



**STATEMENT FOR THE RECORD**

**SUBMITTED TO THE**

**HOUSE FINANCIAL SERVICES COMMITTEE,  
SUBCOMMITTEE ON INVESTOR PROTECTION,  
ENTREPRENEURSHIP AND CAPITAL MARKETS**

**“PUTTING INVESTORS FIRST? EXAMINING THE SEC’S BEST  
INTEREST RULE”**

**March 14, 2019**

**AARP  
601 E Street, N.W.  
WASHINGTON, D. C. 20049**

**Submitted By  
Lee Baker, CFP®  
AARP Georgia State President**

**For further information contact:  
Jasmine R. Vasquez  
Financial Security & Consumer  
Affairs, Government Affairs  
202-434-3711**

On behalf of our 38 million members and all Americans saving for their retirement, AARP thanks Chairwoman Maloney, Ranking Member Huizenga, and members of the Subcommittee on Investor Protection, Entrepreneurship and Capital Markets for tackling this important issue and hosting today's hearing. We appreciate the opportunity to testify on the Security and Exchange Commission's (Commission) proposed Regulation Best Interest (BI) and Customer Relationship Summary (CRS) disclosure form.

AARP is the nation's largest nonprofit, nonpartisan organization dedicated to empowering Americans 50 and older to choose how they live as they age. With nearly 38 million members and offices in every state, the District of Columbia, and the U.S. territories, AARP works to strengthen communities and advocates for what matters most to families with a focus on financial security, retirement planning, healthcare, and protection from financial exploitation.

A priority for AARP is to assist Americans in accumulating and effectively managing adequate retirement assets to supplement Social Security. Nearly half of our members are employed full or part-time, with many of their employers providing retirement plans. The shift from defined benefit plans to defined contribution plans has transferred significant responsibility to individuals for investment decisions that directly impact the adequacy of the assets available to fund future retirement needs. Unfortunately, the state of America's retirement landscape is cause for great concern. According to calculations by the Center for Retirement Research at Boston College, only about half of households have retirement savings and the "retirement income deficit" for American households continues to grow.<sup>1</sup> According to recent analysis by EBRI, 47 percent of workers in 2017 reported that the total value of their household's savings and investments, not just for retirement, was less than \$25,000 and 24 percent had less than \$1,000.<sup>2</sup> Given these trends, it is critical to do all we can to help Americans keep as much of their hard-earned nest egg as possible and AARP has historically supported the development of rules and regulations that protect savers when they make investment decisions concerning their retirement monies. We believe that without such protections, it is difficult for individuals to effectively plan for a secure and adequate retirement.

All financial professionals should act in the best interest of the savers they are serving -- they should put the client's best interest first and ahead of their own. AARP members and the public have generally demanded and supported the protections of a fiduciary standard. In survey after survey, we have found that retirement savers overwhelmingly want advice that is in their best financial interest. In a 2018 poll, almost 70 percent of respondents agreed that the government should establish a rule that would require financial professionals to give advice that is in the best interest of the account holders when giving advice about retirement accounts.<sup>3</sup> In addition,

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<sup>1</sup> Alicia H. Hummell, *401(K)/IRA Holdings in 2013: An Update from the SCF* (Sept. 2014), [http://crr.bc.edu/wp-content/uploads/2014/09/IB\\_14-151.pdf](http://crr.bc.edu/wp-content/uploads/2014/09/IB_14-151.pdf).

<sup>2</sup> Lisa Greenwald et al., *The 2017 Retirement Confidence Survey: Many Workers Lack Retirement Confidence and Feel Stressed About Retirement Preparations* (Mar. 21, 2017), [https://www.ebri.org/pdf/briefspdf/EBRI\\_IB\\_431\\_RCS.21Mar17.pdf](https://www.ebri.org/pdf/briefspdf/EBRI_IB_431_RCS.21Mar17.pdf). This figure refers to the total value of their household's savings and investments, excluding the value of their primary home.

<sup>3</sup> AARP 2018 Mid-Term Voter Issues Survey (2018), <https://www.aarp.org/content/dam/aarp/politics/advocacy/2018/08/aarp-national-multi-issue-voter-survey-Q21.pdf>.

in a 2013 AARP survey of over 1,400 adults who had money saved in either a 401(k) or a 403(b) plan, more than nine in ten (93 percent) respondents favored requiring retirement advice to be in their sole interest, and fewer than four in ten (36 percent) respondents indicated they would trust the advice from an adviser who is not required by law to provide advice that is in their best interests.<sup>4</sup> A survey taken after the Department of Labor's (DOL) Fiduciary Rule was promulgated demonstrated that an overwhelming percentage of respondents were in favor of the rule and believed it was important for financial professionals to give advice in a client's best interest.<sup>5</sup> Among those individuals who have received professional financial advice, the support was the deepest, with nearly 8 in 10 (78 percent) strongly agreeing with a fiduciary rule.

