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SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 240, 249, 275 and 279

Release No. 34-83063; IA-4888; File No. S7-08-18

RIN: 3235-AL27

Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the use of Certain Names or Titles

AGENCY: Securities and Exchange Commission.

ACTION: Proposed Rule.

SUMMARY: The Securities and Exchange Commission ("Commission") is proposing new and amended rules and forms under both the Investment Advisers Act of 1940 ("Advisers Act") and the Securities Exchange Act of 1934 ("Exchange Act") to require registered investment advisers and registered broker-dealers (together, "firms") to provide a brief relationship summary to retail investors to inform them about the relationships and services the firm offers, the standard of conduct and the fees and costs associated with those services, specified conflicts of interest, and whether the firm and its financial professionals currently have reportable legal or disciplinary events. Retail investors would receive a relationship summary at the beginning of a relationship with a firm, and would receive updated information following a material change. The relationship summary would be subject to Commission filing and recordkeeping requirements. The Commission also is proposing two rules to reduce investor confusion in the marketplace for firm services, a new rule under the Exchange Act that would restrict broker-dealers and associated natural persons of broker-dealers, when communicating with a retail investor, from using the term "adviser" or "advisor" in specified circumstances; and new rules under the Exchange Act and Advisers Act that would require broker-dealers and investment advisers, and

their associated natural persons and supervised persons, respectively, to disclose, in retail investor communications, the firm's registration status with the Commission and an associated natural person's and/or supervised person's relationship with the firm.

DATES: Comments should be received on or before [insert date 90 days after publication in the Federal Register].

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (*http://www.sec.gov/rules/proposed.shtml*); or
- Send an email to *rule-comments@sec.gov*. Please include File Number S7-08-18 on the subject line.

Paper Comments:

- Send paper comments to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File Number S7-08-18. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (*http://www.sec.gov/rules/proposed.shtml*). Comments also are available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to

make available publicly. Investors seeking to comment on the relationship summary may want to submit our short-form tear sheet for providing feedback on the relationship summary, available at Appendix F.

Studies, memoranda or other substantive items may be added by the Commission or staff to the comment file during this rulemaking. A notification of the inclusion in the comment file of any such materials will be made available on the Commission's website. To ensure direct electronic receipt of such notifications, sign up through the "Stay Connected" option at *www.sec.gov* to receive notifications by email.

FOR FURTHER INFORMATION CONTACT: Emily Rowland, Jennifer Songer, Gena Lai, Roberta Ufford, Jennifer Porter (Branch Chief), and Sara Cortes (Assistant Director), Investment Adviser Regulation Office at (202) 551-6787 or IArules@sec.gov, and Benjamin Kalish, Elizabeth Miller, Parisa Haghshenas (Branch Chief), and Holly Hunter-Ceci (Assistant Director), Chief Counsel's Office at (202) 551-6825 or IMOCC@sec.gov, Division of Investment Management, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

SUPPLEMENTARY INFORMATION: The Commission is proposing new rule 204-5 under the Investment Advisers Act of 1940 [15 U.S.C. 80b],[1] and is proposing to amend Form ADV to add a new Part 3: Form CRS [17 CFR 279.1] under the Advisers Act. The Commission is also proposing to amend rules 203-1 [17 CFR 275.203-1], 204-1 [17 CFR 275.204-1], and 204-2 [17 CFR 275.204-2] under the Advisers Act. The Commission is proposing new rule 17a-14 under

[1] 15 U.S.C. 80b. Unless otherwise noted, when we refer to the Advisers Act, or any paragraph of the Advisers Act, we are referring to 15 U.S.C. 80b, at which the Advisers Act is codified, and when we refer to rules under the Advisers Act, or any paragraph of these rules, we are referring to Title 17, Part 275 of the Code of Federal Regulations [17 CFR 275], in which these rules are published.

the Securities Exchange Act of 1934 [17 CFR 240.17a-14],[2] and new Form CRS [17 CFR 249.640] under the Exchange Act. The Commission is also proposing to amend rules 17a-3 [17 CFR 240.17a-3] and 17a-4 [17 CFR 240.17a-4] under the Exchange Act. The Commission is further proposing new rule 15l-2 under the Exchange Act [17 CFR 240.15l-2], new rule 15l-3 under the Exchange Act [17 CFR 240.15l-3], and new rule 211h-1 under the Advisers Act [17 CFR 275.211h-1].

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[2] 15 U.S.C. 78a. Unless otherwise noted, when we refer to the Exchange Act, or any paragraph of the Exchange Act, we are referring to 15 U.S.C. 78a, at which the Exchange Act is codified, and when we refer to rules under the Exchange Act, or any paragraph of these rules, we are referring to Title 17, Part 240 of the Code of Federal Regulations [17 CFR 240], in which these rules are published.

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I. BACKGROUND

Individual investors rely on the services of broker-dealers and investment advisers when making and implementing investment decisions. Such "retail investors" can receive investment advice from a broker-dealer, an investment adviser, or both, or decide to make their own investment decisions.[3] A number of firms are dually registered with the Commission as broker-

[3] *See* Staff of the U.S. Securities and Exchange Commission, *Study on Investment Advisers and Broker-Dealers as Required by Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (Jan. 2011), at 10-11, *available at* www.sec.gov/news/studies/2011/913studyfinal.pdf ("913 Study"). As discussed below, we have considered the findings, conclusions and recommendations of the 913 Study in developing this proposal.

Retail investors also can choose to receive advisory services from other sources, such as banks, that are not required to be registered with the Commission.

dealers and investment advisers, and offer both types of services.[4] Broker-dealers, investment advisers and dually registered firms all provide important services for individuals who invest in the markets. Studies show that retail investors are confused about the differences among them.[5] These differences include the scope and nature of the services they provide, the fees and costs associated with those services, conflicts of interest, and the applicable legal standards and duties to investors.

We recognize the benefits of retail investors having access to diverse business models and of preserving investor choice among brokerage services, advisory services, or both. We also believe that retail investors need clear and sufficient information in order to understand the differences and key characteristics of each type of service. Providing this clarity is intended to assist investors in making an informed choice when choosing an investment firm and professional, and type of account to help to ensure they receive services that meet their needs and expectations.

The Commission, as the primary regulator of both broker-dealers and investment advisers, has considered ways to address this confusion and preserve investor choice for some time, including through the RAND study of investor perspectives commissioned in 2006, the 913

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4 Investment advisers also may be registered with one or more states if, among other things, they have less than a certain amount of assets under management. *See* section 203A of the Advisers Act. References in this release to investment advisers generally refer only to SEC-registered investment advisers.

5 *See, e.g.*, 913 Study, *supra* note 3. *See also* Letter from Barbara Roper, Director of Investor Protection, Consumer Federation of America, *et al.*, (Sept. 15, 2010) ("CFA Survey") (submitting the results of a national opinion survey regarding U.S. investors and the fiduciary standard conducted by ORC/Infogroup for the Consumer Federation of America, AARP, the North American Securities Administrators Association, the Certified Financial Planner Board of Standards, Inc., the Investment Adviser Association, the Financial Planning Association and the National Association of Personal Financial Advisors); Siegel & Gale, LLC/Gelb Consulting Group, Inc., *Results of Investor Focus Group Interviews About Proposed Brokerage Account Disclosures* (Mar. 5, 2005), *available at* http://www.sec.gov/rules/proposed/s72599/focusgrp031005.pdf ("Siegel & Gale Study"); Angela A. Hung, *et al.*, RAND Institute for Civil Justice, *Investor and Industry Perspectives on Investment Advisers and Broker-Dealers* (2008), *available at* https://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf ("RAND Study").

Study conducted in 2010-2011, and a solicitation of data and other relevant information in 2013.[6] A number of approaches with a range of formats have been considered to address this issue, such as a statement by broker-dealers that an account is a brokerage account and not an advisory account, and encouraging investors to ask questions.[7] Through these initiatives, we have heard and considered the views of a wide range of commenters – financial firms, investors, consumer advocates, academics, and others. Improving retail investors' understanding of their different options for investment-related services through better disclosure is one key area on which commenters have focused. Commenters have suggested a range of presentations. Some commenters recommended a short disclosure document that explains the firm's services, fees, certain conflicts of interest, and the scope and nature of its services to the retail investor.[8] Others recommended a longer, more comprehensive narrative document such as the Form ADV Part 2 brochure that investment advisers are required to deliver to their clients.[9]

Similarly, the staff in the 913 Study and the Commission's Investor Advisory Committee, as part of its recommendation that the Commission adopt a fiduciary duty for broker-dealers, recommended uniform, simple, and clear summary disclosures to retail customers about the

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6 *See* RAND Study, *supra* note 5; 913 Study, *supra* note 3; Duties of Brokers, Dealers, and Investment Advisers, Exchange Act Release No. 69013 (Mar. 1, 2013) [78 FR 14848 (Mar. 7, 2013)] ("2013 Request for Data").

7 *See*, *e.g.*, Certain Broker-Dealers Deemed Not to Be Investment Advisers, Exchange Act Release No. 51523 (Apr. 12, 2005) [70 FR 20424, 20435 (Apr. 19, 2005)], at n.124 and accompanying text ("2005 Broker Dealer Release").

8 *See*, *e.g.*, Comment letters of Sammons Retirement Solutions (Jun. 4, 2013) and Insured Retirement Institute (Jul. 3, 2013) (recommending a short summary disclosure document together with a longer disclosure document similar to Form ADV, to be offered by both broker-dealers and investment advisers); Comment letter of AARP (Jul. 25, 2013); Comment letter of American Council of Life Insurers (Jul. 5, 2013) (incorporating by reference its comment letter, dated Aug. 30, 2010); Comment letter of Financial Services Institute (Jul. 5, 2013).

