the year?
    - How will the client's investments perform (*i.e.*, will there be gains and losses that affect the fee)?
    - Will the client reach or fall below fee break-points?
    - Does the firm "household" the client's and his or her family member's assets for fee reductions, and, if so, will a family member open an account and add assets?
- What other fees and expenses should be taken into account when determining what the client pays?
    - Custody fees paid to a third-party custodian?
    - Compensation the adviser receives from third-party investment sponsors in connection with the client's investments (*e.g.*, sub-TA, omnibus recordkeeping, and revenue sharing)?

[51] Form CRS Proposal at 21430.

- Compensation paid to affiliates in connection with investments in proprietary products?
- Commissions and other transaction charges (noting that these will depend on various unknowable factors like what investments are traded, trade sizes, and trade volumes?
- Expenses internal to the investment products in which the client invests?

Given its transaction-based compensation structure, this calculation would be even more complicated for a brokerage account. Moreover, if a representative "does the math" and comes up with the "wrong" answer, firms could be liable for the misstatement.

To address concerns about the potential for misstatements or incomplete answers, firms may feel obligated to develop scripts for answering the questions to ensure that representatives' statements are not misleading. In some cases, such as where a representative is speaking at a prospective investor seminar, this would result in the cumbersome outcome that firms would likely have a principal approve such scripts prior to use and then *submit the scripts (i.e., the answers to the "key questions") for FINRA's review*.[52] This will only add to the costs and compliance burdens of running brokerage and advisory businesses.

Under our proposed solution, instead of the "Do the math for me" prompt (#2), the question could be "Do *I* understand the differences in fee structures between an advisory account and brokerage account; what would make those fees more or less; and what services will *I* receive for these fees?" The "key questions" could then be followed by a note, "If you don't know the answers or have other questions, ask your representative for help." By styling the questions and prompts in this manner, there would be less of a burden on firms and representatives to respond to predetermined questions. This would result in a more casual prompt for conversations and reduce the risk of firms being accused of having a disclosure obligation as a result of the questions.[53]

Alternatively, the "key questions" could be restyled as "Key Topics to Discuss" or "Key Topics to Consider." This would permit the SEC to propose a more concise topic list and would also serve the purpose of reducing the risk of firms being deemed to have an affirmative disclosure obligation in response to the specific questions currently proposed. It would also serve to facilitate an open and informed conversation with the representative as opposed to a one-way Q&A.

3. The Form CRS Delivery Requirement Should Be Streamlined and Simplified

Issue: The requirement that a broker-dealer "communicate without charge the information in an amended relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made," is unduly burdensome regardless of whether the document is delivered in paper or electronically.

Proposed Solution: Expressly permit firms to satisfy the Form CRS requirements by posting Form CRS on their public websites and providing customers and prospective customers the

[52] *See* FINRA Rule 2210(b)(1), (c)(2).
[53] *See supra* n.45 (regarding the NAIC buyer's guide, which takes the suggested approach).

website link. If the customer requests a paper Form CRS, the firm should provide it, but should not otherwise be required to obtain consent to electronic delivery.

Comment: We appreciate that the SEC would explicitly permit Form CRS to be delivered electronically, but this does not fully address the operational issues related to paper delivery because privacy laws dictate that customers would still have to consent to receive the form electronically. While ratios of consumers who provide consents for electronic delivery may be increasing over time, they are still low as a percentage of accounts. In many states, these consents need to be updated periodically, such as annually.[54]

Paper delivery is costly, creating a new disincentive to serve the middle market who typically have smaller account sizes. Additionally, the SEC's Proposals raise concerns about how the delivery requirements could practically be complied with when the form is delivered in paper. Specifically, the Proposals would require paper relationship summaries to be the ***first*** among any documents that are delivered at the same time.[55] This ignores the reality of two people sitting down face-to-face at a kitchen table, wherein a PFSI representative may pull Form CRS from his or her briefcase after, by chance, pulling another document. People and personal interactions are just not that scripted. Furthermore, there is no such functionality to ensure Form CRS is "the first" document opened in an email when documents are delivered initially electronically.

This requirement is also detached from "recommendations" that otherwise anchor the initial Form CRS delivery requirement and creates an ongoing disclosure obligation for broker-dealers that is akin to that required of investment advisers.[56] The SEC should consider, given there is no ongoing obligation to monitor a retail customer's account or to make recommendations, whether this is an appropriate or necessary obligation.

Building upon the layered disclosure regime discussed above, the firm specific subsequent layers of disclosure could then be updated on the web periodically for any changes, without the need to redeliver, unless of course a customer specifically requests the document in paper. This approach would recognize that—in 2018—most of the investing public is able to access information through the internet, if not through a computer then through a phone, and that generally this is a preferred method of doing so.

4. The Form CRS Recordkeeping Requirements Should Be Clarified

Issue: The Proposal is contradictory with respect to Form CRS' delivery and timing.

Proposed Solution: Clarify the types of recommendations that may be made prior to delivery of the relationship summary and further clarify generally the proper timing of delivery. Eliminate the requirement that records be kept when the relationship summary is provided to prospects and require that that such records only be retained when an account is opened and funded.

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[54] *See, e.g.*, Cal. Fin. Code § 4053(b)(1).
[55] Form CRS Proposal at 21453.
[56] *Id.* at 21455.

<u>Comment</u>: Under proposed Form CRS, firms would be required "to maintain each amendment to the relationship summary as well as to make and preserve a record of dates that each relationship summary and each amendment was delivered to any customer or to any prospective customer who subsequently becomes a customer, as well as to any retail investor before such retail investor opens an account."[57] This would apparently require broker-dealers and investment advisers to retain records of the dates on which its representatives provided a relationship summary to a *prospective* retail customer, even though elsewhere in the Proposals the SEC states that no delivery would be required until the prospect determines to then actually engage the broker-dealer.[58]

When a prospect ultimately "engages" a broker-dealer is also unclear. The SEC describes "engagement" as the earlier of when the retail investor places an order or an account is opened. A mere recommendation, however, would not trigger the delivery requirement if the retail investor does not open or have an account with the broker-dealer or the recommendation does not lead to a transaction. This suggests that at least certain recommendations to prospective customers may precede delivery of the relationship summary, so long as the relationship summary is delivered before an account is opened or transaction is effected.