In April 2018, AARP applauded the Commission's important first step to tackling this issue and developing rules aimed at helping retail investors make informed investment decisions. We believe that the Commission can play a critical role in ensuring that all financial industry professionals, who provide retail clients with advice about securities, are held to a clear and uniform standard of conduct where the advice is solely in the interest of the investor. AARP also appreciates the opportunity to respond to the Commission's request for public comment on standards of conduct for registered investment advisers (IA) and broker-dealers (BD) and we have done so on a number of occasions both in writing, as well as at local town halls and meetings with many of the Commissioners and Chairman.

We have also undertaken a couple of rounds of independent testing of the Commission's proposed disclosure, the Customer Relationship Summary (CRS), most recently in December 2018. Recognizing the important role the CRS plays in the Commission's proposed regulatory approach to Regulation Best Interest, AARP hired Kleimann Communications Group, a non-affiliated third party, for two separate research projects. The first project was concluded in September 2018 and the findings were filed with the Commission.<sup>6</sup> That research was centered on testing the combined BD and IA services disclosure with typical consumers using the Commission's Dual Registrant Mock-up of Form CRS. In that study we found that overall participants had difficulty distinguishing the standards of conduct between different financial professionals, they did not understand how conflicts of interest could affect them, and they struggled with the language used on the form, especially with respect to fees and conflicts of interest.

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<sup>4</sup> AARP, *Fiduciary Duty and Investment Advice: Attitudes of 401(k) and 403(b) Participants* (Sept. 2013), <http://www.aarp.org/research/topics/economics/info-2014/fiduciary-duty-and-investment-advice---attitudes-of-401-k--and-4.html>.

<sup>5</sup> S. Kathi Brown, *Attitudes Toward the Importance of Unbiased Financial Advice* 4, 6 (May 2016), [http://www.aarp.org/content/dam/aarp/research/surveys\\_statistics/econ/2016/attitudes-unbiased-fin-advice-rpt-res-econ.pdf](http://www.aarp.org/content/dam/aarp/research/surveys_statistics/econ/2016/attitudes-unbiased-fin-advice-rpt-res-econ.pdf).

<sup>6</sup> Letter from AARP, the Financial Planning Coalition, and the Consumer Federation of America to the SEC, dated Sept. 11, 2018, available at <https://www.sec.gov/comments/s7-08-18/s70818-4341455-173259.pdf>.

In December 2018, and much like our first round of testing, our findings clearly indicated the need for the Commission to rethink, revise, and retest the content, language, and format of the CRS, as well as its underlying policy. During this testing, we found multiple opportunities to amend the CRS and improve the experience of the retail investor. Most significant was the challenge retail investors experienced when trying to understand the underlying best interest standard, which continued to cause confusion and ultimately rendered retail investors unable to make informed decisions about which type of account or service would be best for them.<sup>7</sup>

This finding has amplified for our organization the reality that adoption of a uniform standard -- that would apply to both BDs and IAs when providing personalized investment advice to retail customers, as contemplated by Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Section 913) -- is of critical importance and long overdue. The standard should be based on the core principle that when providing personalized investment advice to retail customers, a financial professional must always act in the best interest of those customers regardless of their marketing strategy, business model, or registration status. Ensuring that all financial professionals who offer investment advice to retail investors are subject to a fiduciary standard is needed to ensure a level and transparent market for consumers seeking investment advice.

As we have in the past, we continue to urge the Commission to continue developing and testing its regulatory package until it can clearly communicate the meaning and scope of the new best interest standard, and be certain that the disclosures that form the centerpiece of its regulatory package function to support informed investor decision-making.

**I. Despite The Commission's Best Effort, The Proposed Regulation Best Interest Undercuts Retail Investors' Ability To Distinguish Between The Standards Of Care Applicable To Financial Professionals.**

Both BDs and IAs play an important role in helping Americans manage their financial lives, and accumulate and manage retirement savings. Retail investors receiving investment advice should get a consistent standard of care that is solely in their best interest, regardless of whether the advice comes from a BD or an IA. In 2011, AARP supported the SEC staff recommendation in its Section 913 Study to adopt parallel rules under the Advisers Act and the Securities Exchange Act of 1934 establishing an over-arching fiduciary duty that is identical for BDs and IAs but only if, as the Dodd-Frank Act mandates, it is no less stringent than the existing standard under the Advisers Act. We believe that such an approach, if properly implemented, could both enhance

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<sup>7</sup> Letter from AARP and CFP Board to the SEC, dated Dec. 7, 2019, available at <https://www.sec.gov/comments/s7-07-18/s70718-4729850-176771.pdf>.

investor protections and preserve key beneficial elements of the transaction-based BD business model.