9 *See*, *e.g.*, Comment letter of Committee of Annuity Insurers (Jul. 5, 2013); Comment letter of Edward D. Jones and Co., L.P. (Jul. 12, 2013); Comment letter of North American Securities Administrators Association, Inc. (Jul. 5, 2013); Comment letter of PFS Investments, Inc. (Jul. 5, 2013).

terms of their relationships with broker-dealers and investment advisers, including any material conflicts of interests.[10] Disclosure has also been a feature of other regulatory efforts that address investment advice, including those of the U.S. Department of Labor ("DOL") applicable to services provided by broker-dealers and investment advisers,[11] and rules applicable to broker-dealers issued by the Financial Industry Regulatory Authority ("FINRA").[12]

In 2017, Commission Chairman Clayton continued the discourse on these issues by outlining a series of questions and welcoming the public to submit their views on standards of conduct and related disclosures for investment advisers and broker-dealers. More than 250 commenters responded.[13] Many commenters recommended enhanced disclosures in addition to

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10 *See* 913 Study, *supra* note 3, at 114-117. The 913 Study contemplated that the general relationship guide would be akin to Part 2A of Form ADV, which is generally referred to as an investment adviser's "brochure" and is the form investment advisers use to register with the Commission and states, which is provided to advisory clients. The 913 Study identified a number of potential disclosures that the Commission should consider including in such relationship guide. *See also* Recommendation of the Investor Advisory Committee: Broker-Dealer Fiduciary Duty, *available at* https://www.sec.gov/spotlight/investor-advisory-committee-2012/fiduciary-duty-recommendation-2013.pdf ("Broker-Dealer Fiduciary Duty Recommendations"). The recommendation of the Investor Advisory Committee suggested that the disclosure be provided at the start of the engagement and periodically thereafter, and that it cover basic information about the nature of the services offered, fees and compensation, conflicts of interest, and disciplinary record.

11 For example, DOL regulations relating to "reasonable plan service arrangements" require firms providing advisory and other services to workplace retirement plans covered by the Employee Retirement Income Security Act of 1974 ("ERISA") and the prohibited transaction provisions under section 4975 of the Internal Revenue Code ("Code") to disclose in writing (among other things) a description of services and applicable fees. *See* 29 CFR 2550.408b-2. *See also* 29 CFR 2550.408g-1 (regulation requires fiduciary advisers to plans and individual retirement accounts ("IRAs") seeking to rely on the statutory exemption for participant investment advice to provide certain disclosures, among other conditions). *See also infra* Section IV.A.1.c, which further describes disclosure obligations under DOL regulations and exemptions, including the DOL's "Best Interest Contract Exemption" (the "BIC Exemption").

12 Disclosure of Services, Conflicts and Duties, FINRA Notice 10-54 (Oct. 2010), *available at* http://www.finra.org/sites/default/files/NoticeDocument/p122361.pdf ("FINRA Notice 10-54").

13 Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers, Chairman Jay Clayton (Jun. 1, 2017), *available at* https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31 ("Chairman Clayton's Request for Comment").

regulations that would raise the standard of conduct for broker-dealers providing advice.[14] Some recommended that both broker-dealers and investment advisers should provide a uniform disclosure document to retail investors,[15] while others suggested new disclosure requirements only for broker-dealers.[16] Commenters also noted that investor confusion based on financial professionals' titles persists, and made a range of suggestions.[17] Specifically, some commenters believed that particular titles cause investors to either form misimpressions about whether the services received are those of an investment adviser and subject to a fiduciary duty, or these investors are misled by financial professionals to form such beliefs.[18]

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14 *See, e.g.*, Comment letter of T. Rowe Price (Oct. 12, 2017) ("T. Rowe 2017 Letter"); Comment letter of Vanguard (Sept. 29, 2017) ("Vanguard 2017 Letter"); Comment letter of Teachers Insurance and Annuity Association of America (Sept. 26, 2017) ("TIAA 2017 Letter"); Comment letter of the Investment Adviser Association (Aug. 31, 2017) ("IAA 2017 Letter"); Comment letter of Stifel, Nicolaus & Co. (Jul. 25, 2017) ("Stifel 2017 Letter"); Comment letter of Bernardi Securities, Inc. (Sept. 11, 2017) ("Bernardi Securities 2017 Letter"); Comment letter of UBS Financial Services Inc. (Jul. 21, 2017) ("UBS 2017 Letter"); Comment letter of SIFMA (Jul 21, 2017) ("SIFMA 2017 Letter"); Comment letter of the Equity Dealers of America (Sept. 11, 2017) ("Equity Dealers of America 2017 Letter"); Comment letter of AARP (Sept. 6, 2017) ("AARP 2017 Letter"); Comment letter of Financial Services Institute (Oct. 30, 2017); Comment letter of Financial Services Roundtable (Oct. 17, 2017) ("FSR 2017 Letter"); Comment letter of Consumer Federation of America (Sept. 14, 2017) ("CFA 2017 Letter").

15 *See, e.g.*, Stifel 2017 Letter; Equity Dealers of America 2017 Letter; Comment letter of Michael Kiley (Jul. 6, 2017) ("Kiley 2017 Letter"); Comment letter of the American Council of Life Insurers (Oct. 3, 2017) ("ACLI 2017 Letter"); Comment letter of Allianz Life Insurance Company of North America (Oct. 13, 2017) ("Allianz 2017 Letter"); AARP 2017 Letter; Comment letter of Robert Shaw (Jun. 5, 2017) ("Shaw 2017 Letter"); Comment letter of Alan Syzdek (Jul. 2 2017); Comment letter of Americans for Financial Reform (Sept. 22, 2017) ("AFR 2017 Letter").

16 *See, e.g.*, SIFMA 2017 Letter; Comment letter of the Investment Company Institute (Feb. 5, 2018); IAA 2017 Letter; Comment letter of Fidelity Investments (Aug. 11, 2017) ("Fidelity 2017 Letter"); Vanguard 2017 Letter; T. Rowe 2017 Letter; FSR 2017 Letter; UBS 2017 Letter; TIAA 2017 Letter; Comment letter of Wells Fargo & Company (Sept. 20, 2017) ("Wells Fargo 2017 Letter"); Bernardi Securities 2017 Letter; Comment letter of State Farm Mutual Automobile Insurance Company (Aug. 21, 2017) ("State Farm 2017 Letter"); Comment letter of PFS Investments Inc. (Dec. 10, 2017); Comment letter of Davis & Harman LLP (Jan. 18, 2018); Comment letter of LPL Financial LLC (Feb. 22, 2018).

17 *See, e.g.*, CFA 2017 Letter; Comment letter of the Public Investors Arbitration Bar Association (Aug. 11, 2017) ("PIABA 2017 Letter"); IAA 2017 Letter; Comment letter of Pefin (Sept. 13, 2017) ("Pefin 2017 Letter"); Comment letter of Jackson National Life Insurance Company (Nov. 1, 2017) ("Jackson 2017 Letter"); Comment letter of CFA Institute (Jan. 10, 2018); Comment letter of First Ascent Asset Management (Jan. 10, 2018) ("First Ascent 2018 Letter").

18 *See e.g.* CFA 2017 Letter; IAA 2017 Letter; Comment letter of the National Employment Law Project (Oct. 20, 2017) ("National Employment Law Project 2017 Letter").

Many commenters recommended a short disclosure document addressing the nature and scope of services, fees and material conflicts of interest.[19] These suggestions are consistent with our staff's financial literacy study,[20] which found that retail investors favor a summary document and find these categories of disclosures, plus a financial intermediary's disciplinary history, to be important in choosing financial intermediaries.[21] Regarding investor confusion based on titles, commenters also recommended, for example, prohibiting the use of certain terms in titles, and prohibiting a firm not registered as an investment adviser from holding itself out in a manner that implies it is an investment adviser.[22]

We agree that it is important to ensure that retail investors receive the information they need to understand the services, fees, conflicts, and disciplinary history of firms and financial professionals they are considering. Likewise, we believe that we should reduce the risk that retail investors could be confused or misled about the financial services they will receive as a result of the titles that firms and financial professionals use, and mitigate potential harm to investors as a result of that confusion. We also believe the information should be reasonably concise. Accordingly, we are proposing new rules to require broker-dealers and investment advisers to deliver to retail investors a customer or client relationship summary ("Form CRS")

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19 *See, e.g.*, SIFMA 2017 Letter; UBS 2017 Letter; Stifel 2017 Letter; AARP 2017 Letter; Bernardi Securities 2017 Letter; Fidelity 2017 Letter; Allianz 2017 Letter.

20 *See, e.g.*, Staff of the Securities and Exchange Commission, *Study Regarding Financial Literacy Among Investors as required by Section 917 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (Aug. 2012), at iv, v, xiv, 37, 73, 121-23 and 131-32, *available at* https://www.sec.gov/news/studies/2012/917-financial-literacy-study-part1.pdf ("917 Financial Literacy Study").

21 *See, e.g.*, 917 Financial Literacy Study, *supra* note 20, at iv, x – xiii, xxi, 37, 66-67, 73, 119.

22 *See, e.g.* Comment letter of Mark D. Moss (Jun. 2, 2017); Comment letter of Gimme Credit (Aug. 8, 2017); PIABA 2017 Letter; AFL-CIO 2017 Letter; IAA 2017 Letter; Pefin 2017 Letter; Jackson 2017 Letter; AFR 2017 Letter; National Employment Law Project 2017 Letter; First Ascent 2018 Letter.

that would explain general information about each of these topics.[23] Second, we are proposing rules that would (i) restrict the use of the terms "adviser" and "advisor" by broker-dealers and their associated financial professionals, and (ii) require broker-dealers and investment advisers to disclose in retail investor communications the firm's registration status while also requiring their associated financial professionals to disclose their association with such firm.

Together, these requirements would complement a separate release that the Commission is proposing concurrently to enhance existing broker-dealer conduct obligations ("Regulation Best Interest").[24] Regulation Best Interest would establish a standard of conduct for broker-dealers and associated natural persons of broker-dealers to act in the best interest of a retail customer when making a recommendation of a securities transaction or investment strategy involving securities. While Regulation Best Interest would enhance the standard of conduct owed by broker-dealers to retail customers, it would not make that standard of conduct identical to that of investment advisers, given important differences between investment advisers and broker-dealers. The requirements we are proposing in this release would help an investor better understand these differences, and distinguish among different firms in the marketplace, which in turn should assist the investor in making an informed choice for the services that best suit her particular needs and circumstances.