In the absence of clarity, Form CRS would effectively require that a broker-dealer retain records of the dates of delivery to any prospective customer for some indefinite period of time to ensure that, should the prospect at some point become an actual customer, the broker-dealer will have the required records to satisfy this requirement.

Part III

Investment Advisers

A. The SEC Should Not Propose New Registration, Licensing or Qualification Requirements on Investment Advisers

<u>Issue</u>: New federal requirements on Investment Advisers would be duplicative of current registration, licensing, and qualification requirements under state law, and continuing education requirements that NASAA is considering.

<u>Proposed Solution</u>: Avoid imposing new registration, licensing or qualification requirements on investment advisers.

<u>Comment</u>: We do not believe any additional enhancements are needed to the regulatory regime under the Advisers Act. As such, we urge the SEC not to propose any new regulatory requirements

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[57] Form CRS Proposal at 21458.

[58] *See id.* at 21419 ("We are proposing to require registered investment advisers and registered broker-dealers to deliver a relationship summary to retail investors. In the case of an investment adviser, initial delivery would occur before or at the time the firm enters into an investment advisory agreement with the retail investor; in the case of a broker-dealer, initial delivery would occur before or at the time the retail investor first engages the firm's services. Dual registrants would deliver the relationship summary at the earlier of entering into an investment advisory agreement with the retail investor or the retail investor engaging the firm's services."). *See also id.* at 21453 ("The rule does not require delivery to a retail investor to whom a broker-dealer makes a recommendation, if that retail investor does not open or have an account with the broker-dealer, or that recommendation does not lead to a transaction with that broker-dealer.").

for investment advisers. These “enhancements,” which are generally drawn from broker-dealer regulations, are not appropriate for investment advisers, and would only add to the costs of operating advisory models—costs that will inevitably be at least partially passed on to advisory clients.

Our primary concern would be “enhancements” to licensing and continuing education. Any such new requirements would not only add costs but they would also create significant barriers to entry for financial professionals who want to provide advice through advisory models. These types of requirements generally involve testing that has been shown to discriminate against minorities, non-English speakers, and those without college degrees,[59] which our vast experience in this area has borne out.

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PFSI would be pleased to provide further information, participate in any direct outreach efforts the Commission undertakes, or respond to questions the Commission may have about our comments.

Sincerely,

cc: The Honorable Jay Clayton, Chair
The Honorable Kara M. Stein, Commissioner
The Honorable Robert J. Jackson, Jr., Commissioner
The Honorable Hester M. Peirce, Commissioner
Dalia Blass, Director, Division of Investment Management
Brett Redfearn, Director, Division of Trading and Markets

[59] *See, e.g. Ricci v. DeStefano*, 557 U.S. 557 (2009).

APPENDIX A

Who We Are and How We Help Middle-Income Families

A. *About Primerica*

For over 40 years, Primerica has focused on helping middle-income individuals across North America. Our goal is to create more financially independent families. While other financial services companies typically focus on the wealthy, Primerica serves everyday Americans in neighborhoods all across our nation. We take an educational approach and offer financial tools to help our clients reach their goals. We underwrite our own term life insurance products and distribute straightforward investments on behalf of industry-leading third parties. The investment and savings products we offer comprise mutual funds, managed accounts, and annuities. Our "buy term [life insurance] and invest the difference" philosophy has generated $764 billion of term life insurance in force and $61 billion in asset values for millions of middle-income families.[60] This is our mission.

Our customers earn, on average, between $30,000 and $100,000 in annual household income, a category that represents approximately 50% of all U.S. households.[61] We educate customers about the long-term benefit of dollar-cost averaging through systematic investing into a diversified investment portfolio. Our business model allows our representatives to accept the smaller-sized transactions typical of middle-income customers, while providing these customers with personal services that ordinarily would be out of their reach. We are proud that we created a successful business model where we can open an account for an individual with as little as $50 per month or $250 to invest. We know firsthand that individuals with access to a financial representative accumulate greater and more balanced assets than those without, a fact that is supported by numerous studies.[62] Consequently, we have one of the largest and most diverse sales forces in North America with approximately 24,300 brokerage licensed representatives helping over two million middle-income customers with their investment accounts.[63] Our securities representatives generally hold Series 6 and 63 FINRA registrations, and approximately 3,400 of our registered representatives are also registered as Investment Adviser Representatives.

Our representatives serve the communities in which they live. Accordingly, they are well-acquainted with the ever-changing financial challenges facing the middle-income market. The

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[60] As of December 31, 2017.

[61] U.S. Census Bureau, *Census Population Survey 2016 Annual Social and Economic Supplement*, last revised Aug. 26, 2016. Based upon 125.8 mm households.

[62] *See*, *e.g.*, *The Role of Financial Advisors in the US Retirement Market*, at 17, OLIVER WYMAN (July 10, 2015), http://fsroundtable.org/wp-content/uploads/2015/07/The-role-of-financial-advisors-in-the-US-retirement-market-Oliver-Wyman.pdf (finding that, on average, individuals that use a financial representative have more assets than nonadvised individuals across all the age and income levels examined and that the differences are meaningful); Robert Litan and Hal Singer, *Good Intentions Gone Wrong: The Yet-To-Be Recognized Costs of the Department of Labor's Proposed Fiduciary Rule*, ECONOMISTS INC. (July 2015), https://www.dol.gov/agencies/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00517.pdf; Claude Montmarquette and Nathalie Viennot-Briot, *Econometric Models on the Value of Advice of a Financial Advisor,* CIRANO (July 2012), http://www.cirano.qc.ca/pdf/publication/2012RP-17.pdf.