AARP appreciates that the Commission's proposal under discussion today seeks to impose a higher standard than the existing suitability standard on BDs. AARP has long supported advice in the best interest of individuals saving and investing. To that end, AARP was very supportive of the DOL's fiduciary rule, which required that retirement investment advice be in the best interest of the client saving for retirement -- that means advice that minimizes conflicts of interest, is solely in the interest of the client, and which is provided with the care, skill, prudence and diligence that a prudent person would use. Unfortunately, in its current form, the Commission's proposed Regulation Best Interest rule does not impose a fiduciary standard and further fails to define the contours of the "best interest" standard. Absent a full fiduciary standard, investors will continue to be vulnerable and will not receive the protections they need and deserve. AARP has long stated that a suitability standard does not protect investors from the potentially detrimental impact of conflicted advice. AARP recommends that the Commission amend its proposal and adopt the state trust definition of best interest (which the Employee Retirement Income Security Act (ERISA) also adopted). Such a definition is of long-duration and understandable to industry stakeholders and consumers. A financial professional would have to make recommendations both "solely in the interest" of the consumer and with the "care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use." Quite simply, it is not enough for the financial professional to solely rely on their own opinion. The professional must assess what a prudent expert would recommend and document their decision-making process.

**a. The Proposed Regulation Best Interest leaves investors confused and at risk.**

AARP commends the Commissions' effort to restrict the use of the terms "adviser" and "advisor" by a BD in its CRS. The regulatory imbalance between the duties of BDs and IAs has persisted for many years, even as evidence demonstrating that brokers have transformed themselves from salesmen into advisers has grown. Many BDs today call themselves "financial advisers," offer services that clearly are advisory in nature, and market themselves based on the advice offered. For example, one firm advertises that it "proudly strive[s] to embrace [its] own fiduciary responsibilities" and that its "highest value is to 'always put the client first,'"<sup>8</sup> even though its Form ADV brochure (a regulatory filing that the SEC requires to be given to clients after a transaction is completed) demonstrates otherwise, noting that "[d]oing business with our affiliates could involve conflicts of interest if, for example, we were to use affiliated products and services when those products and services may not be in our clients' best interests."<sup>9</sup> As a result of such marketing and misleading statements, the average investor

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<sup>8</sup> Letter from Robert Reynolds, President and CEO of Putnam Investments, to U.S. Dep't of Labor (July 20, 2015), *available at* <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-ZA25/00077.pdf>.

<sup>9</sup> Putnam Advisory Company, LLC, SEC Form ADV Part 2A at 25 (Mar. 30, 2016), *available at* [http://www.adviserinfo.sec.gov/IAPD/Content/Common/crd\\_iapd\\_Brochure.aspx?BRCHR\\_VRSN\\_ID=375046](http://www.adviserinfo.sec.gov/IAPD/Content/Common/crd_iapd_Brochure.aspx?BRCHR_VRSN_ID=375046). (Putnam Investments wholly owns Putnam Advisory Company through various subsidiaries.)

cannot distinguish between BDs and IAs and does not recognize that their “financial adviser” operates under a lower legal standard than that to which an investment adviser is held. Nor is it surprising that investors expect that those who advertise themselves as a trusted adviser will provide financial advice in the best interest of the investor.

Federal regulations have not kept pace with changes in business practice, and BDs and IAs continue to be subject to different legal standards when they offer advisory services. According to the Commission’s 2011 Study on Investment Advisers and Broker-Dealers, as of the end of 2009, FINRA-registered BDs held over 109 million retail and institutional accounts and approximately 18 percent of FINRA-registered BDs also are registered as IAs with the Commission or a state.<sup>10</sup>

Consumers and regulators face a fundamental problem – there are tens of thousands of financial products, many of which contain complex rules, requirements, and fees. Regulators face the enormous challenge of ensuring that these products are fairly structured and sold, and that consumers understand all of the key terms and conditions of these products. Where there are different standards of conduct dependent merely upon which investment and for what purpose the investment will be used, the result can be not only continued investor confusion and reduced personal savings but also an unfair system which only the most sophisticated investors can navigate.