II. FORM CRS RELATIONSHIP SUMMARY

We are proposing to require registered investment advisers and registered broker-dealers to deliver a relationship summary to retail investors. In the case of an investment adviser, initial

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[23] For investment advisers, Form CRS would be required by Form ADV Part 3. For broker-dealers, Form CRS would be required by proposed new rule 17a-14 under the Exchange Act. When we refer to Form CRS in this release, we are referring to Form CRS for both broker-dealers and investment advisers.

[24] Regulation Best Interest, Exchange Act Release No. 34-83062 (Apr. 18, 2018) ("Regulation Best Interest Proposal").

delivery would occur before or at the time the firm enters into an investment advisory agreement with the retail investor; in the case of a broker-dealer, initial delivery would occur before or at the time the retail investor first engages the firm's services. Dual registrants would deliver the relationship summary at the earlier of entering into an investment advisory agreement with the retail investor or the retail investor engaging the firm's services.[25]

The relationship summary would be as short as practicable (limited to four pages or equivalent limit if in electronic format), with a mix of tabular and narrative information, and contain sections covering: (i) introduction; (ii) the relationships and services the firm offers to retail investors; (iii) the standard of conduct applicable to those services; (iv) the fees and costs that retail investors will pay; (v) comparisons of brokerage and investment advisory services (for standalone broker-dealers and investment advisers); (vi) conflicts of interest; (vii) where to find additional information, including whether the firm and its financial professionals currently have reportable legal or disciplinary events and who to contact about complaints; and (viii) key questions for retail investors to ask the firm's financial professional. Form CRS would be required by Form ADV Part 3 and rule 204-5 of the Advisers Act for investment advisers, and by Form CRS and rule 17a-14 of the Exchange Act for broker-dealers.[26]

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[25] For purposes of the relationship summary, we propose to define dual registrant as a firm that is dually registered as a broker-dealer and an investment adviser and offers services to retail investors as both a broker-dealer and investment adviser. Proposed General Instruction 9.(b) to Form CRS. Accordingly, a firm that is registered with the Commission as a broker-dealer and with one or more states as an investment adviser would be a dual registrant.

[26] We propose to amend Form ADV, which investment advisers must file to register with the Commission and with state securities regulators, to include a new Part 3: Form CRS that describes the requirements for the relationship summary, and we propose conforming technical amendments to the General Instructions of Form ADV. *See* proposed amendments to Advisers Act rule 203-1; proposed amendments to General Instructions to Form ADV. We also propose a rule 17a-14 to require a Form CRS for broker-dealers registered with the Commission. *See* Exchange Act proposed rule 17a-14. Advisers use Form ADV to apply for registration with us (Part 1A) or with state securities authorities (Part 1B), and must keep it current by filing periodic amendments as long as they are registered. *See* Advisers Act rules 203-1 and 204-1. Form ADV has two parts. Part 1(A and B) of Form ADV provides regulators with information to process registrations and to manage their regulatory and examination programs. Part 2 is a uniform form

We are proposing to define "relationship summary" as a written disclosure statement that firms must provide to retail investors.[27] A "retail investor" would be defined as a prospective or existing client or customer who is a natural person (an individual).[28] All natural persons would be included in the definition, regardless of the individual's net worth (thus including, *e.g.*, accredited investors, qualified clients or qualified purchasers).[29] The definition would include a trust or other similar entity that represents natural persons, even if another person is a trustee or managing agent of the trust.[30] We believe that this definition is appropriate because section 913 of the Dodd-Frank Act defines "retail customer" to include natural persons and legal representatives of natural persons without distinction based on net worth, and because financial literacy studies report deficiencies in financial literacy among the general population.[31] While

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used by investment advisers registered with both the Commission and the state securities authorities. *See* Instruction 2 of General Instructions to Form ADV. This release discusses the Commission's proposal of Form ADV Part 3: Form CRS and related rules applicable to advisers registered with the Commission. To the extent that state securities authorities could consider making similar changes that affect advisers registered with the states, we can forward comments to the North American Securities Administrators Association ("NASAA") for consideration by the state securities authorities.

27 Proposed General Instruction 9.(d) to Form CRS.

28 Proposed General Instruction 9.(e) to Form CRS.

29 Advisers Act proposed rule 204-5(d)(2) and Exchange Act proposed rule 17a-14(e)(2); proposed General Instruction 9.(e) to Form CRS. We recognize that the definition of "retail investor" would differ from that of "retail customer," as used in Regulation Best Interest. "Retail customer" for broker-dealers under Regulation Best Interest would be defined as "a person, or the legal representative of such person, who: (1) receives a recommendation of any securities transaction or investment strategy involving securities from a broker, dealer or a natural person who is an associated person of a broker or dealer, and (2) uses the recommendation primarily for personal, family, or household purposes." Regulation Best Interest Proposal, *supra* note 24, section II.C.4. We believe it is beneficial to require firms to provide a relationship summary to all natural persons to facilitate their understanding of account choices, regardless of whether they will receive investment advice primarily for personal, family, or household purposes. The relationship summary is intended for an earlier stage in the relationship between an investor and a financial professional, potentially before discussing the investment purposes of the investor. In contrast, Regulation Best Interest focuses on recommendations to "retail customers" who have chosen to engage the services of a broker-dealer after receiving the relationship summary.

30 Advisers Act proposed rule 204-5(d)(2) and Exchange Act proposed rule 17a-14(e)(2); proposed General Instruction 9.(e) to Form CRS.

31 *See* Federal Research Division, Library of Congress, *Financial Literacy Among Retail Investors in the United States* (Dec. 30, 2011), *available at* https://www.sec.gov/news/studies/2012/917-financial-literacy-

studies also report variability in financial literacy among certain sub-sections of the general population,[32] we believe that all individual investors would benefit from clear and succinct disclosure regarding key aspects of their advisory and brokerage relationships.

As discussed further below, the relationship summary would be in addition to, and not in lieu of, current disclosure and reporting requirements for broker-dealers and investment advisers.[33] The relationship summary would alert retail investors to important information for them to consider when choosing a firm and a financial professional, and would prompt retail investors to ask informed questions. In addition, the content of the relationship summary would facilitate comparisons across firms that offer the same or substantially similar services. We are promoting these goals through specifying much of the content and presentation of Form CRS in the form's instructions ("Instructions"); while firms will be required to include firm-specific information in Form CRS, they will have limited discretion in the scope and presentation of that information. We are proposing that firms electronically file the relationship summary and any updates with the Commission, and therefore such filings would be subject to section 207 of the Advisers Act[34] and section 18 of the Exchange Act.[35] Investment advisers would file on the Investment Adviser Registration Depository ("IARD"), broker-dealers would file on the Commission's Electronic Data Gathering, Analysis and Retrieval System ("EDGAR"), and dual registrants would file on both IARD and EDGAR.

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study-part2.pdf ("Library of Congress Report"). The Library of Congress Report is incorporated by reference into the 917 Financial Literacy Study, *supra* note 20, at Appendix 1.

32 *See, e.g.*, 917 Financial Literacy Study, *supra* note 20, at viii ("In addition, surveys demonstrate that certain subgroups, including women, African-Americans, Hispanics, the oldest segment of the elderly population, and those who are poorly educated, have an even greater lack of investment knowledge than the average general population."); Library of Congress Report, *supra* note 31, at 1.

33 *See infra* Section II.C.

34 15 U.S.C. 80b-7.

35 15 U.S.C. 78r.

To aid firms in understanding the type of disclosures we propose to require, we have created mock-ups of a relationship summary for an investment advisory firm, a brokerage firm, and a dual registrant, and have included them as Appendices C-E to this release. The mock relationship summaries are for illustrative purposes only, reflect the business models of hypothetical firms, and are not intended to imply that they reflect a "typical" firm. They do not provide a safe harbor and, depending on the circumstances of a particular firm, a relationship summary that merely copies the mock-ups may not provide sufficient or accurate information about the firm, including for purposes of meeting the firm's obligations under the antifraud provisions of the federal securities laws. Investors seeking to comment on the relationship summary may want to submit our short-form tear sheet for providing feedback on the relationship summary, available at Appendix F. Below we request comments on all requirements of the relationship summary, including format, content, method of filing, method of delivery, updating, and other aspects as discussed below.

We preliminarily believe that providing this information before or at the time a retail investor enters into an investment advisory agreement or first engages a brokerage firm's services, as well as at certain points during the relationship (*e.g.*, switching or adding account types), as further discussed below, is appropriate and in the public interest and will improve investor protection, and will deter potentially misleading sales practices by helping retail investors to make a more informed choice among the types of firms and services available to them.[36]

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[36] *See* Exchange Act section 15(l)(2) and Advisers Act section 211(h)(2) (providing that the Commission shall examine and, where appropriate, promulgate rules prohibiting or restricting certain sales practices, among other things, for brokers, dealers, and investment advisers that the Commission deems contrary to the public interest and the protection of investors).

A. Presentation and Format

We are proposing requirements designed to make the relationship summary short and easy to read. We believe that the required disclosure provides an overview of information that would help retail investors when choosing a firm, financial professional, and account type. The proposed formatting requirements would help retail investors, many of whom may not be sophisticated in legal or financial matters, to understand the information in the relationship summary and be in a better position to ask informed questions. The proposal is also informed by our experience with the mutual fund summary prospectus, which has illustrated the benefits of highlighting certain information in summary form, coupled with layered disclosure and disclosure designed to facilitate comparisons across investments.[37] We encourage firms to use innovative technology to create a relationship summary that is user-friendly, concise, easy-to-read, and more interactive than paper, and request comment below on ways to do so. The relationship summary would be provided to retail investors in addition to, and not in lieu of, any other required disclosures.[38]

As noted in the General Instructions, the requirements of the relationship summary are designed to promote effective communication between the firm and its retail investors.[39] First, as several commenters have recommended, we propose requiring that firms use "plain language"

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37 In a previous study, Commission staff found that most of the retail investors agreed that it was important to read a summary prospectus prior to investing in a mutual fund, and a majority of the retail investors surveyed on the mutual fund summary prospectus panel agreed that the actual summary prospectus they reviewed highlighted important information, was well-organized, written using words that they understood, clear and concise, and user friendly, and agreed that summary prospectuses contain the 'right amount' of information. 917 Financial Literacy Study, *supra* note 20, at xvii and xix.

