



CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

Testimony of Susan MacMichael John
Founder and President, Financial Focus
Chair, Certified Financial Planner Board of Standards, Inc.

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Entrepreneurship and Capital Markets
U.S. House of Representatives

“Putting Investors First? Examining the SEC’s Best Interest Rule”
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Executive Summary

CFP Board of Standards, Inc. (“CFP Board”) is a non-profit organization whose mission is to benefit the public by granting the CFP® certification and upholding it as the recognized standard for competent and ethical personal financial planning. Today, CFP® certification is held by more than 83,000 professionals in the United States. Consistent with our mission to benefit the public, CFP Board supports a fiduciary standard for financial advice.

Importantly, CERTIFIED FINANCIAL PLANNER™ professionals provide fiduciary-level services across business models – as investment advisers, broker-dealers, and insurance agents – and across compensation models – including commission and fee models. It is this unique perspective that we bring to your consideration about the proper standard of conduct for personalized investment advice.

On public policy-related issues, CFP Board works in collaboration with the two membership organizations representing CFP® professionals – the Financial Planning Association¹ and the National Association of Personal Financial Advisors² – as the Financial Planning Coalition.³

The Financial Planning Coalition has long advocated in support of a fiduciary standard of conduct for personalized investment advice. We supported Section 913(g) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”) and for more than a decade have urged the SEC to move forward in rulemaking to accomplish what that provision contemplated. While we waited for the SEC to act, the Coalition supported the Department of Labor’s fiduciary rule for retirement investment advice.

Faced with an increasingly complex universe of financial products and services, Americans today depend on competent and ethical advisors to help them make decisions critical to their financial security. When they seek financial advice, however, they face a marketplace in which it is virtually impossible to distinguish a salesperson from an advisor, or between those advisors who are legally obligated to provide advice in the investor’s best interest versus those who are not. A clear fiduciary standard applied equally to all financial professionals who provide personalized investment advice, including broker-dealers, would help clarify the investment decisions Americans face every day. The expanded fiduciary obligation in the revised CFP Board *Code of Ethics and Standards of Conduct* (“CFP Board *Standards*”), adopted in March 2018, reflects the simple and unambiguous principle that CFP® professionals operating under all business models must, at all times when providing Financial Advice to a Client, act as a fiduciary.

¹ FPA® is the largest membership organization for CFP® professionals and those who support the financial planning process in the U.S. with 23,000 members nationwide. With a national network of 88 chapters and state councils, FPA® represents tens of thousands of financial planners, educators and allied professionals involved in all facets of providing financial planning services. FPA® works in alliance with academic leaders, legislative and regulatory bodies, financial services firms and consumer interest organizations to represent its members.

² NAPFA is the nation’s leading organization of fee-only comprehensive financial planning advisors with more than 3,500 members nationwide. NAPFA members are highly trained professionals who adhere to high professional standards. Each NAPFA advisor annually must sign and renew a Fiduciary Oath and subscribe to NAPFA’s Code of Ethics.

³ The Financial Planning Coalition is a collaboration of the leading national organizations representing the financial planning profession. Together, the Coalition seeks to educate policymakers about the financial planning profession, advocate for policy measures that ensure financial planning services are delivered in the best interests of the public, and enable the public to identify trustworthy financial advisers. See, <http://financialplanningcoalition.com>.

It is against this backdrop that CFP Board and our partners in the Financial Planning Coalition evaluated the Securities and Exchange Commission's ("Commission" or "SEC") package of rule proposals⁴ intended to: (i) raise the standard of conduct for broker-dealers; (ii) reaffirm the fiduciary obligation of investment advisers; (iii) enhance investor understanding by requiring both broker-dealers and investment advisers to deliver a relationship summary document to retail investors; and (iv) reduce investor confusion by restricting the use of certain titles by broker-dealers.

This package of proposals provides the SEC the long-awaited opportunity to raise the standard of conduct applicable to broker-dealers who provide personalized investment advice from the current "suitability" standard to a fiduciary standard of conduct. We are concerned, however, that the rule proposals offer the appearance, but not the reality, of increased investor protection. A final rule must include robust and explicit fiduciary protections for retail investors, regardless of the business model under which that advice is provided. Without these critical safeguards, Reg BI not only will fail to increase protections for retail investors, it may unintentionally mislead the public by implying that compliance with the final rule will cause financial firms and professionals to recommend only those investments that are truly in a retail investor's "best interest."

In comments⁵ submitted to the Commission last year, the Coalition recommended that the Commission consider the framework set out in CFP Board's practical approach to a fiduciary standard that accommodates various business models, as described in CFP Board *Standards*. If the proposed rules are improved and strengthened, as recommended by the Financial Planning Coalition⁶ and others, and with appropriate implementation, we believe the Commission will realize its goal of increasing investor protection and enhancing the quality of investment advice provided to the public.