Ensuring all securities professionals who offer investment advice to retail investors are subject to a fiduciary standard is needed to ensure a level and transparent market for investors seeking advice. Investors deserve a regulatory system that is designed to promote their best interests and imposes comparable standards on investment professionals who are performing essentially the same functions. Research has found that investors typically rely on the recommendations they receive from BDs and IAs alike. The trust most investors place in financial professionals is encouraged by industry marketing, leaving investors vulnerable not only to fraud but also to those who would take advantage of that trust in order to profit at their expense. Investors who place their trust in salespeople who market services as acting in their best interest can end up paying excessively high costs for higher risk or underperforming investments that only satisfy a suitability standard but not a fiduciary standard. That is money most middle-income investors cannot afford to lose.<sup>11</sup>

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<sup>10</sup> S.E.C., *Study on Investment Advisers and Broker-Dealers* (Jan. 11, 2011).

<sup>11</sup> See Craig Copeland, *2015 Update of the EBRI IRA Database: IRA Balances, Contributions, Rollovers, Withdrawals, and Asset Allocation*, EBRI ISSUE BRIEF NO. 437, at Figures 2, 4, 6, 19 (Sept. 2017), [https://www.ebri.org/pdf/briefspdf/EBRI\\_IB\\_437\\_IRAs.12Sept17.pdf](https://www.ebri.org/pdf/briefspdf/EBRI_IB_437_IRAs.12Sept17.pdf) (finding that the average IRA account balance in 2015 was \$99,017, but 45% of those owning IRAs had less than \$25,000 in their accounts at year-end 2015; accounts were largest closest to retirement age); Alicia H. Munnell & Anqi Chen, *401(k)/IRA Holdings in 2016: An Update from the SCF* (Issue Brief No. 17-18), Ctr. for Retirement Research at Boston College (Oct. 2017), <http://crr.bc.edu/briefs/401k-ira-holdings-in-2016-an-update-from-the-scf/> (households approaching retirement had approximately \$135,000 in 401(k) and IRA assets which provides only \$600 per month in retirement).

These are not theoretical issues and the risk includes direct harm to the retirement savings of retail investors. For example, AARP recently spoke with Anna Duressa Pujat, a retired university librarian who contributed to her employer provided retirement account for 20 years before retiring.<sup>12</sup> When Anna retired, she rolled her savings into a ROTH IRA and was ultimately deceived twice by unscrupulous advisers. Anna states, “I want people to know that investors often don’t know what is happening with their accounts until something goes wrong... even with the information at one’s disposal, it can be hard to fully comprehend.” Anna and her husband shared that outside of their home, her retirement accounts were their greatest financial assets and they depend on this money for their basic needs and financial security. After suffering the financial losses from exorbitant service fees and inappropriate and risky investments with her retirement funds from previous advisers, Anna recently shared, “Having the fiduciary rule would give me confidence that I am receiving the financial guidance I know I need.”

Retiree Janice Winston also testified at a Senate briefing on the importance of unconflicted advice and in her testimony she shared, “I thought that anyone I paid to advise me would be guided only by my best interests. This is important, because I really have no good way to evaluate whether my investments are performing well or whether I am paying too much in fees. Imagine my surprise when I learned that my investment adviser was not necessarily required to act in my best interest.”<sup>13</sup>

**b. The duties of brokers must be clearly defined.**

The Commission’s proposal does not define a best interest standard. Instead the question of whether a BD acted in the best interest of its retail investor is left to be determined by consideration of the facts and circumstances surrounding the recommendation. However, AARP’s research indicates that investors do not understand the different legal standards that apply to different types of financial professionals. Investors believe that financial professionals are required to act in the investor’s best interest. Further, older Americans may not be able to tell you the precise legal definition of fiduciary but they have clear views on what they expect from financial professionals.

In six state specific opinion polls conducted by AARP, AARP asked residents age 50 plus questions related to the various investor and consumer reforms.<sup>14</sup> Respondents overwhelmingly favored requiring financial professionals to put the consumer’s interest ahead

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<sup>12</sup> See Declaration of Anna Duressa Pujat, attached to AARP’s Motion to Intervene in Chamber of Commerce v. U.S. Dep’t of Labor, Case No. 17-10238 (5th Cir. filed Apr. 26, 2018).