[63] As of December 31, 2016 (includes 18,000 in the United States and 6,000 in Canada); 40% of life licensed representatives are millennials, 30% of Regional Vice Presidents (RVPs) are women, 19% of RVPs are African-American and 13% of RVPs are Hispanic as of December 31, 2016.

diversity of our sales force fully reflects the make-up of the middle-income market and continues to be both a primary strength and a goal of ours. There is no doubt that our representatives are a big reason for our success, as well as the success of many middle-income American families saving for their future needs.

Our business model is designed to allow us to reach the middle-income market in a sustainable manner. In fact, it encourages our representatives to concentrate on the smaller-sized transactions typical of middle-income customers. However, as is widely known, increased costs and risks associated with heightened regulatory requirements or legal uncertainty have induced many financial services companies to focus on more affluent consumers and abandon the middle-income market. This frailty became increasing evident during the partial implementation of the DOL Fiduciary Rule.

Primerica has tailored its offering of investment products to those that are most understandable and suitable for our middle-income customers. Through PFSI, our affiliated broker-dealer, we offer open-end mutual funds and variable annuities, all from well-known and respected companies. Our platform includes off-the-shelf products with commission levels consistent with those paid to other product distributors.

We gear our financial literacy and investment services toward our middle-income customers, who oftentimes are new or less experienced investors. In this regard, we continually produce plain language educational pieces highlighting fundamental investing concepts. Our primary investing principle, which is consistent throughout our educational pieces, is the long-term benefit of dollar-cost averaging through systematic investing into a diversified investment portfolio. In addition, we emphasize the benefits of a well-structured asset allocation, which spreads investment dollars across different asset classes to reduce risk and increase returns. We encourage our customers to stay with their savings plan and take a long-term view so that they can achieve their personal financial goals.

B. Our Focus on Saving for the Future

Our investing products and principles fit hand-in-glove with the primary financial needs of most middle-income Americans, which is to establish a long-term savings plan for future financial needs, such as college tuition and retirement. In response to these needs, Primerica and its representatives have made providing savings education and information a priority. Over our history, we have produced and distributed hundreds of thousands of educational brochures and pieces to help American families save and invest for their futures.[64]

We introduce customers to fundamental retirement savings concepts, such as the difference between expected retirement age and life expectancy, the “Rule of 72” which produces the years required to double one’s investment based on an assumed rate of return, and how inflation and rate of return affect a long-term savings plan. As a result of our efforts to educate American families about the need to save for the future, and to provide beneficial, cost-effective savings solutions, in

[64] For example, some of the current retirement brochures are identified as follows: Investing at Retirement; Asset Management; IRAs; Power of Dollar-Cost Averaging; Invest for Success; and ABC’s – The Basics of Investing.

just about any given year more than two-thirds of all accounts opened by PFSI are individual retirement accounts ("IRAs").

The Survey of Consumer Finances (the "SCF") is conducted by the Federal Reserve Board every three years and is a leading source of data on American's wealth. It provides detailed information on the incidence of retirement plan ownership—a critical tool for amassing sufficient savings—and categorizes the results by different criteria, one of which is family income. In its analysis of the results of the 2013 SCF, the Employee Benefit Research Institute (the "EBRI") finds that participation in an employment-based retirement plan (either a defined benefit or defined contribution plan) is strongly linked to family income.[65] According to the EBRI's report, in 2013 the SCF shows that 67.1% of all families with an income of $100,000 or more had someone participating in a plan at a current job. But in middle-income America, with incomes below $100,000, participation is significantly lower; in 2013, just 53.5% of families with incomes ranging from $50,000 to $99,999 had a participant in a plan. In the $25,000 to $49,999 income range, participation is even lower; in 2013, the number of families with a participant in a plan at a current job was just 25.8%.[66] These results show that middle-income market families take advantage of employer-sponsored retirement plans at rates far below their more affluent counterparts.[67]

Also, the SCF takes a more inclusive look at retirement plan ownership by measuring the percentage of all families with a participant in an employer-based plan or an IRA or Keogh plan. A wide variance in participation remains. In 2013, for families with incomes of $100,000 or more, fully 93.0% had a participant in one of these plans. But for families with incomes of $50,000 to $99,999, participation drops to 81.8%, and for incomes of $25,000 to $49,999, participation drops to a lowly 58.9%.[68] Again, the lack of participation is particularly acute in the lower income range, where more than 4 out of 10 families have no retirement account or savings.

Finally, the EBRI report allows further insight by reviewing the SCF data on *total average retirement portfolio account balance* for families in any plan or IRA. The SCF categorizes all families into five net worth percentiles. The average account balances again drop off considerably in the lower three net worth percentiles. These balances are $69,144 for the 50-74.9% percentile, $18,543 for 25-49.9%, and only $10,458 for families with a net worth in the bottom 25%.[69] This data confirms what we know anecdotally that savings is ***heavily*** skewed to higher net worth families, and that everybody else needs to save more. Those families with a net worth in the bottom 50%, which would be most middle-income families, are in real financial trouble and need help.

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[65] *See* Craig Copeland, *Individual Account Retirement Plans: An Analysis of the 2013 Survey of Consumer Finances*, EBRI Issue Brief, no. 406, November 2014, available at www.ebri.org.

[66] *Id.* at 7 (Figure 2).

[67] This negative trend is an ominous sign for savings in the middle-income market, Oliver Wyman recently found that 84% of more than 4,300 retail investors surveyed only began saving for retirement via a workplace retirement plan. *See* OLIVER WYMAN, *supra* n.62, at 5.

[68] *See* Copeland, *supra* n.65, at 10 (Fig. 5).

[69] *Id.* at 11 (Fig. 6).