Finally, CFP Board strongly supports the draft "SEC Disclosure Effectiveness Testing Act." Research conducted on behalf of the SEC and others has shown how difficult it is to convey even the most basic concepts in a way that investors understand. And, it is not enough to simply survey investors or use other informal input to determine whether proposed disclosures would be effective at achieving their regulatory purpose. For this reason, we are particularly pleased that the draft legislation includes a requirement for qualitative testing in the form of one-on-one cognitive interviews of retail investors.

⁴ U.S. Securities and Exchange Commission, Proposed Regulation Best Interest ("Proposed Regulation Best Interest"), 83 Fed. Reg. 21574 (May 9, 2018), *available at* <https://www.federalregister.gov/documents/2018/05/09/2018-08582/regulation-best-interest> ("Reg BI"); Proposed Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation, 83 Fed. Reg. 21203 (May 9, 2018), *available at* <https://www.federalregister.gov/documents/2018/05/09/2018-08679/proposed-commission-interpretation-regarding-standard-of-conduct-for-investment-advisers-request-for> ("IA Interpretation"); Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the use of Certain Names or Titles, 83 Fed. Reg. 21416 (May 9, 2018), *available at* <https://www.federalregister.gov/documents/2018/05/09/2018-08583/form-crs-relationship-summary-amendments-to-form-adv-required-disclosures-in-retail-communications> ("proposed Form CRS").

⁵ Financial Planning Coalition, Letter to Brent J. Fields regarding "Regulation Best Interest" (dated Aug. 7, 2018), *available at* <https://www.sec.gov/comments/s7-07-18/s70718-4186652-172763.pdf>; Financial Planning Coalition, Letter to Brent J. Fields regarding "Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers" (dated Aug. 7, 2018), *available at* <https://www.sec.gov/comments/s7-09-18/s70918-4185807-172700.pdf>; Financial Planning Coalition, Letter to Brent J. Fields regarding "Form CRS Relationship Summary" (dated Aug. 7, 2018), *available at* <https://www.sec.gov/comments/s7-08-18/s70818-4185790-172672.pdf>.

⁶ *Id.*

I. CFP Board *Standards*: A Business-Model Neutral Fiduciary Standard

CFP Board is a professional body that sets and enforces education, examination, experience and ethics requirements for CFP® professionals. As a professional standard-setting organization, CFP Board develops and enforces business conduct standards that are consistent with, and in certain instances may exceed, existing legal and regulatory requirements. Today, more than 83,000 CFP® professionals agree to abide by high standards for competency and ethics, which CFP Board periodically reviews and updates to maintain the value, integrity and relevance of CFP® certification.

A. CFP Board *Standards* Adopted in 2007 Limited the Fiduciary Obligations To Financial Planning Services

CFP Board first adopted a fiduciary standard for CFP® professionals in 2007, when it issued revised *Standards* providing that a CFP® professional owes to the client a fiduciary duty when providing financial planning or material elements of financial planning.⁷ Notably, “CFP Board’s embrace of the fiduciary standard in 2007 wasn’t greeted with fanfare.”⁸ At that time, major financial services firms, as well as industry organizations representing the brokerage and insurance industries, raised significant concerns, asserting that CFP Board’s fiduciary requirement was unworkable with their business models and that CFP® professionals would be forced to rescind their certification if required to operate under a fiduciary standard of conduct.⁹

Contrary to these dire predictions, the number of CFP® professionals has grown by nearly 50 percent since that time, to more than 83,000 today. CFP® professionals, many of whom work at large financial services firms that represent a cross-section of business models, proudly promote that they deliver fiduciary-level services when providing financial planning.

A 2013 Aité survey found that most registered representatives and registered investment advisers agree that a fiduciary standard of conduct is appropriate for financial services providers who deliver personalized investment advice.¹⁰ This finding cuts across a multitude of business models subject to different regulatory provisions. The Aité study surveyed financial professionals at various firm types, including broker-dealers, wirehouses, independent registered investment advisers, and online brokerage firms. Those surveyed cited greater alignment among provider and investor interests as the primary benefit of a uniform fiduciary standard.

In July 2015, Princeton Survey Research Associates International (PSRAI) surveyed¹¹ 1,852

⁷ COMMENTARY TO CODE OF ETHICS AND STANDARDS OF CONDUCT, at p. 3 (March 2018), available at <https://www.cfp.net/docs/default-source/for-cfp-pros---professional-standards-enforcement/CFP-Board-Code-and-Standards-with-Commentary> (“COMMENTARY”).

⁸ Kevin R. Keller, “A fiduciary standard is good, old-fashioned common sense,” Investment News (Oct. 10, 2011), available at [https://www.cfp.net/docs/press-kit/investmentnews-\(oct2011\).pdf?sfvrsn=2](https://www.cfp.net/docs/press-kit/investmentnews-(oct2011).pdf?sfvrsn=2).

⁹ Coalition Letter to the Department of Labor, Regarding “Proposed Conflict of Interest Rule and Related Proposals, RIN-1210-AB32” (July 21, 2015), available at <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00702.pdf>.