<sup>13</sup> Pension Rights Center, Retiree Janice Winston speaks out in support of strong fiduciary regulations (September 13, 2013), <http://www.pensionrights.org/newsroom/speeches-statements/retiree-janice-winston-speaks-out-support-strong-fiduciary-regulation-0>

<sup>14</sup> To view the state-specific surveys go to [http://www.aarp.org/money/scams-fraud/info-04-2010/finprotect\\_states.html](http://www.aarp.org/money/scams-fraud/info-04-2010/finprotect_states.html).

of their own when making recommendations. In addition to a fiduciary duty of care, respondents favored upfront disclosure of fees, commissions, and potential conflicts that could bias advice. The level of support for this commonsense reform ranged from a low of 88 percent (Arkansas) to a high of 95 percent (Indiana).<sup>15</sup> Moreover, not only do investors believe that investment advice should be provided in their best interests, but the financial services industry generally agrees. See, e.g., SIFMA Comment Letter 506 to DOL (“The industry ... shares that goal” “to ensure financial services providers are looking out for their customer’s best interest”).<sup>16</sup> For decades, registered IAs and certified financial planners have successfully and profitably provided fiduciary advice. Expanding that model to the BD space would provide consistency across the regulatory landscape as well as much need consumer protection.

## **II. Failure To Impose A Fiduciary Standard Undermines The Financial Security Of Americans Saving For Retirement.**

As consumers move closer to retirement, they may be more vulnerable to the negative impact of advice that is not in their best interests for three reasons: (1) the assets they have to invest are larger; (2) they may lack strong financial literacy skills;<sup>17</sup> and, (3) reduced cognition may affect financial decision-making.<sup>18</sup> In addition, the detrimental effects of advice that is not in the investors’ best interests may have the most negative potential impact on individuals with modest balances<sup>19</sup> as they have fewer economic resources -- any additional costs or losses diminish what little savings they have. For all these reasons, investors close to retirement are especially vulnerable as they make significant and often one-time decisions such as moving retirement savings out of more protected employer-based plans.

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<sup>15</sup> *Id.*

<sup>16</sup> <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00506.pdf>.

<sup>17</sup> Annamaria Lusardi, et al., *Financial Literacy and Financial Sophistication in the Older Population: Evidence from the 2008 HRS* (Sept. 2009), <http://www.mrrc.isr.umich.edu/publications/papers/pdf/wp216.pdf> (“In view of the fact that individuals are increasingly required to take on responsibility for their own retirement security, this lack of [financial] knowledge has serious implications.”); see also Annamaria Lusardi & Olivia S. Mitchell, *Financial Literacy and Planning: Implications for Retirement Wellbeing*, Nat’l Bureau of Econ. Research Working Paper 17,078, at 6 (May 2011), <http://www.nber.org/papers/w17078.pdf> (one-third of survey respondents did not understand compound interest, one-quarter did not understand inflation implications and half did not know about risk diversification).

<sup>18</sup> E.g., Keith Jacks Gamble, et al., *How Does Aging Affect Financial Decision Making?* (Issue Brief No. 15-1), Ctr. for Retirement Research at Boston College, at 1, 6 (Jan. 2015), [http://crr.bc.edu/wp-content/uploads/2015/01/IB\\_15-1-508.pdf](http://crr.bc.edu/wp-content/uploads/2015/01/IB_15-1-508.pdf) (declining cognition begins to accelerate after age 60 and has a noticeable effect on financial literacy; “given the increasing dependence of retirees on 401(k)/IRA savings, cognitive decline will likely have an increasingly significant adverse effect on the well-being of the elderly.”); see generally Tara Siegel Bernard, *As Cognition Slips Financial Skills Are Often the First to Go*, NEW YORK TIMES (Apr. 24, 2015), [http://www.nytimes.com/2015/04/25/your-money/as-cognitivity-slips-financial-skills-are-often-the-first-to-go.html?\\_r=0](http://www.nytimes.com/2015/04/25/your-money/as-cognitivity-slips-financial-skills-are-often-the-first-to-go.html?_r=0) (“A person’s financial decision-making ability peaks at age 53, or more generally, in their 50s”).

<sup>19</sup> See n. 1, *supra*.

Increasingly, the way that most Americans save and invest is through their employer sponsored retirement plans, most typically a 401(k) type savings plan. The Government Accountability Office (GAO) has estimated that \$20,000 in a 401(k) account that had a one percentage point higher fee for 20 years would result in an over 17 percent reduction in the account balance, a loss of over \$10,000.<sup>20</sup> We estimate that over a 30-year period, the account would be about 25 percent less. Even a difference of only half a percentage point — 50 basis points — would reduce the value of the account by 13 percent over 30 years. Conflicted advice resulting in higher fees and expenses can have a huge impact on retirement income security levels.