Middle-Income Families Need Help to Understand the Need to Save and Invest

In the *New York Times* bestselling book "Nudge,"[70] behavioral economist Richard Thaler and law professor Cass Sunstein draw from behavioral science research to propose ways that sensible "choice architecture" (the context in which people make decisions) can successfully "nudge"[71] people toward better decisions, without giving up their freedom of choice. One of the societal problems they examine is saving for retirement, and the choices that participants make, or fail to make, inside of employer-based retirement plans. In so doing, the authors provide their insights into why saving for retirement and other future goals is such a challenge for many people:

> The standard economic theory of saving for retirement is both elegant and simple. People are assumed to calculate how much they are going to earn over the rest of their lifetime, figure out how much they will need when they retire, and then save up just enough to enjoy a comfortable retirement without sacrificing too much while they are still working.
>
> As a guideline for how to think sensibly about saving, this theory is excellent, but as an approach to how people actually behave, the theory runs into two serious problems. First, it assumes that people are capable of solving a complicated mathematical problem in order to figure out how much to save. Without good computer software, even a trained economist would find this problem daunting. The truth is that we know few economists (and no lawyers) who have made a serious attempt at doing it (even with software).
>
> The second problem with the theory is that it assumes that people have enough willpower to implement the relevant plan. Under the standard theory, flashy sports cars or nice vacations never distract people from their project of saving for a condo in Florida. In short, the standard theory is about Econs [previously described as the "textbook picture of human beings offered by economists", that "think like Albert Einstein, store as much memory as IBM's Big Blue, and exercise the willpower of Mahatma Gandhi"], not Humans [real people that "have trouble with long division if they don't have a calculator, sometimes forget their spouse's birthday, and have a hangover on New Year's Day"].[72]

We agree with the authors' opinion that the decision to save for retirement is one where most people need help (in the form of both education and encouragement) to do the right thing. The authors explain that the act of saving for retirement tests one's self-control, and that "self-control issues often arise when choices and their consequences are separated in time."[73] This seems particularly relevant, as when a 37-year-old parent opts to put off saving for retirement, a decision that will not have consequences for 20 or 30 years, in order to buy a new car, a choice that generates

[70] Richard H. Thaler and Cass R. Sunstein, *Nudge: Improving Decisions About Health, Wealth, and Happiness*, Penguin Bks. (2009).

[71] The authors define a nudge as "any aspect of the choice architecture that alters people's behavior in a predictable way without forbidding any options or significantly changing their economic incentives." *Id.* at 6.

[72] *Id.* at 6 and 106.

[73] *Id.* at 75.

immediate gratification. The authors also posit that it is particularly hard for people to make good decisions when they have trouble translating the choices they face into terms that they can easily understand.[74]

Thaler and Sunstein conclude that saving for retirement is, for most people, a hard choice, and that people need a "nudge," or help, to do the right thing. We completely agree, especially for people in the middle-income market with modest resources, where the decision to allocate current income to savings all most always giving up on a new consumer purchase or a current activity, such as a vacation or even a movie. We believe that our representatives, empowered with our educational materials, our philosophy of focusing on this market and our ability to successfully service small balance accounts, are this "nudge" helping American families to make the difficult decision to save on a daily basis.

People that Use Financial Professionals Report Better Savings Results

LIMRA Secure Retirement Institute published a Consumer Survey that shows that "advisors" (defined as paid financial professionals, such as brokers, financial planners, or advisors) add significant value to the customers they serve by encouraging them "to save holistically."[75] For nearly every identified savings goal surveyed (except vacation), LIMRA found that "advisors' customers are significantly more likely to save on a regular basis compared with people who don't consult advisors."[76]

Another study conducted by consulting firm Oliver Wyman confirms that financial representatives add substantial value to their customer's financial well-being.[77] This study focused on the role of financial representatives in the U.S. retirement system, and primarily drew upon proprietary surveys of more than 4,300 retail investors (the "Retail Investor Retirement Survey") and analysis of two datasets from IXI Services, a division of Equifax.[78] Based on the Retail Investor Retirement Survey, the study found that on average, individuals that use a financial representative have more assets than non-advised individuals across all the age and income levels examined. For example, concerning individuals with $100,000 or less in annual income (*i.e.*, middle-income individuals), Oliver Wyman found that advised individuals have a minimum of 38% more assets than non-advised individuals.[79] Moreover, with respect to individuals in or approaching retirement, the differences in assets are even more significant. On average, advised individuals ages 55 to 64 had 51% more assets than non-advised individuals, and those 65 and older had 113% more assets (*i.e.*, more than double) than the non-advised.[80] These are meaningful differences in assets for middle-

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[74] *Id.* at 74.

[75] *See Matters of Fact: Consumers, Advisors and Retirement Decisions (and Results)*, LIMRA Secure Retirement Institute, May 2015, http://www.limra.com/.

[76] *Id.* at 6. The identified savings goals were as follows: retirement (outside of the workplace), education, specific one-time large purchase (other than home), home purchase, vacation or travel, unexpected expenses/rainy day fund, home improvement, medical costs, and taxes.

[77] Oliver Wyman states that it "was engaged to perform a rigorous investigation of the role of financial advisors in the US retirement market, and quantify differences in investing behavior and outcomes between advised and non-advised individuals." *See* OLIVER WYMAN, *supra* n.62, at iii.

[78] *See id.* at iii-iv.

[79] *Id.* at 16.

[80] *Id.* at 16.

income individuals that use advisors, which should translate into significant improvements in their ability to save and invest for future goals.[81]

Oliver Wyman's analysis of the IXI dataset, representing approximately 20% of U.S. consumer-invested assets, substantiated its findings from the retirement survey. With respect to middle-income savers ($100,000 or less in annual income), Oliver Wyman found that on average, individuals who employ the services of an investment professional, like a broker, have had "at least 50% more" in total invested assets than others since at least 2006, the first year of the dataset.[82] This advantage in total invested assets rose throughout the 2009 recession and its immediate aftermath, and remained at "more than 200% more" in total invested assets from 2011 through 2013, the last year of the dataset. Clearly, the results of the study during the 2009 recession and its immediate aftermath are a testament to the benefit of receiving the assistance of a financial representative during a period of extreme market turmoil.