38 *See* Proposed General Instruction 3 to Form CRS. Broker-dealers and investment advisers have disclosure and reporting obligations under state and federal law, and broker-dealers are also subject to disclosure obligations under the rules of self-regulatory organizations. Delivery of the relationship summary would not necessarily satisfy a firm's other disclosure obligations.

39 Proposed General Instruction 2 to Form CRS.

principles for the organization, wording, and design of the entire relationship summary, taking into consideration retail investors' level of financial sophistication.[40] Specifically, firms would be required to be concise and direct and to use short sentences, active voice, and definite, concrete, everyday words.[41] Firms would not be permitted to use legal jargon, highly technical business terms or multiple negatives.[42] Firms should write the relationship summary as if addressing the retail investor, using "you," "us," or "our firm."[43]

Second, we are proposing to require that, whether in electronic or paper format, the relationship summary should be no more than four 8 ½ x 11 inch pages if converted to Portable Document Format ("PDF"), using at least an 11 point font size, and margins of at least 0.75 inches on all sides.[44] For example, if delivered directly in the text of an email or in a mobile viewing format on the firm's website, the content of the relationship summary should not exceed this four-page PDF-equivalent length. This approach is consistent with our experience and commenters' suggestion that brief disclosure is more effective than a long-form narrative to focus retail investors on relevant information, and with suggestions from commenters who advocated for a clear, concise disclosure.[45] If delivered in paper, the paper size, font, and margin requirements would also encourage a clear presentation for retail investors, for example, by

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40 Proposed General Instruction 2 to Form CRS. *See, e.g.*, PIABA 2017 Letter; State Farm 2017 Letter; Fidelity 2017 Letter; Comment letter of BlackRock (Aug. 7, 2017); Comment letter of the Investor Advisory Committee (Aug. 24, 2017); CFA 2017 Letter; AFR 2017 Letter; ACLI 2017 Letter; FSR 2017 Letter.

41 Proposed General Instruction 2 to Form CRS.

42 Proposed General Instruction 2 to Form CRS.

43 Proposed General Instruction 2 to Form CRS.

44 Proposed General Instruction 1.(c) to Form CRS.

45 *See, e.g.*, Shaw 2017 Letter; SIFMA 2017 Letter; AFL-CIO 2017 Letter; AARP 2017 Letter; CFA 2017 Letter; AFR 2017 Letter; TIAA 2017 Letter; Vanguard 2017 Letter; ACLI 2017 Letter; FSR 2017 Letter; Allianz 2017 Letter.

presenting important disclosures in a readable font-size and eliminating fine print.[46] Recognizing, however, that many firms deliver disclosures in electronic format and employ a variety of technologies to interact with prospective and existing retail investors, the Commission is requesting comment on formatting and other features of the relationship summary in electronic form.

In the past, the Commission has declined to impose page limits on disclosures required by the Investment Company Act of 1940 ("Investment Company Act"), including the summary prospectus, expressing concern that page limits could constrain appropriate disclosure and lead funds to omit material information about fund offerings.[47] The proposed relationship summary is intended to serve different purposes than the summary prospectus, including to provide a general overview of firms that could prompt a more detailed, individualized, and open conversation between the retail investor and his or her financial professional. The Commission preliminarily believes that the utility and effectiveness of the relationship summary lie in its brevity and conciseness; accordingly, we believe a page limit (or equivalent limit if in electronic format) is appropriate.

Brief disclosure would also facilitate a layered approach to disclosure in which firms would include certain information in the relationship summary, along with references and links to other disclosure where interested investors can find additional information.[48] The proposed

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46 *See*, *e.g.*, 917 Financial Literacy Study, *supra* note 20, at xiii and 32.

47 *See* Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, Investment Company Act Release No. 28584 (Jan. 13, 2009) [74 FR 4546 (Jan. 26, 2009)], at 24 ("Enhanced Mutual Fund Disclosure Adopting Release").

48 Firms would be required to include cross-references to where investors could find additional information, such as in the Form ADV Part 2 brochure and brochure supplement for investment advisers or on the firm's website or in the account opening agreement for broker-dealers. For electronic versions of the relationship summary, we would require firms to use hyperlinks to the cross-referenced document if it is available

relationship summary also would encourage retail investors to seek additional information in other ways, including through suggested questions for retail investors to ask their financial professional, as discussed further below.[49] These requirements are intended to create a concise summary that points out relevant areas for retail investors to focus on as they consider financial services, and the cross references and suggested questions facilitate investors' ability to choose to seek additional information. In addition, providing retail investors with a relationship summary containing specified information about the firm in a standardized format should aid retail investors' ability to compare firms at a higher level. The suggested questions and cross references to more information would enable them to more easily find and compare these details about the firms.

We considered requiring more detailed disclosure for broker-dealers similar to many items in the Form ADV brochure that advisers currently must deliver to clients. This longer disclosure would provide, for example, more information about fee amounts for specific accounts and products and more detailed descriptions of a wider range of conflicts of interest. We believe, however, that brief disclosure that focuses on the proposed topics would be more effective in capturing the attention of retail investors, encouraging them to explore certain key areas further, including by asking questions, and allowing them to make a quick comparison among a number of options.[50] We also encourage the use of methods, such as embedded hyperlinks, to direct retail investors to additional disclosures.

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online. *See* proposed Items 7.E.1. and 7.E.2. of Form CRS; proposed General Instruction 1.(g) to Form CRS.

49 *See* proposed Item 8 of Form CRS.

50 *See, e.g.*, 917 Financial Literacy Study, *supra* note 20, at 23-24 (citing CFA 2012 Letter, at 4-5).

Alternatively, we considered shorter disclosure, such as a one-page document (or equivalent length if in electronic format) that would provide either a much abbreviated general description of a firm's services, fees, and conflicts, or a list of suggested questions for retail investors to discuss with their financial professional. We are concerned, however, that these approaches might not provide retail investors with enough information to compare firms and types of accounts. In addition, we are concerned that providing only a list of questions, without sufficient background information for investors to know why the question is important to ask, could make it less likely that investors would ask the questions or have an informed conversation. Only providing questions also would not ensure a standardized minimum of information that retail investors would receive across firms and therefore would not facilitate comparing firms or account types.

The relationship summary would require eight separate items covering: (i) introduction; (ii) relationships and services the firm provides to retail investors; (iii) standard of conduct applicable to those services; (iv) the fees and costs that retail investors will pay; (v) comparisons of brokerage and investment advisory services (for standalone broker-dealers and investment advisers);[51] (vi) conflicts of interest; (vii) where to find additional information, including whether the firm and its financial professionals currently have reportable legal or disciplinary events and who to contact about complaints; and (viii) key questions for retail investors to ask the firm's

[51] For purposes of the relationship summary, we propose to define a standalone investment adviser as a registered investment adviser that offers services to retail investors and (i) is not dually registered as a broker-dealer or (ii) is dually registered as a broker-dealer but does not offer services to retail investors as a broker-dealer. We propose to define a standalone broker-dealer as a registered broker-dealer that offers services to retail investors and (i) is not dually registered as an investment adviser or (ii) is dually registered as an investment adviser but does not offer services to retail investors as an investment adviser. Proposed General Instruction 9.(f) to Form CRS. We are including certain dual registrants in these proposed definitions because we understand that dual registrants do not always offer both brokerage and advisory accounts to retail investors. For example, some dual registrants offer advisory accounts to retail investors, but offer brokerage broker-dealer services only to institutions (*e.g.*, for their underwriting services).

financial professional.[52] In order to promote comparison across firms, we would require firms to present this information under prescribed headings in the same order.[53] Firms also would be prohibited from including any information other than what the Instructions and the applicable item require or permit.[54] We believe that allowing only the required and specified permitted information would promote consistency of information presented to investors, allow retail investors to focus on information that we believe would be particularly helpful in deciding among firms, and help retail investors to decide what further information is needed. It would also encourage impartial information by preventing firms from adding information commonly used in marketing materials, such as performance.[55]

For certain items, firms will have some flexibility in how they include the required information.[56] For others, we are requiring firms to use prescribed wording, as discussed in the following sections. Firms may not include disclosure in the relationship summary other than disclosure that is required or permitted by the Instructions. We believe that this approach balances the need to provide firms flexibility in making the presentation of information consistent with their particular business model while ensuring that all investors receive certain information regardless of the firm. The information in the relationship summary must accurately

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52 *See* proposed Items 1-8 of Form CRS.

53 Proposed General Instruction 1.(b) and (e) to Form CRS. *See also e.g.*, proposed Items 2.A., 3.A., 4.A., 5.A. and 5.B., 6.A., 7.A., and 8 of Form CRS.

54 Proposed General Instruction 1.(d) to Form CRS.

55 Although performance disclosure is a subject on which the Commission focuses, including to promote accuracy, consistency, and comparability, such disclosure is not the subject of this initiative.

56 *See*, *e.g.*, proposed General Instruction 1.(f) to Form CRS ("You may use charts, graphs, tables, and other graphics or text features to explain the required information, so long as the information (i) is responsive to and meets the requirements in these instructions (including space limitations); (ii) is not inaccurate or misleading; and (iii) does not, because of the nature, quantity, or manner of presentation, obscure or impede understanding of the information that must be included. When using interactive graphics or tools, you may include instructions on their use and interpretation."); proposed Items 2.B., 2.C., and 6.B. of Form CRS.

reflect the characteristics of the particular firm and the services that it offers. Accordingly, all information in the relationship summary must be true and may not omit any material facts necessary to make the required disclosures not misleading.[57] If a statement is inapplicable to a firm's business or would be misleading to a reasonable retail investor, the firm may omit or modify that statement.[58]

Based on studies that indicate the effectiveness of graphical presentation for retail investors,[59] we are prescribing the use of graphical formats in specified circumstances. For example, dual registrants would be required to present all of the information required by Items 2 through 4 and Item 6 in a tabular format,[60] comparing advisory services and brokerage services side-by-side, with prescribed headings.[61] Similarly, standalone broker-dealers and investment advisers would be required to provide general information about fee types in tabular format, in a separate comparison section.[62] All firms would be permitted to use charts, graphs, tables, and

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57 Firms should keep in mind the applicability of the antifraud provisions of the federal securities laws, including section 206 of the Advisers Act, section 17(a) of the Securities Act, and section 10(b) of the Exchange Act and rule 10b-5 thereunder, in preparing the relationship summary.