¹⁰ Aité, “Fiduciary Study Findings for CFP® Board” (June 2013), available at <https://www.cfp.net/docs/public-policy/fp-coalition-sec-rfi-comments-july-2013.pdf>.

¹¹ Financial Planning Coalition, “Fiduciary Standard Survey,” Prepared by Princeton Survey Research Associates International (Revised July 2015), available at <http://financialplanningcoalition.com/wp-content/uploads/2015/07/Princeton-Research-Fiduciary-Study-Final.pdf>.

stakeholders from Coalition organizations, including professionals from broker-dealers, registered investment advisers, and insurance companies. The study found that almost nine out of 10 respondents agree with the statement that “a fiduciary standard of care is appropriate for all financial professionals who deliver personalized investment advice to retail investors” and two-thirds believe that a change to extend the fiduciary standard of conduct to broker-dealers would have a positive impact on investors.¹²

B. Revised CFP Board Standards Expands the Fiduciary Obligation

In December 2015, CFP Board announced the formation of a Commission on Standards to review and recommend to the Board of Directors of CFP Board proposed changes to the *Terminology, Code of Ethics and Professional Responsibility, Rules of Conduct, and Financial Planning Practice Standards* sections of the CFP Board *Standards*. Commission members included CFP® professionals and other financial services professionals operating under diverse business models, regulatory experts, an investor advocate, and a public representative.

Before the Commission on Standards began its work, CFP Board sought input from CFP® professionals and the public on the issues that should be addressed in the process of updating the CFP Board *Standards*. Public forums were held across the country to gather comments. The Commission then met to review the initial comments and to begin the process of developing updated and revised CFP Board *Standards* to be presented to the Board of Directors of CFP Board.

CFP Board released a draft of the proposed revisions on June 20, 2017, and announced a 60-day public comment period. In addition to accepting written comments, CFP Board received comments during eight public forums held across the country. In November 2017, CFP Board announced a second comment period on the proposed revisions. In addition, CFP Board met with FPA, NAPFA, the Securities Industry and Financial Markets Association (“SIFMA”), the Financial Services Institute (“FSI”), CFP Board’s Business Model Council (which is comprised of firm representatives from various business models), and many other stakeholders, including CFP® professionals and the firms at which they work. CFP Board also considered more than 1,500 written comments and hundreds of oral comments.

In March 2018, the Board of Directors of CFP Board updated the CFP Board *Standards* by adopting revisions which become effective on October 1, 2019. Consistent with CFP Board’s vision and mission, and in furtherance of its strategic plan committed to a fiduciary standard, the newly revised CFP Board *Standards* extends the application of the fiduciary duty to all “Financial Advice”¹³ provided by a CFP® professional. This is in contrast to the current CFP Board *Standards* (which remain in effect until October) that impose a fiduciary duty on CFP® professionals only when providing “Financial Planning” services.

The expanded fiduciary obligation effective in October is “the crown jewel” that animates a CFP® professional’s commitment to high professional standards. Under CFP Board *Standards*, the public will know that a CFP® professional is committed to acting as a fiduciary at all times

¹² *Id.*, at p. 6.

¹³ CODE OF ETHICS AND STANDARDS OF CONDUCT, adopted March 2018, and COMMENTARY, available at <https://www.cfp.net/docs/default-source/for-cfp-pros---professional-standards-enforcement/CFP-Board-Code-and-Standards> and <https://www.cfp.net/docs/default-source/for-cfp-pros---professional-standards-enforcement/CFP-Board-Code-and-Standards-with-Commentary>, respectively.

when providing Financial Advice.¹⁴ As a result, CFP® professionals will owe their clients the same fiduciary duty both when providing Financial Planning services and when providing Financial Advice, thereby eliminating potential client confusion about the CFP® professional's obligations when providing both types of services.

This development enjoys strong support among CFP® professionals and their membership organizations. More than 96 percent of CFP® professionals who responded to a recent survey agreed that a CFP® professional should be required to act in the client's best interest when providing "Financial Advice."¹⁵ Likewise, FPA and NAPFA support the expanded CFP Board fiduciary obligation. FPA applauded CFP Board "for taking the bold and necessary step in expanding the fiduciary standard for CFP® professionals."¹⁶ NAPFA commented that the proposal "supports CFP Board's efforts to [broaden] fiduciary requirements for CFP® professionals. Working under fiduciary principles is the most transparent – and we believe the most objective – way of serving the public. Consumers have come to expect advice delivered in their best interest and will now be able to count on a CFP® professional to provide it at all times when giving financial advice."¹⁷

II. CFP Board *Standards*: A Roadmap for SEC Rulemaking

The Coalition has compared the Commission's proposed Reg BI to the revised CFP Board *Standards*. While there are important similarities, there are significant differences as well. Key similarities and differences are discussed below.