Oliver Wyman also found that advised individuals more often displayed investing practices "commonly associated with long term investing success," which included having more diversified portfolios, staying invested in the market by holding significantly less cash, taking fewer premature cash distributions, and rebalancing their investments to a desired asset allocation more frequently.[83]

We are concerned that, without the changes outlined in this letter, the Proposals will have the unfortunate, if unintended, consequence of significantly reducing access (by undermining the viability of continuing to service this market) to beneficial relationships with financial professionals for middle-income Americans. Our focus is to ensure that these hard-working Americans will be able to save and accumulate enough asset to meet their future needs.

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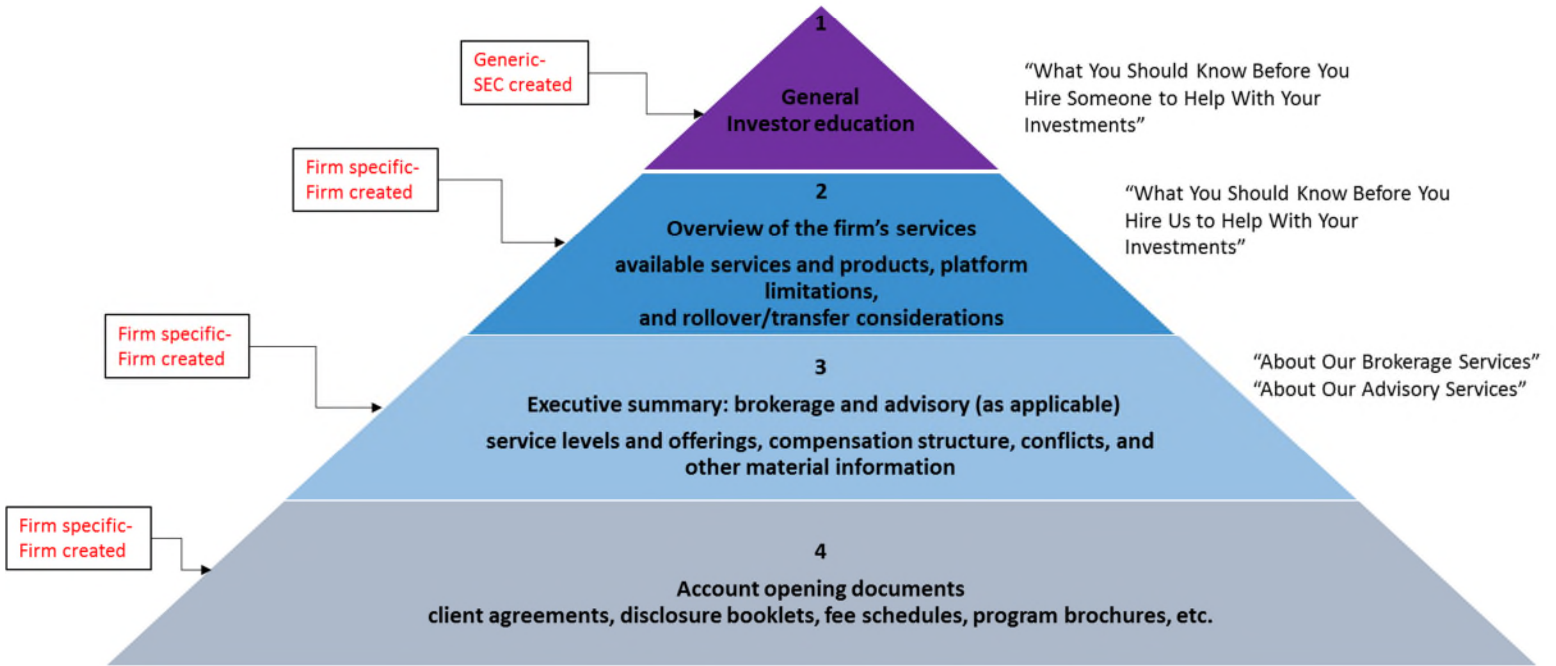
[81] The study states that their findings hold true, even when excluding survey respondents who anticipate receiving income from either an inheritance or trust fund.
[82] OLIVER WYMAN, *supra* n.62, at 17.
[83] *Id.* at 2.

APPRENDIX B

CONCEPT DISCLOSURES



(CONCEPT DRAFT/FOR CONSIDERATION)
Layer 1 SEC CREATED

What You Should Know Before You Hire Someone to Help with Your Investments

Broker-dealers and investment advisers offer many different ways you can get help with your investments. This brochure provides general information about key issues you should consider when comparing your options.

Available services, fee structures, and conflicts vary from firm to firm, so you should review disclosures carefully before making your decision.

What kinds of services do broker-dealers and investment advisers offer?

Both broker-dealers and investment advisers can recommend investment products and strategies, but there are some important differences in their services depending on the type of account you open. Account types:

- ***Broker-dealers: Execution only brokerage—***Some broker-dealers do not make recommendations. Their services are limited to custody, trade-execution and access to trading tools, education and research. These services are generally provided through a call center or internet website.
- ***Broker-dealers: Advised brokerage—***In advised brokerage, a broker-dealer can make recommendations for you to consider but you will make your investment decisions. A broker-dealer's recommendations are typically based on the circumstances at the time they are made to you without an obligation to monitor your investments on an on-going basis. If circumstances change, you will be responsible for making sure you seek new recommendations so that your investment mix stays right for your goals.
- ***Investment advisers: Non-discretionary and discretionary advisory services—***Investment advisers can recommend investments (like advised brokerage), and can also offer "discretionary" management services where the adviser makes the individual trading decisions for you. Many, but not all, investment advisers will monitor your account on an on-going basis—you should ask whether your account will be monitored and about the cost of this service.