Lower and middle-income retirement investors need every penny of their retirement savings. “Among the 48 percent of households age 55 and older with some retirement savings, the median amount is approximately \$109,000 — commensurate to an inflation-protected annuity of \$405 per month at current rates for a 65- year-old.”<sup>21</sup> DOL likewise reported that “small investors” (that is, those with low balances or those with modest means) are most negatively impacted by the detrimental effects of conflicted advice. Those with small accounts have fewer economic resources, and consequently any additional costs or losses diminish what little savings they have worked so hard to amass.

### **III. The Proposed CRS Form Should Be Simplified In Order To Better Meet The Needs Of Investors And Facilitate Informed Decision-making.**

AARP believes that the CRS combined with a strong and enforceable best interest standard could provide invaluable investor protections to Americans saving for retirement. We applaud the Commission’s objectives in proposing a CRS that seeks to “fill the gaps” between investor expectations and legal requirements by “mandating clear disclosures” about how financial professionals describe the customer relationship to retail investors.<sup>22</sup>

However, AARP encourages the Commission to amend and continue testing its CRS in order to ensure a more easily used and valuable resource for retail investors. AARP conducted two rounds of usability testing in 2018. What we found was that a short, plain language, user-friendly form with key information, enabling retail investors to evaluate BDs’ and IAs’ obligations to them are essential characteristics of a useful tool. In our testing, the overall level of comprehension of the complex disclosure among participants was poor; most participants did not understand disclosures regarding legal obligations; participants understood the

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<sup>20</sup> U.S. Gov. Accountability Office, *GAO-07-21, Private Pensions: Changes Needed to Provide 401(k) Plan Participants and the Department of Labor Better Information on Fees* 7 (Nov. 2006).

<sup>21</sup> U.S. Gov’t. Accountability Office, *GAO-15-419, Retirement Security: Most Households Approaching Retirement Have Low Savings* 11 (May 2015), <http://www.gao.gov/assets/680/670153.pdf>.

<sup>22</sup> <https://www.sec.gov/news/public-statement/clayton-overview-standards-conduct-investment-professionals-rulemaking>

existence but not the import of conflicts of interest; and participants were deeply confused by the disclosure of fees and costs -- both the many types and number of fees described in the CRS' Costs and Fees section.

To be effective, it is imperative that the CRS provide information in a manner that is clear, understandable, and not overwhelming in order to facilitate the retail investor's ability to make informed decisions about their investments. Retail investors should be empowered to make informed decisions. They should understand their choices and what they are selecting -- especially when their hard earned savings are on the line. Numerous surveys have shown that consumers need and want complete disclosures concerning their investment options in order to help them make informed decisions about their investments.<sup>23</sup> Financial professionals should be required to tell prospective and engaged retail investors the applicable standard of care and nature of their relationship. The more consistent the standards of care available, the less confusion we can anticipate on the part of retail investors. In addition, clarity is key to breaking through investor confusion -- especially around complex financial investment instruments. During the April 18, 2018, open meeting on Standards of Conduct for Investment Professionals, Chairman Clayton stated:

Misalignment between reasonable investor expectations and actual legal standards can cause investor harm. For example, retail investors may be harmed if they do not understand when BDs and IAs may have conflicting financial interests. In addition, without sufficient clarity, retail investors may be more deferential to, or place greater reliance on, their BD or IA than they otherwise would. I believe that clarifying the legal standards of conduct that apply and reducing investor confusion through disclosure can significantly mitigate these potential harms as well as increase investor protection.<sup>24</sup>

Chairman Clayton further stated, "Put bluntly, we want investors to understand who they are dealing with, i.e., what category — IA, BD, or dual-hatted — their investment professional falls into and, then, what that means and why it matters."<sup>25</sup> This intent, as described by Chairman Clayton, is exactly the right one and would benefit retail investors. In order to meet that objective, however, the CRS should be updated to meet a number of critical core components.

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<sup>23</sup> The report is titled *401(k) Participants' Awareness and Understanding of Fees*, available at <https://assets.aarp.org/rqcenter/econ/401k-fees-awareness-11.pdf>.

<sup>24</sup> <https://www.sec.gov/news/public-statement/clayton-overview-standards-conduct-investment-professionals-rulemaking>

<sup>25</sup> *Id.*

First, the standard of care should be clear, concise, and defined. Distinctions between different standards of care should be clear and easy for “Mr. and Mrs. 401(k)”<sup>26</sup> -- the average retail investor -- to understand. The standard of care should be explained in plain language and terms like “fiduciary” and “best interest,” which are used in the three iterations of the relationship summary currently available, must be well-defined.