A. Similarities

1. Duty of Care

Both Reg BI and the revised CFP Board *Standards* describe the duty of care in terms of acting with care, skill, prudence and diligence. These are common concepts found in traditional trust law, case law under the Advisers Act, and existing self-regulatory regimes. Together, care, skill, prudence, and diligence signify that a financial professional must use reasonable efforts in gathering information about the retail investor. The duty of care, as described by both Reg BI and CFP Board *Standards*, echoes elements found in the common law "prudent person rule" which can serve to measure the reasonableness of a prudent professional's actions concerning the funds with which he or she is entrusted.

It is important to note that Reg BI does not establish a fiduciary standard of conduct and therefore does not include a clear, stand-alone duty of loyalty, unlike the fiduciary obligation under CFP Board *Standards*. In that respect, CFP Board *Standards* more closely reflects the scope and spirit of the prudent person rule.

2. Providing Firms Leeway in Developing and Implementing Policies and Procedures

¹⁴ Financial Advice is defined broadly and includes recommendations as to non-securities-based financial assets, such as bank instruments, real estate, and insurance products. See "Financial Advice" and "Financial Assets" in CFP BOARD CODE OF ETHICS AND STANDARDS OF CONDUCT (March 2018), available at <https://www.cfp.net/docs/default-source/for-cfp-pros---professional-standards-enforcement/CFP-Board-Code-and-Standards>.

¹⁵ COMMENTARY, at p. 4.

¹⁶ *Id.*

¹⁷ *Id.*

Both Reg BI and CFP Board *Standards* acknowledge the importance of firms' policies and procedures. In addition to having duties to their clients, CFP® professionals have duties to their firms, one of which is complying with internal firm policies and procedures, so long as the policy or procedure does not conflict with CFP Board *Standards*.

Firms' written policies and procedures play a large part in Reg BI's conflict of interest obligations. Under proposed Reg BI, firms would be required to establish, maintain, and enforce written policies and procedures reasonably designed to comply with Reg BI's framework of dealing with conflicts of interest. The SEC believes "there is no one-size-fits-all framework, and broker-dealers should have flexibility to tailor the policies and procedures to account for, among other things, business practices, size and complexity of the broker-dealer, range of services and products offered and associated conflicts presented."¹⁸

As with the CFP Board *Standards*, Reg BI gives firms and associated persons some latitude to tailor and depend on their own written guidelines that fit their business, so long as certain required parameters are met. Firms' written policies and procedures must be reasonably designed to comply with the conflicts of interest obligations of Reg BI. In drafting and applying these written policies and procedures, broker-dealers would be permitted to exercise their judgment to account for unique aspects of their business. The SEC envisions a risk-based compliance and supervisory system to accommodate a variety of different business models and to allow for a facts-and-circumstances evaluation of any given situation. CFP Board envisions the same business model-neutral, risk-based approach in its *Standards*, in particular by examining the conflict's potential for harm in determining whether there was informed consent to the conflict.

3. Similar Approaches to Documentation of the Decision-Making Process

Both CFP Board *Standards* and Reg BI allow for principles-based documentation of the process leading up to the final advisory decision. There is no specific documentation standard that applies to all financial advice in the revised CFP Board *Standards*. However, during the financial planning process, the CFP Board *Standards* requires "a CFP® professional to act prudently in documenting information as the facts and circumstances require, and expressly takes into account the [firm's] policies and procedures."¹⁹ Gathering and maintaining documents to evidence the formation of a basis for decisions made during the financial planning process is a flexible activity. Because this is a facts-and-circumstances-based inquiry, the process already may be covered by the firm's own internal policies and procedures. Consistent with the letter and spirit of the CFP Board *Standards*, CFP® professionals must use sound judgment to determine whether a specific situation warrants the keeping of documentation related to their decision-making process. CFP Board will issue guidance materials to more clearly illustrate how the CFP Board *Standards* will be applied in certain situations with differing fact patterns.

Similarly, Reg BI does not prescribe hard-and-fast rules on creating and maintaining documents on a registered representative's decision-making process. Rather, it requires that the broker-dealer or registered representative have a "reasonable basis" for recommending a transaction that would be in the best interest of at least some customers, or of a particular customer, or that a series of recommendations would be in the customer's best interest.

¹⁸ Reg BI, at p. 21618.

¹⁹ COMMENTARY, at p. 19.

4. Educational Materials Exception

Reg BI and CFP Board *Standards* appropriately carve out exceptions to the best interest requirement for educational materials and other client-facing documents that do not provide specific recommendations or advice. For example, the definition of “Financial Advice” under CFP Board *Standards* “excludes the provision of services or the furnishing or making available of marketing materials, general financial education materials, or general financial communications that a reasonable CFP® professional would not view as ‘Financial Advice.’”²⁰ Reg BI excludes from the meaning of “recommendation” communications that would include “providing general investor education (e.g., a brochure discussing asset allocation strategies) or limited investment analysis tools (e.g., a retirement savings calculator).”²¹

B. Differences

While Reg BI and the CFP Board *Standards* share important similarities, certain obligations outlined under each are quite different. CFP Board *Standards* provides a consistent and robust set of fiduciary principles that translate into an effective investor protection standard. In contrast, certain components of proposed Reg BI remain ill-defined and overly reliant on disclosure. CFP Board is concerned that these key differences will result in a diluted investor protection standard under Reg BI that will not meet the Commission’s objectives with respect to retail investors.