Some firms are "dual-registrants" and can offer their services as either a broker-dealer or investment adviser, and can provide access to each of the services above.

When you are looking at different firms, you should find out what services they offer and think about whether their services match your needs.

What fees will I pay?

The fees you pay (and how you pay them) will be different depending on whether you use brokerage or advisory services. Fees and fee structures vary depending on the particular services you choose, and other factors, like how much you invest. Fees and expenses are an important factor in how your account performs over time, so you should make sure you understand what you will pay before you open an account for a particular service. In general:

- ***Broker-dealers typically charge a one-time commission or other fee when you buy or sell an investment.*** They do not charge a separate fee for their investment recommendations.

  Commission amounts depend on various factors like the type of investment and investment amount, and can be charged up-front when you buy, or when you sell. You should ask for the firm's commission schedule for more details. The actual amount of commissions you pay will be disclosed on the confirmation you receive after your trade.

  Commissions may be in addition to some typically smaller fees paid to broker-dealers from your investments over time. These include "Rule 12b-1 fees (from mutual funds) and placement fees. You can get information about these fees from the prospectuses or other offering documents of the investment products in which you invest.

	You may also pay account maintenance, margin interest, custody (including IRA custodial fees) and other fees for maintaining and administering your account. More information about brokerage fees is available from the SEC in "How to Open a Brokerage Account" and "Brokers' Miscellaneous Fees." • ***Investment advisers typically charge an additional fee for their advice.*** Unlike broker-dealers, investment advisers generally charge a separate fee for their advice. Advisory fees typically are charged on an on-going basis, such as monthly, regardless of the amount of trading in your account. They can be calculated as a percentage of the assets in your account, or a fixed dollar amount. Advisory fees can be in addition to commission and other transaction charges such as for execution of trades if they are not otherwise calculated as a percentage of assets in your account. You may also pay account maintenance, margin interest, custody (including IRA custodial fees) and other fees to a broker-dealer or custodian for maintaining and administering your account. More information about advisory fees is available from the SEC in "Opening an Investment Advisory Account" and Investor Publication "Investment Advisers: What You Need to Know Before Choosing One." ***When you are comparing different firms, you should ask about their fees (and compensation) and where you can get more information. You should also ask whether their fees are negotiable, whether lower fee options are available, and their policy of aggregating household accounts for better pricing.*** • ***Remember that account-level fees discussed here and paid directly to broker-dealers and investment advisers are in addition to the fees and expenses of the products you may invest in, such as the expense ratio of a mutual fund or insurance product.*** • ***Ongoing fees may seem small, but over time they can have a major impact on performance.*** For more information, please review the SEC Investor Bulletins "Ask Questions – Questions You Should Ask About Your Investments"; "How Fees and Expenses Affect Your Investment Portfolio"; and "Ten Things You Should Know About Investing." Additional information is on the SEC's Investor.gov website at https://www.investor.gov/introduction-investing/basics/investment-products.xxxxxxx
How else do broker-dealers and investment advisers make money?	Broker-dealers and investment advisers may earn money from various sources in addition to what you may pay directly, including: • ***Certain investment products in which you invest and from the products' sponsors and managers.*** This compensation generally depends on the amount you invest in the particular investment product and can be paid when you invest, an on-going basis or both. • ***Affiliated products.*** If the broker-dealer or investment adviser offers investment products provided, serviced or sponsored by it or an affiliate, your investment will generally result in additional compensation being paid to the firm or the affiliate. • ***Payment for order flow.*** Broker-dealers can also receive compensation from market centers called "payment for order flow" for directing your trades to the market centers. • ***Principal trades/Underwritings.*** Broker-dealers and investment advisers (with your approval) can trade with you for their own accounts on a "principal basis." When they do, they earn compensation by marking up the price of securities they sell to you, and marking down the price of securities they buy from you. They can also earn selling concessions for underwritings and IPOs for which the firm participates in the selling syndicate.

- ***Sweeps.*** If a broker-dealer or investment adviser offers a sweep program for uninvested cash in your account, the firm can earn additional revenue from the banks or money market funds that hold your cash.

- ***Margin.*** If you hold investments in a margin account, the broker-dealer can earn additional compensation from margin interest charged to you, as well as compensation it may receive for using assets held in the account for lending purposes.

Ask the firms you are considering about compensation they receive from other sources and where you can get more information. Even though you do not pay these fees directly, they affect your investment performance indirectly and should be considered part of the overall fees you are paying for services.

What conflicts do firms have?

Broker-dealers and investment adviser have conflicts to recommend, or invest your savings in, investment products, services, and transactions that result in them receiving greater compensation. Conflicts vary from firm to firm, but here are some general conflicts to look out for:

- ***Rollovers and asset transfers.*** Broker-dealers and investment advisers don't generally get paid unless you hire them. Thus, whether you are thinking about moving your assets from an account at another firm, or from your company retirement plan, you should know that the broker-dealer or investment adviser you are talking to has an incentive to encourage you to move your assets to their firm.

- ***Brokerage vs. Advisory.*** If you are working with a dual-registrant offering both advisory and brokerage services, the firm will have a conflict to encourage you to select the service that results in the most compensation for the firm. This will generally depend on your trading volume—if you trade a lot, the firm may have an incentive to get you into a brokerage account, but otherwise, advisory programs often result in the firm earning more compensation.

- ***Advisory Program A vs. Advisory Program B.*** Some advisory programs are more expensive than others, and investment advisers have an incentive to encourage you to pick the most expensive one. When making your choice, understand the differences in service levels, and choose the program that best services your needs.

- ***Product A vs. Product B.*** Firms are compensated more for some products than for others. For example, the commissions you pay to a broker-dealer for a variable annuity may be higher than the commissions you pay for a mutual fund. A mutual fund sponsor may pay a broker-dealer or investment adviser more for selling its mutual funds than it does for selling a similar exchange traded fund ("ETF"). And a firm might get more compensation for selling mutual funds from one fund family than it does from another fund family, or for selling mutual funds managed by an affiliate.