In addition, the CRS should be reformatted. The forms should be short, with a layered approach and/or supplemental pages included in order to allow access to information while avoiding information overload. The information disclosed should be written plainly and concisely, for the purpose of informing the investor, not simply to meet a legal standard. The fee structure should be straightforward and should avoid technical jargon. Finally, the forms should be shared with retail investors in a timely manner, prior to any decisions or actions that may be taken.

**a. Standards of Care must be clearly defined.**

The Commission’s hypothetical, four-page relationship summary forms are intended to explain and clarify whether retail investors are working with an IA, BD, or dually registered representative. Unfortunately, we believe the intended clarity is lost in the forms as currently drafted.

For example, under “Obligations to You,” the relationship summary forms fail to distinguish between the BD’s new “best interest” standard and the investment adviser’s existing “fiduciary” obligation.<sup>27</sup> The duty of IAs is explained as, “We are held to a fiduciary standard that covers our entire investment advisory relationship with you.” Nowhere in the relationship summary is the technical term “fiduciary standard” defined. The BD obligation is illustrated as “We must act in your best interest and not place our interest ahead of yours when we recommend an investment strategy involving securities.” However, the practical definition and application of acting in the “best interest” is not articulated in the standalone relationship summary for BDs.<sup>28</sup> This leaves many open questions – particularly, what is the meaning of best interest, and how does it differ from a fiduciary standard, if at all. Even an expert would struggle to understand the difference and a retail customer would surely be confused. Because of this lack of clarity, AARP is concerned that the CRS will further confuse investors, or worse, provide them with a false sense of security.

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<sup>26</sup> Chairman Clayton has a well-documented record of referring to Main Street investors as “Mr. and Mrs. 401K” beginning with his first public speech as SEC Chair before the Economic Club of New York (July 12, 2017) See <https://www.sec.gov/news/speech/remarks-economic-club-new-york>; see also <https://www.sec.gov/news/testimony/testimony-clayton-2017-09-26>.

<sup>27</sup> <https://www.sec.gov/rules/proposed/2018/34-83063-appendix-c.pdf>

<sup>28</sup> <https://www.sec.gov/news/statements/2018/annex-b-2-bd-registrant-mock-up.pdf>.

Another example of where the CRS can be improved is on the dual registrant's disclosure. In that form, the CRS attempts to provide useful guidance on dual registrants, including tabular formatting that illustrates advisory and brokerage services side-by-side. However, although the visual formatting is helpful, the substantive information laid out within the table remains technical and is likely to be confusing to the average retail investor -- someone who does not have expertise in complex financial products. In addition, the relationship summary does not explain how and when these financial professionals must notify investors if they are switching hats. Such information is critical and should be included in order to assist the retail investor with understanding the potential fluidity of the relationship.

**b. The CRS should be reformatted to ensure accessibility to key information.**

Clear information is essential for making informed decisions, understanding how investments and financial relationships operate, and preparing for retirement. Based on our experience, the format of disclosure forms as well as the vocabulary used can have a significant impact on the comprehension of and value of the information being shared with retail customers. We encourage the Commission to strike a balance between sharing concise, non-technical information in as short a form as possible.

We believe that the current four page relationship is too long, technical, and therefore too onerous for the average investor and household to process. The text of the CRS should be simply written and should avoid technical terms like "asset-based fee" unless such complex terms are clearly defined. Behavioral science has shown that when faced with a complicated choice, people often simplify by focusing on only two or three aspects of the decision.<sup>29</sup> The less they are able to frame the decision in narrow terms, the more likely they will end up overwhelmed, undecided, or procrastinating. A good disclosure statement will be concise and will highlight the information most important to the consumer.

AARP commissioned a report in 2007 to determine the extent to which 401(k) participants were aware of fees associated with their accounts and whether they knew how much they actually were paying in fees. The report revealed participants' lack of knowledge about fees as well as their desire for a better understanding of fees. In response to these findings, the report suggested that information about plan fees be distributed regularly and in plain English,

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<sup>29</sup> Daniel Read et al., *Choice Bracketing*, 19 J. Risk & Uncertainty 171, 171–73 (1999).

including a chart or graph that depicts the effect that the total annual fees and expenses can have on a participant's account balance.<sup>30</sup>

A form that is perceived as easy to understand and helpful is more likely to be used to weigh the advantages and disadvantages of available options and to make informed decisions than one that is more confusing. Layout and design elements can be used to enhance understanding of key information in the relationship summary. Side by side comparisons can be helpful, but the information should be simplified and reduced to the key elements. For example, using bold type, underlining, bullets, and borders to highlight important information may enhance comprehension by drawing attention to it. Furthermore, while tables are a viable way to convey information, additional testing to ensure retail investors think the specific tables contained in the form are helpful would be beneficial.