1. Definition of “Best Interest”

Under CFP Board *Standards*, “best interest” clearly and unambiguously means a fiduciary duty. The fiduciary duty encompasses both a duty of loyalty and a duty of care. The duty of loyalty and duty of care flow directly from traditional fiduciary duty concepts applicable to investment advisers under the Advisers Act. The fiduciary duty is clearly stated and defined, and must be satisfied through the management of conflicts, and not simply through disclosures, policies or procedures. All CFP® professionals owe the fiduciary duty to their clients whenever providing Financial Advice, regardless of the business model under which they operate. By contrast, under Reg BI only a duty of care is required and the SEC notes in the rulemaking package, it “[is] not proposing to define ‘best interest’ at this time.”²²

The Commission overcomplicates the regulations applying to broker-dealers providing investment advice by establishing yet another conduct standard to this activity. During consideration of the DOL Fiduciary Rule, it was suggested that only a uniform and consistent standard would cure investor confusion about the different roles that different professionals play and the different standards of conduct to which they are held. We agree that the goal should be a consistent investment advice conduct standard across account types and advice providers. This is particularly important in an environment where services provided by broker-dealers and investment advisers are indistinguishable to the average investor. As such, Reg BI fails to accomplish its purported investor protection goals.

Moreover, by failing to clearly define “best interest”, it is not clear what standard is being

²⁰ COMMENTARY, at p. 3.

²¹ Reg BI at p. 21593.

²² Reg BI, at p. 21587. The SEC went on to say, “Instead, we preliminarily believe that whether a broker-dealer acted in the best interest of the retail customer when making a recommendation will turn on the facts and circumstances of the particular recommendation and the particular retail customer, along with the facts and circumstances of how the four specific components of Reg BI are satisfied.” *Id.*

applied. The proposed rule text, which requires brokers to act in the best interests of their customers and prohibits them from placing their interests ahead of their customer's interests, is the same language that has been used to describe a broker's obligation under FINRA's suitability rules, an investment adviser's fiduciary duties under the Advisers Act, and the requirements under the DOL Fiduciary Rule. All of these standards are different in significant ways and it is not clear how the proposed standard is similar to and different from each of these established standards.

2. CFP Board Standards' Fiduciary Duty Includes a Distinct and Separate Duty of Loyalty

CFP Board *Standards* prominently features a duty of loyalty that incorporates "without regard to" language originally found in Section 913(g) of Dodd-Frank, thereby placing an affirmative requirement on the CFP® professional to act in the best interest of the Client when conflicts arise. This requirement mandates that the CFP® professional be proactive in placing the Client's interests above his or her own interests or the firm's interests. These interests may be financial or non-financial. If a conflict cannot be avoided, the CFP® professional must fully disclose the material conflict, obtain the Client's informed consent, and properly manage the conflict. This step-by-step process is similar to what is required under the Advisers Act and makes clear that disclosure alone is insufficient to satisfy the duty of loyalty under CFP Board *Standards*.

In contrast, Reg BI lacks a separate, distinct, and well-defined duty of loyalty. Instead, Reg BI attempts to incorporate the concept of loyalty in the requirement to put customers' interests "ahead of" those of the broker-dealer. But the term "ahead of" is likewise undefined. It appears that "best interest" will be satisfied *primarily* through disclosures, firms' written policies and procedures as to conflicts of interest, and the duty of care."²³

The duty of loyalty, along with the duty of care and the duty to follow client instructions form the three-part fiduciary duty under CFP Board *Standards*. It brings clarity to what is expected of the CFP® professional and aligns with retail investors' reasonable expectation that they should always receive advice that is "in their best interests."

3. Conflicts of Interest

CFP Board *Standards* has a single, uniform method of dealing with conflicts of interest, regardless of how they originate. Reg BI, however, distinguishes between different types of conflicts of interest and applies different approaches to handling them, depending on whether they stem from financial incentives or the recommendations themselves.

Rather than relying solely on firms' written policies and procedures, CFP Board *Standards* directs CFP® professionals to take affirmative steps and concrete actions to rein in conflicts of interest. All CFP® professionals must "avoid or disclose and **manage** conflicts of interest." CFP® professionals have two choices when it comes to handling conflicts: either (i) avoid the conflict or (ii) fully disclose the material conflict to the client, obtain the client's informed consent, and properly **manage** the conflict. This applies to all Financial Advice and remains true whether

²³ The SEC explained that its choice of the term "ahead of" stemmed from its concern that "inclusion of the 'without regard to' language [as mandated by Section 913(g) of Dodd-Frank] could be inappropriately construed to require a broker-dealer to eliminate all of its conflicts (i.e., require recommendations that are conflict free)." Reg BI, at p. 21586.

the conflict originates from a recommendation or the advice itself, or an incentive linked to that recommendation or advice.