- ***Share classes.*** A firm may offer investment products in different share classes with different compensation amounts and structures and have an incentive to recommend you invest through the share class that results in the most compensation to the firm. Additionally, depending on the share class compensation structure, the firm may have an incentive to encourage you to buy and sell share classes with up-front commissions, and to hold share classes that pay compensation over time. Not all share classes are offered by all firms to all customers.

- ***Principal trade vs. agency trade.*** Broker-dealers and investment advisers have an incentive to encourage you to invest in securities they hold in inventory or where they are participating in an underwriting syndicate, and to execute trades against their proprietary accounts.

- ***Order routing.*** Broker-dealers have an incentive to route trades to market centers that pay them more.

	You should ask the firms you are considering about their conflicts of interest and how those conflicts affect their services to you. You should also ask for the firm's conflicts disclosures and review these disclosures before making investment decisions.
What conflicts do financial professionals have?	Broker-dealers and investment advisers compensate and incentivize financial professionals for working with investors. Financial professional compensation varies significantly from firm to firm, but is typically affected by the amount of client assets the financial professional is responsible for and the fees and commissions those assets generate. Compensation can include both (i) cash compensation and bonuses, and (ii) non-cash incentives like eligibility for sales clubs, trips, and other awards. Thus, financial professionals have an incentive to encourage you to invest your savings in the services, products, and transactions that result in the financial professional earning the most compensation. ***You should ask the firms you are considering about how financial professionals are compensated (both cash and non-cash) and what the firm does to mitigate and supervise those conflicts.***
How do broker-dealers' and investment advisers' obligations to investors differ?	Federal securities laws use different words to describe the standards that apply to broker-dealers ("best interest") and investment advisers ("fiduciary"), but both types of firms are required to take steps to make sure the investments and strategies they recommend or implement are appropriate or suitable for you. Additionally, broker-dealers and investment advisers are required to address their conflicts. Investment advisers can do this by disclosing their conflicts to you. Broker-dealers must take additional steps and both disclose ***and mitigate or eliminate*** certain conflicts.
What disclosures should I look at before deciding to hire a firm?	Each firm will make a number of disclosures available to you about their specific services, fees and compensation, and conflicts of interest. ***If you need help understanding these disclosures, ask the firm or financial professional for help.*** For information about how to check a financial professional's background, review the SEC Investor Bulletins "Check Out Brokers and Investment Advisers"; "Check Out Your Financial Professional"; and "Top Tips for Selecting a Financial Professional." To report a problem to the SEC, visit the SEC's Center for Complaints and Enforcement Tips or call the SEC's toll-free investor assistance line at (800) 732-0330. To report a problem to FINRA, visit www.finra.org/investors/problem or call FINRA's call center at (301) 590-6500.

(CONCEPT DRAFT/FOR CONSIDERATION)

Layer 2 – Firm Level

What You Should Know Before You Hire Us to Help You with Your Investments

Thank you for considering PFSI, Inc. ("PFSI") to help with your investments and savings goals. This pamphlet provides an overview of our services and other things you should consider before you hire us and move your assets to an account with us. More detailed information is available in our pamphlet "About Our Services," as well as in our account agreements and disclosures available at [CROSS-REFERNCE/LINK].

<table>
<tr><td>What kinds of services does PFSI offer?</td><td>As a registered broker-dealer and investment adviser, we offer you two ways to get help with your investments, including:
• Brokerage services where your representative will give you investment recommendations, but you make the ultimate decisions
• A discretionary investment advisory program where we take responsibility for making investment decisions for you
Each of these services is different, and has different account minimums, fees, and expenses.
We have a conflict of interest to encourage you to hire us for the service that results in greater compensation for us and our affiliates.
For more information about each of these services, including our conflicts of interest, see [CROSS-REFERENCE/LINK].</td></tr>
<tr><td>What kinds of investment products does PFSI offer?</td><td>We offer access to mutual funds, ETFs, and annuities through our brokerage and advisory platforms.
The products we offer are provided and managed by third parties other than us.
We receive payments for marketing and distribution support and other services we provide with respect to third-party products as disclosed in the applicable prospectus or offering document. We have a conflict of interest to encourage you to buy, sell, and hold investments that result in greater compensation for us and our affiliates.
Our platforms do not offer access to all investment products in the universe, and other firms may offer different products or the same products at different cost.</td></tr>
<tr><td>How are PFSI financial professionals compensated?</td><td>We pay our representatives a portion of the fees and commissions you pay to us and we provide other benefits to representatives based on their performance.
Generally, representative compensation depends on the amount of customer assets for which they are responsible and sales of investment products they generate. Thus, representatives have an incentive to encourage you to invest more assets and buy, sell, and hold investments that result in more compensation.
More information about financial professional compensation is available in [CROSS-REFERENCE/LINK]</td></tr>
<tr><td>What if I am moving assets from an employer-sponsored plan or IRA?</td><td>Moving assets from a tax-qualified account, like an account in a 401(k) plan or IRA, requires special considerations. Please see our pamphlet "INSERT TITLE" for more information.</td></tr>
</table>

(CONCEPT DRAFT/FOR CONSIDERATION)

Layer 3 – Firm Level

About Our Services

As a broker-dealer and investment adviser, PFSI, Inc. offers you different ways to meet your investment needs, including a choice of service levels and ways to pay for them. This disclosure summarizes important information regarding our brokerage and advisory services for you. For more information about our services, see our client agreements and other disclosures available at http://www.xyz.com/disclosures. If you would like to change your services, please talk to your Representative. Other firms may offer different or similar services as we do, and may offer access to different or similar investment products—potentially at a lower cost. This disclosure statement does not modify your agreements with us.