58 *See* proposed General Instruction 3 to Form CRS. Firms may omit or modify prescribed wording or other statements required to be part of the relationship summary if such statements are inapplicable to a firm's business or would be misleading to a reasonable retail investor.

59 *See* 917 Financial Literacy Study, *supra* note 20, at iv, xx, 21 – 22; *see also* Benbasat & Dexter, *infra* note 592.

60 Empirical evidence suggests that visualization improves individual perception of information (*see* Hattie, *infra* note 591) and that tabular reports may lead to better decision making (*see* Benbasat & Dexter, *infra* note 592).

61 Dual registrants must present the information in Items 2 through 4 and Item 6 in a tabular format, comparing advisory services and brokerage services side-by-side. In the column discussing brokerage services, firms must include the heading "Broker-Dealer Services" and the sub-heading "Brokerage Accounts." In the column discussing investment advisory services, firms must include the heading "Investment Adviser Services" and the sub-heading "Advisory Accounts." *See* proposed General Instruction 1.(e) to Form CRS.

62 Standalone broker-dealers and investment advisers would be required to include the sub-heading "You can receive advice in either type of account, but you may prefer paying:" and present prescribed information comparing a transaction-based fee and an asset-based fee in side-by-side columns, in a tabular format. *See* proposed Items 5.A.4. and 5.B.6. of Form CRS.

other graphics or text features to explain the information, so long as the information is responsive to and meets the requirements in the Instructions (including the space limitations).[63] The use of a graphical presentation would be prohibited if it is inaccurate or misleading or, because of its nature, quantity, or manner of presentation, obscures or impedes understanding of the information that is required to be included. Firms that choose to use interactive graphics or tools may include Instructions on their use and interpretation.[64] We believe that standardizing the relationship summaries among firms by specifying the headings, sequence, and content of the topics; prescribing language for firms to use as applicable; and limiting the length of the relationship summary will provide comparative information in a user-friendly manner that helps retail investors with informed decision-making.[65]

We request comment on the following for the relationship summary.

- Should firms only be required to deliver the relationship summary to retail investors? Or should they be required to deliver one to other types of investors, too, such as individuals representing sole proprietorships or other small businesses, or institutional investors that are not natural persons, including workplace retirement plans and funds? Would such investors have the need for the information in the relationship summary to facilitate a choice among different firms, financial professionals, and account types? Or would these investors rely directly on the more detailed disclosures in the Form ADV Part 2 brochure or pursuant to Regulation Best Interest?

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63 Proposed General Instruction 1.(f) to Form CRS.

64 *Id*.

65 Empirical evidence suggests that users are better able to make coherent, rational decisions when they have comparative, standardized disclosure that allows them to assess relevant trade-offs. *See infra* note 593 and accompanying text.

- Should retail investors be defined for purposes of Form CRS to include all natural persons, as proposed? Should we instead exclude certain categories of natural persons based on their net worth or income level, such as accredited investors,[66] qualified clients,[67] or qualified purchasers?[68] If we did exclude certain categories of natural persons based on their net worth, what threshold should we use for measuring net worth? Should we exclude certain categories of natural persons for other reasons?

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66 Accredited investors include natural persons who (i) have a net worth over $1 million, either individually or together with a spouse (excluding the value of the primary residence); (ii) had an individual income greater than $200,000 (or $300,000 together with a spouse) in each of the two most recent years, and has a reasonable expectation of reaching the same income level in the current year; or (iii) for purposes of a securities offering of a particular issuer, are directors, executive officers, or general partners of that issuer. Accredited investors also include non-natural persons, such as, banks, broker-dealers, insurance companies, investment companies registered under the Investment Company Act of 1940, and certain partnerships, corporations, nonprofit entities, retirement plans, and trusts. 17 CFR 230.501.

67 A qualified client is a client that meets one or more of the following criteria: (i) is a natural person or company that has at least $1 million in assets under management with the adviser immediately after entering into an investment advisory contract with the adviser; (ii) the adviser reasonably believes the natural person has a net worth (together with assets held jointly with a spouse) of more than $2.1 million immediately prior to entering into an advisory contract (excluding the value of the primary residence); (iii) the adviser reasonably believes the natural person or company is a "qualified purchaser" as defined in section 2(a)(51)(A) of the Investment Company Act at the time an advisory contract is entered into; (iv) is an executive officer, director, trustee, general partner, or person serving in a similar capacity, of the adviser; or (v) is an employee of the adviser who participates in the investment activities of the adviser, and has performed investment activities for at least twelve months. The dollar thresholds under the definition of qualified client are subject to inflation adjustments every five years. 17 CFR 275.205-3(d)(1); Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205-3 under the Investment Advisers Act of 1940, Investment Advisers Act Release No. 4421 (Jun. 14, 2016) [81 FR 39985 (Jun. 20, 2016)].

68 The term "qualified purchaser" has been defined for purposes of the Investment Company Act and for the Securities Act. Under the Investment Company Act, the term "qualified purchaser" includes any natural persons who or certain family-owned companies that own not less than $5 million in investments; certain trusts; and any person, acting for its own account or the accounts of other qualified purchasers, who in the aggregate owns and invests on a discretionary basis, not less than $25 million in investments. 15 U.S.C. 80a-2(a)(51)(A).

For purposes of section 18(b)(3) of the Securities Act, the term "qualified purchaser" means any person to whom securities are offered or sold pursuant to a Tier 2 offering as defined in Regulation A. 17 CFR 230.256. Tier 2 offerings generally may be sold only to (i) accredited investors; (ii) natural persons for whom the aggregate purchase price to be paid by the purchaser for the securities is no more than 10% of the purchaser's annual income or net worth; or (iii) non-natural persons for which the aggregate purchase price to be paid by the purchaser for the securities is no more than 10% of its revenue or net assets for the most recently completed fiscal year. 17 CFR 230.251.

- Should we conform the definition of retail investor to the definition of retail customer as proposed in Regulation Best Interest, which would include non-natural persons who use the recommendation primarily for personal, family, or household purposes? Should the definition of retail investor include trusts or similar entities that represent natural persons, as proposed? Are there other persons or entities that should be covered? Should we expand the definition to cover plan participants in workplace retirement plans who receive services from a broker-dealer or investment adviser for their individual accounts within a plan?
- Should we include any additional definitions of terms or phrases in the relationship summary? Should we omit any definitions we have proposed for the relationship summary? Should any of the proposed definitions be changed? If so, why?
- Will the length and presentation proposed for the relationship summary be effective for retail investors? Are there other approaches we should consider? What are the benefits and drawbacks of shorter or longer disclosure for retail investors relative to the proposed approach?
- We are proposing that the relationship summary discuss all of the firm's advisory and brokerage services in one relationship summary. Should we instead permit firms to prepare a separate relationship summary for different business lines or different programs or types of accounts and/or services that a broker-dealer or investment adviser offers? If we adopt such an approach, how could we modify the requirements to allow for comparison among account options within and across firms? For example, should we require that each such separate summary refer to the other summaries and include hyperlinks or other electronic features if presented on a firm's website? Should we

require the use of hyperlinks that direct the investor directly to specific disclosure (*i.e.*, a "deep link") or a more general landing page? How would delivery obligations be formulated to ensure that retail investors receive sufficient but still user-friendly information?

- In the alternative, should we permit or require firms to prepare one relationship summary for the entire affiliated group or firm complex, *i.e.*, to summarize the services offered to retail investors of all affiliated companies together in a single relationship summary? What factors should dictate whether affiliates should be permitted or required to prepare a single relationship summary? For example, should we base any permissive instruction or requirement on whether the affiliates typically market services of multiple investment advisers and broker-dealer entities together? What about investment advisers and broker-dealers that are not affiliates but have partnership agreements, are part of one wrap fee program,[69] or other arrangements? Should they be required or permitted to cross-reference to other firms?
- Should we permit the relationship summary, or any part of it, to substitute for other disclosure obligations that broker-dealers or investment advisers have, if the disclosure obligations overlap? If so, for what disclosures could the relationship summary substitute? If not, why not?

[69] A wrap fee program would be defined as an advisory program under which a specified fee or fees not based directly upon transactions in a retail investor's account is charged for investment advisory services and the execution of retail investor transactions. Proposed General Instruction 9.(g) to Form CRS. *See infra* note 173.

- Does the proposal sufficiently encourage electronic design and delivery? Are there other ways we can modify the requirements to make clear that paper-based delivery is not the only permissible or desired delivery format?
- With respect to firms that use paper delivery to meet investor preferences, are the proposed presentation and content requirements appropriate for a relationship summary provided in paper or in PDF (*e.g.*, 11 point font, and have margins of at least 0.75 inches on all sides)? Would they be helpful in encouraging relationship summaries that address retail investors' preferences for concise and user-friendly information? If not, what requirements would improve the document's utility and accessibility for retail investors? In particular, are there any areas where requiring the use of a specific check-the-box approach, bullet points, tables, charts, graphs or other graphics or text features would be helpful in presenting any of the information or making it more engaging to retail investors? Should we include different requirements for font size, margins and paper size? Should we restrict certain types or sizes of font, color choices or the use of footnotes?
- Are there special technical specifications we should consider for other forms of electronic or online delivery on phones, tablets and other devices, and for information conveyed via videos, interactive graphics, or tools and calculators? Are the Instructions to the relationship summary sufficiently flexible to permit delivery on phones, tablets and other devices and to accommodate information conveyed via videos, interactive graphics, or tools and calculators? Should we require that firms make the relationship summary available by specific forms of electronic delivery or certain electronic devices? How can the Commission encourage investment advisers and broker-dealers to make fuller use of

innovative technology to enable more interactive, user-friendly relationship summary disclosure, while still creating a short, easy-to-read relationship summary that includes the proposed content? Are there potential tools that the Commission should encourage or require firms to use in order to make their disclosures more interactive and understandable? For instance, should we permit or require a firm to use pop-ups or hovers to provide retail investors with additional information required or permitted by the relationship summary, without retail investors having to scroll to find the information in another section of the relationship summary? Would this tool be useful for firms to use, for example, in the Introduction section of the relationship summary, so that a retail investor could access upfront additional information about the terms used (advisory and brokerage accounts) that is presented in other sections of the relationship summary? Instead of requiring and permitting hyperlinks in certain circumstances (*e.g.*, to link to an adviser's Form ADV or a fee schedule), are there other technological tools that would better help an investor find information that is cross-referenced in the relationship summary? Should we permit or require other technologies (such as QR codes[70]) in addition to or in lieu of hyperlinks to connect to such information?