Reg BI provides different avenues for handling conflicts related to recommendations and conflicts linked to financial incentives. If the material conflict has to do with the recommendation itself, then it either must be eliminated or disclosed. Material conflicts relating to financial incentives must be eliminated or disclosed and mitigated. Mitigation is undefined because the SEC does not seek a one-size-fits-all solution and gives firms the flexibility to develop their own mitigation procedures. Financial incentives are undefined but broadly interpreted to cover compensation incentives, sales of proprietary products, sales contests, and transactions in a principal capacity. Reg BI's conflict of interest obligations are anchored to the written policies and procedures that the broker-dealer reasonably designs, establishes and maintains, rather than on the words, actions, and behaviors of associated persons.

It should be recognized that the requirement for firms to mitigate conflicts of interest that arise from financial incentives has the potential to be one of the most beneficial provisions in Reg BI. However, it is unclear what conflict mitigation practices are required and what practices are restricted.

4. "Client" v. "Retail Customer" v. "Retail Investor"

CFP Board *Standards'* definitions capture a broader segment of the population seeking investment advisory services. A "Client" is defined as "Any person, including a natural person, business organization, or legal entity, to whom the CFP® professional provides or agrees to provide Professional Services pursuant to an Engagement."²⁴ This definition encompasses a variety of individuals and organizations, regardless of their accredited investor or similar status, and regardless of the purpose for which they seek the services of a CFP® professional. It is more comprehensive than either the "retail customer" definition in proposed Reg BI or the "retail investor" definition in the proposed Form CRS.

Reg BI would not apply to business organizations or legal entities. It would also be limited to personal, family, or household purposes. We believe this coverage gap potentially leaves smaller businesses' employee benefit plans without viable options to ensure that they receive sound and unbiased advice. We fundamentally disagree with a "purpose test" (i.e., personal, family or household purpose) and believe that those smaller organizations that are, in turn, responsible for the welfare of their retail beneficiaries should also have the benefit of robust investor protections.

III. The Need for a Bright Line: The Broker-Dealer Exclusion of the Advisers Act

When the federal securities laws were enacted, Congress drew a distinction between broker-dealers, who were regulated as salespeople under the Securities Exchange Act of 1934, and investment advisers, who were regulated as advisers under the Investment Advisers Act of 1940. Brokers were excluded from regulation under the Advisers Act only to the extent that they limited themselves to a sales function and provided advice "solely incidental" to such sales without receiving "special compensation" for such advice.²⁵

Over the last several decades, however, the roles of broker-dealers and investment advisers

²⁴ *Standards*, at p. 13.

²⁵ Investment Advisers Act, Section 202(a)(11)(C).

have largely converged. While differences remain, many broker-dealers today offer advisory services, such as investment planning and retirement planning that are similar to the services offered by investment advisers. In addition, many broker-dealers use titles such as “financial adviser” for their registered representatives and market themselves in ways that highlight the advisory aspect of their services. The original broker-dealer exclusion from the Advisers Act has broadened beyond its original intent to allow incidental advice to include a wider range of investment services.

Because federal regulations have not kept pace with changes in business practices, broker-dealers and investment advisers are subject to different legal standards when they offer advisory services. Those legal standards – a suitability standard for broker-dealers and a fiduciary duty for investment advisers – afford different levels of protection to the investors who rely on those services.

Investors, on the other hand, typically make no distinction between broker-dealers and investment advisers, and most are unaware of the different legal standards that apply to advice and recommendations. Although many investors don’t understand the meaning of “fiduciary duty,” or know whether it or suitability represents the higher standard, investors generally treat their relationships with both broker-dealers and investment advisers as relationships of trust and expect that the recommendations they receive will be in their best interests.

Given the realities of the financial markets today, CFP Board and the Financial Planning Coalition support a uniform fiduciary standard for personalized investment advice. This would ensure that, regardless of who provides advice, a fiduciary standard would apply. How the duty is applied would vary based on the differences in the two business models. This would follow the will of Congress by treating functionally equivalent activity the same by applying a fiduciary standard that is no less stringent than the Advisers Act standard to investment advice, no matter who provides that advice.

The goal of Reg BI is an attempt to fix the inequities that exist in the standards that apply to broker-dealers and investment advisers, both of whom are providing personalized investment advice. However, it falls short of ensuring that investment advice – whether provided by a broker-dealer or investment adviser – is subject to the same high fiduciary standard.

IV. Other Issues

A. Rollovers

Reg BI appears to apply to Individual Retirement Account (IRA) rollovers²⁶ and therefore would have a substantial impact on billions of dollars in the retirement savings accounts of U.S. retail investors. However, the SEC is encouraged to better define the parameters around the application to IRA rollovers. Given the trend towards self-directed retirement planning, it is critically important that additional regulatory guidance be provided.