WHEN WE PROVIDE BROKERAGE SERVICES…

- We execute investment trades ***at your direction*** on an agency basis as broker.
- We receive ***transaction-based compensation*** for trades you choose to implement, including commissions, revenue sharing, and other types of compensation that are disclosed to you in our brokerage disclosure booklet, your brokerage agreement and online at (www.xyz.com). We also charge monthly custodian fees for maintaining your account with us. We disclose the exact cost of each transaction on your trade confirmations and we will send you account statements with additional details on the fees you pay.
- Unlike how we charge for investment advisory services, we ***do not charge or receive a separate fee for our advice or recommendations*** and our recommendations are provided ***solely incidental*** to our brokerage services.
- The federal securities laws and FINRA rules require us to:
  - ***Deal fairly*** with you.
  - Ensure that ***prices you receive on trades are favorable*** considering market conditions, and that our brokerage-related
  - Provide recommendations that are appropriate for you given your individual financial circumstances, needs, and goals (based on information you provide), and not put our interests ahead of your interests.

Although brokerage services may be a cost effective way of investing your retirement assets, it is not for everyone. As a brokerage client, you need to understand and agree to our service limitations and conflicts.

WE DO NOT ACT AS A "FIDUCIARY" OR REGISTERED INVESTMENT ADVISER

Unlike fiduciary investment advisers that charge ongoing advisory fees, we are compensated when you choose to implement trades. Thus, ***we have a financial interest in your decision*** to follow our investment recommendations.

Accordingly, ***we do not act as a "fiduciary"*** under federal law when we provide brokerage recommendations for your account assets, or as a registered investment adviser.

You are responsible for ***evaluating*** and deciding whether to direct trades we recommend, after considering our conflicts.

WE HAVE NO DUTY TO PROVIDE ONGOING RECOMMENDATIONS OR MONITOR YOUR INVESTMENTS

We are not obligated to provide recommendations to you, or to update recommendations made previously, and our silence should not be viewed as a recommendation to hold an investment.

We will not (and have no obligation to) monitor your account investments on an ongoing basis.

You are responsible for ***independently ensuring*** that the investments in your account remain appropriate, given your investment objectives, risk tolerance, financial circumstances, and investment needs.

If you would like us to act as an investment fiduciary for your assets and provide ongoing investment advice and monitoring, then consider enrolling in our investment advisory program.

CONFLICT OF INTEREST
TRANSACTIONAL COMPENSATION

When we act as your broker, we and our representatives earn more depending on the types and frequency of your trades. We are compensated by the commissions and fees you pay us (as disclosed at www.xyz.com). We also receive payments from third parties, including the investment products in which you invest and their sponsors. These third-party fees are disclosed in the investment product's prospectus and other offering documents.

This creates an incentive for us to recommend that you:

- invest in investment products that result in greater compensation to us; and
- trade more frequently.

By choosing brokerage for your personal assets, you understand these conflicts and limitations and agree that we are not acting as a "fiduciary" with respect to any recommendations we may provide with respect to the assets held in your brokerage account. You also acknowledge that your Brokerage Account Agreement contains a more fulsome discussion of these conflicts and limitations. If you have any questions or concerns, please contact us at (XXX) XXX XXXX or talk to your Financial Representative.

WHEN WE PROVIDE ADVISORY SERVICES…

- Depending on the services you select, we will make certain asset allocation model recommendations and ***we will make and implement investment decisions for you***.
- We receive an ***on-going advisory fee*** that is a percentage of the value of the assets in your advisory account. We also receive

  fees, omnibus recordkeeping fees, and other types of compensation that are disclosed to you in our brochure, your advisory agreement and online at (www.xyz.com). Your custodian (which may be one of our affiliates) charges monthly custodian fees for maintaining your account. The exact amount of fees you pay will be disclosed to you on the account statement you receive from the account custodian.
- As an investment adviser fiduciary, we have a duty to:
  - ***Deal fairly*** with you and provide ***full and fair disclosure of material facts***, including conflicts of interest.
  - Provide recommendations that we reasonably determine are ***suitable*** for you given your individual financial situation, investment objectives and goals (based on information you provide).

We believe that professional investment advisory programs can help investors reach their investment objectives. However, the fees and expenses associated with advisory services may exceed those that apply to brokerage services, and depending on your circumstances advisory services may not be appropriate. Please speak with your Representative for additional information.

WE ACT AS A "FIDUCIARY" AND REGISTERED INVESTMENT ADVISER

We are viewed as a "fiduciary" under federal securities law when we act as a registered investment adviser to provide investment recommendations and management services to you and your account.

Our interests can conflict with your interests. We are required to disclose our material conflicts to you so you can decide whether to agree to them. You are responsible for ***evaluating*** our investment advice and management services and deciding whether to use our services, after considering our conflicts.

WE PROVIDE ONGOING ADVICE AND MONITOR YOUR INVESTMENTS

Under our client agreements, we will provide advice and management services (as applicable) on an ongoing basis.

We will also monitor your account investments on an ongoing basis.

If you do not want to pay for ongoing investment advice and monitoring, then consider opening a brokerage account with us instead.

CONFLICT OF INTEREST
ASSET BASED COMPENSATION

When we act as your investment adviser, we and our representatives earn more the more money you invest in your advisory account, and we earn the same advisory fee regardless of how frequently you trade. We also receive payments from third parties, including the investment products in which you invest and their sponsors. These third-party fees are disclosed in the investment product's prospectus and other offering documents.

This creates an incentive for us to recommend that you:

- increase the assets in your advisory accounts to increase our fees; and
- invest in investment products that result in greater compensation to us (including, services provided by us and our affiliates or those for which we receive a portion of product-level fees that you pay).

By choosing advisory for your personal assets, you understand these conflicts and limitations and that you will pay a separate ongoing asset based fee for our services. You also acknowledge that your Advisory Account Agreement and our brochure contain a more fulsome discussion of these conflicts and limitations. If you have any questions or concerns, please contact us at (XXX) XXX XXXX or talk to your Financial Representative.