- Would retail investors be more likely to read a firm's relationship summary if we required or permitted firms to use certain design elements – such as larger font sizes or greater use of white space, colors, or visuals? Could this be accomplished while still providing retail investors with the information we are proposing to require in a short and easy-to-read relationship summary?

[70] A QR code is a two-dimensional barcode capable of encoding information such as a website address, text information, or contact information. These codes are becoming increasingly popular in print materials and can be read using the camera on a smartphone.

- We are proposing that the firm use plain language principles and the Instructions refer to the SEC's Plain English Handbook. Should we modify any of these principles? Should the Instructions refer to any other principles to promote understandable wording?
- Do firms commonly market to non-English speakers or provide information – including marketing materials – in languages other than English? To what extent would firms expect to deliver a relationship summary in a language other than English? Should we propose requirements to prepare relationship summaries in languages other than English? For example, should we require that firms prepare, file, and deliver a relationship summary in any language in which they disseminate marketing materials? Are there concerns with translating the relationship summary without also having to translate the firm's other disclosures? If so, what are those concerns?
- Should we limit the relationship summary to four pages (or equivalent limit if in electronic format), as proposed? Is this enough space for firms to provide meaningful information? Should we instead eliminate page limits (and their equivalent for electronic format) or increase the amount of permitted pages or their equivalent? Are there particular items that may require longer responses than others? If so, how should the Commission take these into account in considering page limits? For example, if commenters believe the use of graphics will be more effective to communicate fees, should we permit a greater number of pages to account for the use of graphics? Conversely, will retail investors read four pages? Should the page limit be shorter, such as one to three pages? If so, what information in the proposed requirements should we omit? Should we have different page limits for dual registrants than for firms that offer

only brokerage or only advisory services? If we do require shorter disclosure, what information should firms be required to provide regardless of the length?

- Are there too few or too many items that would be required in the relationship summary? Are there other items that we should also require or proposed items that we should delete? Do commenters agree that we should only permit the items required by the relationship summary? Is there other information that we should permit, but not require, firms to include? If so, what items are those?
- Do commenters agree that all items should be presented in the same order under the same heading to promote comparability across firms? Why or why not? If the items are not listed in the same order, could retail investors still easily compare firm relationship summaries? Does the prescribed order work, or should we consider a different order? Is there information that we should always require to appear on the first page or at the beginning of an electronic relationship summary? Are there any specifications we should include to enhance comparability for electronic delivery of the relationship summary in various forms?
- Should we, as proposed, prescribe headings for each item or allow firms to choose their own headings? Should we require or permit a different style of headings, such as a question and answer format or other wording to encourage retail investors to continue reading?
- Should we permit firms to include additional disclosure with the relationship summary, such as a comprehensive fee table, or other disclosures? Would the inclusion of additional disclosures affect whether retail investors would view the relationship summary? What are the benefits and drawbacks of such an approach?

- Should we generally permit firms to use charts, graphs, tables, and/or other graphics or text features to explain the information required by the relationship summary (so long as any such feature meets requirements as specified in the Instructions), as proposed? Should we permit firms to choose the graphical presentation that they will use? Are there specific graphical presentations that we should require? Should we permit other mediums of presentation, such as the use of video presentations?
- Do any elements of the proposed presentation requirements impose unnecessary costs or compliance challenges? Please provide specific data. Are there any changes to the proposal that could lower those costs? Please provide examples.
- Are the mock relationship summaries useful and illustrative of the proposed form requirements? Do they appropriately show the level of detail that firms might provide?

With respect to each item for which we prescribe wording in the relationship summary, we request the following comment on each of those required disclosures:

- Does the narrative style work for the prescribed wording or are there other presentation formats that we should require? Should the Commission instead require more prescribed wording? Conversely, is there prescribed wording we have proposed that we should modify or replace with a more general instruction that allows firms to use their own description?

B. Items

1. Introduction

We are proposing that the beginning of the relationship summary contain a title highlighting the types of investment services and accounts the firm offers to retail investors, specifically "Which Type of Account is Right for You – Brokerage, Investment Advisory or

Both?" for dual registrants and "Is a[n] [Brokerage/Investment Advisory] Account Right for You?" for standalone brokerage firms or investment advisory firms, respectively.[71] A firm also would be required to include its name, whether it is registered with the Commission as a broker-dealer, investment adviser, or both, and date of the relationship summary prominently on the first page or beginning of the electronic disclosure (this information could be included in the header or footer).[72]

An introductory paragraph would briefly explain the types of accounts (brokerage accounts and/or investment advisory accounts) and services the firm offers. Using prescribed wording, all firms would be required to state: "There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you." In a new paragraph and using prescribed wording and bold font, a standalone broker-dealer would be required to state: "We are a broker-dealer and provide brokerage accounts and services rather than advisory accounts and services."[73] Likewise, a standalone investment adviser would be required to state in bold font: "We are an investment adviser and provide advisory accounts and services rather than brokerage accounts and services."[74] Dual registrants would include a similar statement in bold font that discusses both types of services, specifically: "Depending on your needs and investment objectives, we can provide you with services in a

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71 Proposed Items 1.B., 1.C. and 1.D. of Form CRS.

72 Proposed Item 1.A. of Form CRS. The disclosure of Commission registration would make the relationship summary consistent with proposed rules 15l-3 of the Exchange Act and 211h-1 of the Advisers Act, which would require that a broker-dealer and a registered investment adviser prominently disclose that it is registered with the Commission as a broker-dealer or investment adviser, respectively, in print or electronic retail investor communications.

73 Proposed Item 1.B. of Form CRS.

74 Proposed Item 1.C. of Form CRS.

brokerage account, investment advisory account, or both at the same time."[75] Finally, all firms would be required to include: "This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page [ ]."[76]

The proposed introductory paragraph sets up a key theme of the relationship summary – helping retail investors to understand and make choices among account types and services. For example, some retail investors want to receive periodic recommendations while others prefer ongoing advice and monitoring. Some retail investors wish to pursue their own investment ideas and direct their own transactions, while others seek to delegate investment discretion to the firm. Emphasizing that there are different types of accounts and services from which a retail investor may choose would help the retail investor make an informed choice about whether the firm provides services that are the right fit for his or her needs and help the retail investor to choose the right firm or account type. Although the disclosures are intentionally simplified and generalized, we believe they would help retail investors to obtain more detailed information.

We request comment generally on the proposed requirement for firms to include specific information in the introduction.

- In addition to the title, firm name and SEC registration status, and date, is there other information that we should require at the beginning of the relationship summary? Should we instead require a cover page? Are the titles we proposed in the Instructions appropriate? What alternatives should we consider? Should we allow firms to select their own title for the relationship summary?

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75 Proposed Item 1.D. of Form CRS.

76 Proposed Items 1.B. – 1.D. of Form CRS.

- Should we require firms to include the prescribed wording, as proposed, or should we allow more flexibility in the words they use? Should we modify the prescribed wording? Does the proposed wording capture the range of business models among investment advisers and broker-dealers? Would the prescribed wording require a firm to provide any inaccurate information given that firm's circumstances? Instead of the proposed prescriptive wording, should the Commission permit or require a more open-ended narrative?
- Is there additional information we should require in the introduction?
- Should we require that standalone brokerage and investment advisory firms include a statement that the retail investor may instead prefer investment advisory or brokerage services, respectively? Why or why not?

2. Relationships and Services

After the introduction, the proposed relationship summary would provide information about the relationships between the firm and retail investors and the investment advisory account services and/or brokerage account services the firm provides to retail investors.[77] The section would begin with the heading "Relationships and Services" for a standalone broker-dealer or investment adviser.[78] A dual registrant would use the heading "Types of Relationships and Services," followed by this statement: "Our accounts and services fall into two categories."[79] Each firm would discuss specific information about the nature, scope, and duration of its

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77 Proposed Item 2 of Form CRS.

78 Proposed Item 2.A. of Form CRS.

79 *Id.*

relationships and services, including the types of accounts and services the firm offers, how often it offers investment advice, and whether the firm monitors the account.

This item requires firms to provide specific information with a mix of prescribed wording and short narrative statements. As discussed above, if a prescribed statement is not applicable to the firm's business or would be misleading to a reasonable retail investor, the firm would be permitted to omit or modify that statement.[80] We have designed these requirements to provide retail investors with consistent, concise, and meaningful information about the services they would receive from a firm and help them to ask relevant questions, compare firms' services against each other, and make more informed choices about the services they choose.

We considered an approach whereby firms would be required to complete a prescribed checklist of common characteristics of brokerage and advisory accounts, indicating which characteristics applied to their accounts and services. This approach could improve comparability among firms. We are concerned, however, that this approach would not be sufficiently flexible to accommodate the variety of business models and services that broker-dealers and advisers provide, and that a mix of prescribed wording and narrative format would help investors better understand the firm's services. We believe that our proposed approach provides enough information to help retail investors understand and choose between investment advisory accounts and brokerage accounts without overwhelming them with too much information.

Brokerage Account Services. We propose requiring broker-dealers to summarize the principal brokerage services that they provide to retail investors.[81] First, broker-dealers would

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80 *See supra* note 58 and accompanying text.

81 Proposed Item 2.B. of Form CRS.

include the following wording to explain the transaction-based nature of their fees (emphasis required): "If you open a brokerage account, you will pay us a ***transaction-based fee***, generally referred to as a commission, every time you buy or sell an investment."[82] Even though a separate section of the relationship summary would discuss a firm's fees, we believe it is important for broker-dealers to explain transaction-based fees at the beginning of the disclosure because these types of fees are typically a critical distinction between brokerage and investment advisory accounts.[83]

Next, broker-dealers that offer accounts in which they offer recommendations to retail investors would state that the retail investor may select investments or the broker-dealer may recommend investments for the retail investor's account, but that the retail investor will make the ultimate investment decision regarding the investment strategy and the purchase or sale of investments.[84] Broker-dealers that offer accounts in which they do not offer recommendations to retail investors (*e.g.*, execution-only brokerage services) would state that the retail investor will select the investments and make the ultimate investment decision regarding the investment strategy and the purchase or sale of investments.[85] Starting with a clear description of the services provided in a brokerage account by a broker-dealer – including the retail investor's choice of receiving recommendations or self-directing his or her investments, and the fact that the retail investor will make the ultimate investment decision – would help address confusion

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82 Proposed Item 2.B.1. of Form CRS.