Reg BI implies, but never clearly codifies in the text of the proposed rule, that it may apply to

²⁶ Reg BI, at p. 21595 (“We are not proposing at this time that the duty extend to recommendations of account types generally, unless the recommendation is tied to a securities transaction (e.g., to roll over or transfer assets such as IRA rollovers).”); See also Fred Reish, “Interesting Angles on the DOL’s Fiduciary Rule #97” (July 10, 2018), available at <http://fredreish.com/interesting-angles-on-the-dols-fiduciary-rule-97/> (With respect to recommendations to retail customers, as defined by Reg BI, “[b]oth the rollover recommendation and the recommended IRA investments would be covered by the best interest standard.”).

IRA rollovers if the rollover recommendation is tied to a securities transaction. The sheer impact of IRA rollovers on the U.S. economy and retail investors' retirement savings warrants an additional provision in Reg BI specifically for IRA rollovers. Given that IRA rollovers represent a primary way workers save for retirement, the SEC should clearly and affirmatively state that IRA rollovers are covered by Reg BI and clearly explain the precise framework in the rule text.

B. Dual Registrants

CFP Board *Standards* addresses the issue of dual registrants and “hat switching” with a clean and elegant solution: a fiduciary standard that applies to all financial advice, and not simply investment advice. Investors are unlikely to understand that a single financial advisor operates under a fiduciary standard in one context and under a suitability standard in another context.

The Coalition believes that the Commission's proposal to restrict the use of the titles “adviser” or “advisor” to registered investment advisers is a limited step in the right direction. However, the restriction is limited in its effectiveness because of its narrow application and failure to account for “holding out.” A firm's dual registration status, as both a broker-dealer and investment adviser, should not be the basis upon which representatives of the firm hold themselves out to the public as “advisors.”

V. **Disclosure-Related Issues**

Disclosure is a key component of the securities regulatory scheme. Yet, research conducted on behalf of the SEC and others has demonstrated how challenging it is to develop clear, understandable disclosures in this area, both because the issues to be disclosed are often complex and technical in nature, and because the level of investor understanding of these concepts is typically poor.

A decade ago, for example, RAND Corporation concluded in research conducted on behalf of the Commission that most investors, including those who had employed financial professionals for years, “do not have a clear understanding of the boundaries between investment advisers and broker-dealers.”²⁷ An October 2018 focus group study conducted jointly by RAND Corporation and the SEC's Office of Investor Advocate confirmed that this lack of understanding persists today.²⁸ Moreover, just as in the 2008 study, researchers in 2018 found that presenting participants with fact sheets describing key differences between broker-dealers and investment advisers did little to dispel that confusion.²⁹ This is the challenge when trying to develop a disclosure that will enable investors to make an informed choice between different types of investment accounts and service providers.

A 2016 RAND Corporation study examined the academic literature related to effective disclosures in financial decision-making and concluded that, “disclosure, particularly disclosure used in isolation, may not provide sufficient support in helping investors make more informed decisions.” Looking specifically at disclosures related to conflicts of interest, the RAND

²⁷Angela A. Hung, et al., “Investor and Industry Perspectives on Investment Advisers and Broker-Dealers,” at p. 87 (RAND, 2008), available at <http://bit.ly/1OrrZ3v>.

²⁸ See generally, Brian Scholl, Ph.D., SEC Office of the Investor Advocate and Angela A. Hung, Ph.D., RAND Corporation, et al. “Re: Investor Testing Regarding Standards of Conduct for Investment Professionals” (Oct. 12, 2018), available at <https://www.sec.gov/comments/s7-07-18/s70718-4513005-176009.pdf>.

²⁹ See generally, Angela A. Hung, et al., “Investor Testing of Form CRS Relationship Summary” (November 2018), available at <https://www.sec.gov/comments/s7-07-18/s70718-4628415-176399.pdf>.

researchers found that “many consumers fail to adjust their behavior sufficiently, if at all”³⁰ when conflicts are disclosed. Research has shown, moreover, “that the longer, more detailed disclosure documents have not been effective at helping consumers make informed choices in selecting mortgages, credit cards, and mutual funds, due to either limited attention or limited understanding of the material itself.”³¹ Lengthy, detailed disclosures necessary to convey the relevant information would be unlikely to be read or understood by investors.

Based on this real world experience, CFP Board strongly supports the draft “SEC Disclosure Effectiveness Testing Act.” As noted above, research conducted on behalf of the SEC and others has shown how difficult it is to convey even the most basic concepts in a way that investors understand. And, it is not enough to simply survey investors or use other informal input to determine whether proposed disclosures would be effective at achieving their regulatory purpose. For this reason, we are particularly pleased that the draft legislation includes a requirement for qualitative testing in the form of one-on-one cognitive interviews of retail investors.

A. Why Qualitatively Test Disclosure?

Simply surveying investors about how they feel with regard to a particular disclosure form or whether they can point to specific information in the form is not enough to determine whether the proposed disclosures would be effective at achieving their regulatory purpose. A deeper look into the way investors analyze and synthesize information is necessary to determine the usefulness of the disclosure document in the investor’s decision-making process.