**c. The delivery of the CRS should allow adequate time for review and questioning.**

Of particular importance to AARP is when the CRS will be delivered to the retail investor. When a retail investor fails to receive accurate and complete information regarding the financial professionals' potential conflicts then they are seriously disadvantaged and unable to make an informed decision about their financial security. Given the importance of these forms and potential actions by retail investors, the timing and method by which they receive this information is significant. Investors should have clear and reasonable opportunities to protect their interest and discuss conflicts that may place them at a disadvantage.

As currently drafted, retail investors would receive the CRS at the beginning of a relationship with a firm, and would receive updated information following a material change. AARP recommends that such information be made available upon the first interaction with a prospective retail investor with time allowed for review. Furthermore, the CRS should also include information like the timing of when, and if, the financial professional has an obligation to notify the investor if a conflict arises.

**d. Disclosure alone is not enough. Evidence shows that disclosures can do more harm and may add confusion.**

AARP agrees that all financial professionals should disclose and mitigate or eliminate material conflicts of interest. The Commission should require financial professionals to eliminate practices that directly conflict with the best interest standard appropriate for personalized

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<sup>30</sup> The report is titled *401(k) Participants' Awareness and Understanding of Fees*, available at [http://www.aarp.org/research/financial/investing/401k\\_fees.html](http://www.aarp.org/research/financial/investing/401k_fees.html).

advice such as bonuses, competitions, and rewards. A best interest standard that does not require firms to prohibit incentives that reward and encourage advice that is not in investors' best interests is likely to be a best interest standard in name only.

Recent behavioral science studies have shown that disclosures are largely ineffective because they tend to increase conflict in advisers and make the investor more likely to trust the adviser and thus follow biased advice.<sup>31</sup> Indeed, simply disclosing conflicts does not provide adequate protection and does not shield investors from potential financial harm of conflicted advice. Disclosure may even have unintended effects, such as making a consumer more confident that a financial professional is meeting a higher standard than he or she actually may be meeting. In fact, the less substantive protection there is in the Regulation Best Interest, the more critical the need for a strong relationship summary that discloses the critical components of the investor-financial professional relationship.

Furthermore, the CRS should include a duty on the financial professional's part to document key aspects of the client relationship. This should include precise capturing of what the client wanted, what the financial professional recommended and why. The financial professional should also be required to document not only if conflicts exist, but also how they will be mitigated or minimized, and when and how this conflict was disclosed to the retail investor. The financial professional should acknowledge his/her standard of care, agree to adhere to the standard of care, and document steps taken to comply with that standard. This acknowledgement should be disclosed and delivered in writing to the retail investor and with adequate time for the investor to review (and follow up with questions) prior to engagement.

#### **IV. The financial services industry agrees that a fiduciary standard is the appropriate standard for providing retirement investment advice.**

The financial services industry repeatedly states that investment advice should be provided in the best interests of the participant and retirement investor. Registered IAs and certified financial planners have for decades successfully provided fiduciary advice. Noting that the public demand for fiduciary advice has increased dramatically and that the market continues to move in the direction of providing fiduciary advice, in 2018 the Certified Financial Planner (CFP) Board of Standards approved revisions to its *Standards of Professional Conduct*, which sets forth the ethical standards for CFP® professionals. The revision broadens the application of the

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<sup>31</sup> Sunita Sah, *Gray Matter: The Paradox of Disclosure*, NEW YORK TIMES, July 8, 2016, [https://www.nytimes.com/2016/07/10/opinion/sunday/the-paradox-of-disclosure.html?\\_r=0](https://www.nytimes.com/2016/07/10/opinion/sunday/the-paradox-of-disclosure.html?_r=0); Sunita Sah and George Loewenstein, *Nothing to Declare: Mandatory and Voluntary Disclosure Leads Advisors to Avoid Conflicts of Interest*, 25(2) PSYCHOL. SCI. 575–584 (2014); cf. Sunita Sah, Angela Fagerlin, and Peter Ubel, *Effect of physician disclosure of specialty bias on patient trust and treatment choice*, <http://www.pnas.org/content/113/27/7465.full.pdf>.

fiduciary standard, effectively requiring CFP® professionals to put a client's interest first at all times.

## **V. Conclusion**

We thank the Committee for the opportunity today to share AARP's views on the Commission's proposed rule and required disclosures. AARP remains committed to the strongest possible fiduciary standard for investment advice. For this package to be truly effective, it must reflect an underlying clear and strong rule that protects the best interest of investors. AARP stands ready to serve as a resource and partner in developing an effective standard for investment advice that will promote and protect the financial and retirement security of American families.