83 *See infra* note 126 (discussing our use of the term "transaction-based fees" in the relationship summary).

84 Proposed Item 2.B.2. of Form CRS.

85 *Id.*

about the services that broker-dealers offer to retail investors.[86] This language also highlights differences from the services that investment advisers would describe, discussed below.

Next, we propose requiring broker-dealers to state if they offer additional services to retail investors, including, for example: (a) assistance with developing or executing the retail investor's investment strategy (*e.g.*, the broker-dealer discusses the retail investor's investment goals or designs with the retail investor a strategy to achieve the retail investor's investment goals); or (b) monitoring the performance of the retail investor's account.[87] They would also state that a retail investor might pay more for these additional services, if applicable.[88] Broker-dealers that offer performance monitoring as part of the standard brokerage account services would indicate how frequently they monitor the performance.[89] While broker-dealers do not undertake to provide investment strategy and performance monitoring services when they give recommendations, we recognize that many broker-dealers offer these services to retail investors as part of their account agreement. We believe that retail investors would benefit from disclosure that such services exist, and that broker-dealers might charge higher fees for these services. Broker-dealers would also be required to briefly describe any regular communications they have with retail investors, such as providing account statements, giving an overview of transactions during a period, or evaluating the account's performance.[90] Firms would include the frequency (*e.g.*, at least quarterly) and the method (*e.g.*, by email, phone or in person) of the

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86 We believe that retail investors have the ultimate investment decision for their investment strategy and the purchase or sale of investments, even if the broker-dealer has temporary or limited discretion over retail investors' accounts. *See* Regulation Best Interest Proposal, *supra* note 24, at section II.F.

87 Proposed Item 2.B.3. of Form CRS.

88 *Id.*

89 *Id.* Broker-dealers that monitor the performance of the retail investor's account, as market and customer conditions demand (rather than on a specific time schedule), could state so.

90 *Id.*

communications.[91]

Finally, broker-dealers would be required to include the following if they significantly limit the types of investments available to retail investors in any accounts: "We offer a limited selection of investments. Other firms could offer a wider range of choices, some of which might have lower costs."[92] A broker-dealer would significantly limit the types of investments if, for example, the firm only offers one type of asset (*e.g.*, mutual funds, exchange-traded funds, or variable annuities), the firm only offers mutual funds or other investments sponsored or managed by the firm or its affiliate (*i.e.*, proprietary products), or the firm only offers a small choice of investments.[93] In addition, if the limitations only apply to some of the accounts the firm offers, such as, for example, limiting the types of investments for retail investors within different asset tiers, then the firm would have to identify those accounts.[94]

Limitations on investments offered could have a significant effect on investor choice and performance of the account over time. In particular, firms that offer proprietary products exclusively preclude investor access to competing products that could offer lower fees or result in better performance over time. As a result, retail investors should understand these limitations before they enter into a relationship with a firm.

Advisory Account Services. We propose requiring investment advisers that offer investment advisory accounts to retail investors to summarize the principal investment advisory services provided to retail investors.[95] First, investment advisers would be required to state the

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91 *Id.* We are proposing the same requirement for investment advisers, described below. *See infra* note 102 and accompanying text.

92 Proposed Item 2.B.4. of Form CRS.

93 *Id.*

94 *Id.*

95 Proposed Item 2.C. of Form CRS.

type(s) of fee they receive as compensation if a retail investor opens an investment advisory account.[96] For example, an investment adviser would state if it charges an on-going asset-based fee based on the value of the cash and investments in the advisory account, a fixed fee, or some other fee arrangement. A standalone adviser would also state how frequently it assesses the fee.[97] Similar to the requirement for broker-dealers,[98] we are proposing to require a statement about how investment advisers charge fees up-front because of the importance that investors understand how they will pay for services and to highlight this critical distinction between brokerage and advisory accounts. We are proposing to require that firms describe additional fees associated with these services in the discussion of fees and costs. Because the fees charged by each investment adviser may differ, we are not prescribing specific wording and instead are allowing firms flexibility in choosing the exact wording to use for this disclosure. Advisers would, however, emphasize the type of fee in bold and italicized font.[99]

Next, investment advisers would state that they offer advice on a regular basis, or, if they do not offer advice on a regular basis, they would state how frequently they offer advice.[100] They would also state the services they offer to retail investors including, for example, (a) assistance with developing the retail investor's investment strategy (*e.g.*, the investment adviser discusses the retail investor's investment goals or designs with the retail investor a strategy to achieve the

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96 Proposed Item 2.C.1. of Form CRS. The relationship summary would refer to "account advisory services" and "opening an account" to simplify the explanations for retail investors. When an investment adviser provides investment advisory services, the client may have a custodial account with another firm, such as a broker-dealer or bank. A dual registrant may maintain custody for an advisory client's assets as broker-dealer. We are not proposing to require that firms include these nuances in the discussion of relationships and services.

97 *Id.*

98 *See supra* note 82 and accompanying text.

99 Proposed Item 2.C.1 of Form CRS.

100 Proposed Item 2.C.2. of Form CRS.

retail investor's investment goals), or (b) how frequently they monitor the retail investor's accounts.[101] Similar to broker-dealers, advisers would include the frequency (*e.g.*, at least quarterly) and the method (*e.g.*, by email, phone or in person) of the communications.[102] We believe that the regularity of advice and other services that investment advisers commonly provide, including, as applicable – discussions with the retail investor, designing a strategy to achieve investment goals, monitoring, and reporting on performance – are key aspects of services that advisers commonly provide.[103] As discussed above with respect to broker-dealers, these services can distinguish advisory accounts from brokerage accounts and therefore the disclosure will help retail investors determine which type of account best suits their needs.

Additionally, investment advisers would state if they offer advisory accounts for which they exercise investment discretion (*i.e.*, discretionary accounts), accounts for which they do not exercise investment discretion (*i.e.*, non-discretionary accounts), or both.[104] For purposes of this Item in the relationship summary, investment advisers generally should use the same definition of "discretionary authority" as in Form ADV, which is the authority to decide which securities to purchase and sell for the client, or the authority to decide which investment advisers to retain on behalf of the client.[105] If an investment adviser offers a discretionary account, the relationship summary would state that a discretionary advisory account allows the firm to buy and sell investments in the retail investor's account, without asking the retail investor in advance. For a non-discretionary advisory account, the relationship summary would state that the firm gives

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101 *Id.*

102 *Id.*

103 An agreement for advisory services typically defines the scope and specific types of services provided.

104 Proposed Item 2.C.3. of Form CRS. Investment advisers would be required to emphasize the type of account (discretionary and non-discretionary) in bold and italicized font.

105 Term 12 of Glossary of Terms to Form ADV.

advice and the retail investor decides what investments to buy and sell.[106]

We believe it is important for retail investors considering an advisory account to understand the difference between discretionary services and non-discretionary services, as that distinction would affect the degree of control the retail investor would provide to the adviser. Discretionary advice is also a common feature of many investment advisory accounts,[107] so explaining discretion would benefit a retail investor in choosing between brokerage and investment advisory services, as well as between different types of advisory accounts.

Finally, as we are proposing for broker-dealers, investment advisers that significantly limit the types of investments available to retail investors in any accounts would include the same statement that broker-dealers would be required to include, and if such limits only apply to certain accounts, the investment adviser would identify those accounts, for the same reasons discussed above.[108]

Affiliate Services. We recognize that many investment advisers and broker-dealers that are not dual registrants nonetheless have affiliates that are broker-dealers or investment advisers, respectively. Often, these standalone firms offer their affiliates' services to retail investors. For example, an affiliated sub-adviser also may manage a portion of a retail investor's portfolio or an investment adviser may effect trades for client accounts through an affiliated broker-dealer. We would allow these firms to state that they offer retail investors their affiliates' brokerage or

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106 Proposed Item 2.C.3. of Form CRS.

107 In 1992, only approximately three percent of SEC-registered advisers had discretionary authority over client assets; as of March 31, 2018, according to data collected on Form ADV, 91 percent of SEC-registered advisers have that authority.

108 Proposed Item 2.C.4. of Form CRS. The required statement would be "Our investment advice will cover a limited selection of investments. Other firms could provide advice on a wider range of choices, some of which might have lower costs." Also consistent with the requirements for broker-dealers, such limitations could include, for example, only offering a selection of mutual funds, equities, or proprietary products.

advisory services, as applicable.[109] We believe that the inclusion of this disclosure could make clear the choice investors have within affiliated firms and give financial professionals an opportunity to discuss these services.

We request comment generally on the proposed requirement for firms to include specific information about the relationships and services offered in their advisory and brokerage accounts.

- Would the proposed summary of relationships and services help retail investors to make informed choices about whether investment advisory or brokerage services better suit their needs? If not, how should we revise it?
- Would the proposed requirements result in disclosure that is clear, concise, and meaningful to retail investors? Would this information help retail investors to better understand the general differences in the services that investment advisers and broker-dealers provide? Are there other differences in the services provided by investment advisers and broker-dealers that we should require firms to discuss in this section? If so, should we permit or require information about those differences in the summary of services? Are there any common misconceptions about services provided by broker-dealers, investment advisers, or dual registrants that the relationship summary should specifically seek to clarify or correct?
- Would more or less information about a firm's services be helpful for retail investors? Are there any elements of the proposed requirements that firms should or should not include? If so, why? Should any of the required disclosures be

[109] Proposed Item 2.D. of Form CRS. This disclosure only applies in the context of an affiliate of the firm. This is not intended to describe disclosure of a financial professional's outside business activities, such as an outside investment advisory business of a broker-dealer registered representative.

included in a different section of the relationship summary? Is the proposed order of the information appropriate, or should it be modified? If so, how should it be modified? Should we allow firms the flexibility to present this information in a different order if doing so makes their relationships and services more understandable to retail investors?