For example, despite the fact that investors say they like the proposed Form CRS disclosure and believe that it is helpful, the 2018 RAND report³² for the SEC provides compelling evidence that the proposed summary relationship disclosure fails to achieve its intended purpose. The results of that research – and, in particular, the significant discrepancy between the survey results, which document investor opinion, and the findings from the in-depth interviews, which test investor comprehension – highlight just how vitally important qualitative testing is to a determination of whether the disclosures actually support informed investor decision-making.

B. Qualitative Testing of the Proposed Form CRS

Recognizing the important role Form CRS plays in the Commission’s proposed regulatory approach to Regulation Best Interest, the Financial Planning Coalition joined with AARP and Consumer Federation of America to engage Kleimann Communications Group, Inc. (“Kleimann”), 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.³³ That research was centered on testing with typical investors the SEC’s Dual Registrant Mock-up of Form CRS, which combined disclosures about Broker-Dealer and Investment Adviser in a side-by-side format. That research 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

³⁰ Angela A. Hung, et al., “Effective Disclosures in Financial Decisionmaking,” at p. 9 (2015), *available at* [file:///C:/Users/aratner/Downloads/Effective%20Disclosures%20in%20Financial%20Decisionmaking%20\(1\).pdf](file:///C:/Users/aratner/Downloads/Effective%20Disclosures%20in%20Financial%20Decisionmaking%20(1).pdf).

³¹ *Id.*, at p. 24.

³² See n. 28, *supra*.

³³ AARP, et al., Letter to The Hon. Jay Clayton (dated Sept. 11, 2018), *available at* <https://www.sec.gov/comments/s7-08-18/s70818-4341455-173259.pdf>.

language used on the form, especially with respect to fees and conflicts of interest.

In a second round of testing,³⁴ Kleimann, directed by AARP and CFP Board, developed and tested alternate language and design for a suggested Form CRS used by the dually registered Investment Adviser and Broker-Dealer. Within that task, three overarching goals were set for the alternative Form CRS:

- 1) Enable retail investors to understand the basic services offered by an Investment Adviser, Broker-Dealer, and dual registrant, and the terms under which those services are offered;
- 2) Enable retail investors to compare the services of an Investment Adviser and a Broker-Dealer; and
- 3) As a result of improved comprehension and comparability, enable retail investors to make informed decisions about the types of accounts and services that are most appropriate for them.

Toward that end, alternative language and formatting was adopted based on lessons learned in the first round of research. This included shortening the document from four pages to the front and back of one page, reordering the topics, simplifying and clarifying the language in plain English, and adopting a question-and-answer format. The purpose of these changes was to improve the usability of Form CRS, reinforce the differences between the two types of accounts, and thereby facilitate a retail investor's ability to make an informed decision.

Despite extensive revisions to the disclosure document based on investor testing, the inescapable conclusion of this second round of testing, like the previous round, was that many, if not most, investors failed to understand many of the key points illustrated in Form CRS and, therefore, could not use it to make an informed choice of accounts.

For example, participants understood the existence, but not the import, of conflicts of interest. Participants struggled to define "conflicts of interest" although they had a vague and general intuitive sense that it would not be good for them. As previously found, most participants were able to understand, based on Form CRS, that conflicts of interest were present in both the brokerage and the advisory accounts. They understood, moreover, that these conflicts took the form of payments that created incentives to recommend certain products. For most participants, however, that is where their understanding ended, and some did not even demonstrate that level of comprehension.

In addition, participants could not adequately explain what it meant to consent to a conflict. Some participants wondered to what they were giving consent, finding the definition and the timing unclear. Other participants mistakenly assumed that having to give consent implied that they would be giving explicit consent for any transaction that included a conflict of interest. Across testing, few participants knew what the word "mitigate" meant and, thus, were confused about how exactly conflicts of interest were to be handled, some even wondering if they would know if a conflict existed. Finally, some investors were confused by what they considered to be contradictory statements: (1) that the financial professional would work in their best interest; and (2) that same professional would have conflicts of interest. Regardless of whether they saw the conflicts as a threat or simply as business as usual, they want their interests to come first.

³⁴ AARP, et al., Letter to The Hon. Jay Clayton (dated Dec. 7, 2018), available at <https://www.sec.gov/comments/s7-07-18/s70718-4729850-176771.pdf>.

Too often, mandated disclosures, as in the proposed Form CRS, are too technical, wordy and lengthy to be useful to investors. The danger on the other end is that the disclosures are nothing more than marketing tools. Conducting thorough one-on-one cognitive testing is the only way of determining if a proposed disclosure document will meet its intended purpose.

VI. Conclusion

We believe that the Reg BI package of proposals presents an opportunity to strengthen investor protection for retail investment advice. We encourage the Commission to improve the rule proposals, as suggested by the Financial Planning Coalition and others, so that it lives up to its promise.