- Is the proposed heading and the introductory wording for firms clear and useful to retail investors? Are there alternative headings we should consider?
- Does the mix of prescribing wording for some information and requiring brief narratives for other information strike the right balance between having similar, neutral wording to promote comparisons and permitting firms to conform the language to reflect the services they offer? Should the Commission instead require more prescribed wording in this Item? Conversely, is there prescribed wording we have proposed that we should modify or replace with a more general instruction that allows firms to use their own description?
- Does the prescribed wording we are proposing capture the range of business models of investment advisers and broker-dealers? Would the prescribed wording require any firm to state something inaccurate in the relationship summary? Should we instead provide more flexibility to change the prescribed wording?
- Should we require broker-dealers to include prescribed wording about transaction-based fees and investment advisers to state the type of fee for an advisory account at the beginning of this section, or should fees only be discussed in the fee section?

- How should broker-dealers describe execution-only accounts, sometimes referred to as "discount" brokerage, and accounts in which they provide recommendations concerning securities, sometimes referred to as "full-service" brokerage? Should we, as proposed, require that broker-dealers offering recommendations to retail investors state that the retail investor may select investments or the broker-dealer may recommend investments, but the retail investor will make the ultimate investment decision? Should we also, as proposed, require that broker-dealers only offering discount brokerage accounts to retail investors state that the retail investor will select the investments and make the ultimate investment decision? Should we require prescribed language about these accounts, or should we permit a brief narrative as proposed? Should firms be permitted or required to use the terms "full-service" accounts and "discount" brokerage accounts, or other terms, so long as they are likely to be understood? Do investors understand the meanings of these terms?
- Should investment advisers that provide investment advisory services be required to discuss both discretionary and non-discretionary account services, regardless of whether they offer both discretionary and non-discretionary accounts? Should they instead be permitted to describe only the service they offer? Do firms offer accounts that involve limited discretionary services that would not be covered in the proposed discussions of discretionary and non-discretionary accounts? If so, how should the requirements be changed to reflect these accounts? Should we also require investment advisers to state that they offer advice on a regular basis, or, if not on a regular basis, state how frequently they offer advice? Should we

require the disclosure of any additional information about the advice an investment adviser provides?

- We are proposing to require firms to disclose if they offer certain additional services, such as assistance with developing or executing the retail investor's investment strategy, and performance monitoring, and to briefly describe any regular communications they have with retail investors. Are there services in addition to those in the Instructions that broker-dealers and investment advisers also should disclose? Should we require disclosure of the same types of additional services for both broker-dealers and investment advisers?
- We understand that, to some extent, all firms limit the investments offered to retail investors. Would other disclosures regarding a firm's product offering limitations be helpful to investors, in addition to the proposed disclosures for firms that significantly limit the types of investments that are available? Why or why not? Should we, for example, require firms that only offer proprietary investments to also state that the only investments available to a retail investor are investments that the firm or its affiliates issue, sponsor, or manage? How feasible would this disclosure be for a firm that has several account types? Should we consider other alternatives?
- Is it clear what we mean by "significantly limit" with regard to the requirement to disclose limitations on investment choices? Should we provide additional examples or more prescriptive instructions regarding when firms must disclose such limitations? Are there other ways a firm may significantly limit the types of investments that should be captured by this instruction?

- Should we permit firms to prepare different relationship summaries for different types of services and lines of business, particularly where the firm offers a broad array of accounts and services? Would separate relationship summaries still promote comparability across firms and the ability to understand the differences between advisory and brokerage services?
- Would the proposed summary of services allow retail investors to easily compare the services provided by different firms? If not, what changes to the requirements should we make to increase comparability?
- Would other disclosures about a firm's services be more helpful for retail investors? Should we permit or require firms to describe services they offer to retail investors, in addition to brokerage and advisory services, such as insurance services? Would such disclosure about other services give retail investors a more complete overview of a firm's offerings, or would it detract from the other disclosures, for example, by overwhelming the more important information about a firm's brokerage and advisory services?
- Should we require firms to include more details about the specific services provided for each type of advisory account or brokerage account that they offer? Should the relationship summary help investors to choose among a variety of account options that the firm offers, rather than providing more summary information about the advisory and brokerage services that are offered?
- Some dual registrants have implemented a default relationship for retail investors, where, for example, the firm will act as a broker-dealer with respect to the account unless specifically stated otherwise. Should we require these firms to

disclose that they are acting as a broker-dealer (or investment adviser, as applicable) with respect to the account unless the firm specifically states otherwise?

- Should we, as proposed, allow firms with affiliated broker-dealers or investment advisers to state that they offer retail investors additional brokerage or advisory services, as applicable, through their affiliates? Should we require such statements, if applicable? Should we permit or require firms to expand on the different types of services available to their retail investors through the firm's affiliates? Should affiliates be required or permitted to use a single relationship summary that describes the services of all affiliates? If not, why not? What are the advantages and disadvantages to the retail investor?
- Should we also permit or require disclosure regarding a firm's relationships with other third parties, such as where the registered representatives of a broker-dealer are also investment adviser representatives of an unaffiliated investment adviser or where an investment adviser uses a single unaffiliated broker-dealer to provide execution and custody and generally does not consider execution through other firms?
- Should we require investment advisers and broker-dealers to disclose whether they have a minimum account size and state that minimum (or range of minimums) if the account minimum varies by account? If applicable, should we require disclosure that the selection of investments or services is limited by account size? Would this help investors understand whether they are eligible for certain accounts or certain services and understand the ways in which their

investment choices may be limited? Are there any drawbacks to requiring such disclosure?

- So-called robo-advisers and online broker-dealers represent a fast-growing trend within the brokerage and investment advisory industries. They employ a wide range of business models. For example, differences among robo-advisers and online broker-dealers include: the degree of reliance on computer algorithms (as opposed to individualized human judgment) to generate financial advice; the level of human interaction between the client or customer and firm personnel; and the use of the internet to communicate with clients and customers. Are the Instructions pertaining to relationships and services sufficient and appropriate to capture the business models of robo-advisers and online broker-dealers? For example, would it be appropriate to require or permit descriptions regarding the degree of human involvement in the oversight and management of individual client accounts, how computer algorithms are used in generating investment advice, and the availability of financial professionals to answer retail investors' questions? Do the requirements with respect to the content and delivery of the relationship summary, as further discussed below, allow retail investors to make informed decisions about entering into a relationship with a robo-adviser, other type of investment adviser, or broker-dealer?

3. Obligations to the Retail Investor – Standard of Conduct

Following the relationships and services section, the relationship summary would include a brief section, using prescribed wording, to describe the firm's legal standard of conduct to the

retail investor.[110] The section would begin with the heading "Our Obligations to You" and the following language: "We must abide by certain laws and regulations in our interactions with you." Firms would then use prescribed wording describing the standard of conduct applicable to investment advisers and/or broker-dealers.[111] As with certain other sections of the relationship summary, dual registrants would provide this information in tabular format to facilitate comparison.

We understand that the standard of conduct that applies to firms and financial professionals has been a source of investor confusion.[112] For example, the 913 Study noted that retail investors were not clear about the specific legal duties of broker-dealers and investment advisers.[113] We believe that providing a brief overview of the standards of conduct to which broker-dealers and investment advisers must adhere, including the differences between the standards of care of broker-dealers and investment advisers, could help alleviate this confusion. We further believe that providing this overview, in combination with the key question about the financial professional's legal obligations discussed below, would encourage a conversation between the retail investor and the financial professional about applicable legal obligations.[114]

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110 Proposed Item 3.A. of Form CRS.

111 Proposed General Instruction 1.(e) to Form CRS.

112 *See, e.g.*, Siegel & Gale Study, *supra* note 5; and RAND Study, *supra* note 5. *See also* CFA Survey, *supra* note 5.

113 *See* 913 Study, *supra* note 3, at v. *See also* Rand Study, *supra* note 5.

114 *See infra* at Section II.B.8. Similarly, certain DOL regulations already obligate firms and financial professionals to acknowledge fiduciary status when they provide certain advisory type services to workplace retirement plans subject to ERISA and to IRAs. *See, e.g.*, 29 CFR 2550.408g-1(b)(7)(i)(G) (regulation under statutory exemption for participant advice requires fiduciary advisers to plans and IRAs seeking exemptive relief to provide advice and receive compensation to acknowledge fiduciary status); 29 CFR 2550.408b-2(c)(1)(iv)(B) (regulation under statutory exemption for reasonable service arrangements requires certain ERISA-covered plan service providers to state, if applicable, that the service provider will provide or reasonably expects to provide services as a "fiduciary" as defined by ERISA). Similarly, the DOL's BIC Exemption, *see infra* note 504, would require an investment advice fiduciary that seeks to rely

We also believe that prescribing language is appropriate to promote consistency in communicating these standards to retail investors.[115]

Broker-Dealers. We are proposing a required description of the standard of conduct for broker-dealers based on the proposed standards in Regulation Best Interest, as well as existing obligations of broker-dealers when they provide services to customers. First, a broker-dealer that provides recommendations subject to Regulation Best Interest[116] would include the following wording: "We must act in your best interest and not place our interests ahead of yours when we recommend an investment or an investment strategy involving securities."[117] Execution-only broker-dealers and other broker-dealers that do not provide such recommendations would not be required to include this sentence. We believe retail investors receiving recommendations that are subject to Regulation Best Interest would benefit from understanding the new obligation.

Second, all broker-dealers providing services to retail investors would state, "When we provide any service to you, we must treat you fairly and comply with a number of specific obligations." This would inform retail investors that broker-dealers have a duty of fair dealing under the federal securities laws and self-regulatory organization rules, as well as other

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on that exemption to receive compensation in connection with investment recommendations to state in writing that it is acting as a fiduciary under ERISA or the Code.

115 As noted above, if a prescribed statement is inapplicable to a firm's business or would be misleading to a reasonable retail investor, the firm may omit or modify that statement, as further discussed below. Proposed General Instruction 3 to Form CRS. *See supra* note 58.

116 Regulation Best Interest Proposal, *supra* note 24.

117 Proposed Item 3.B.1. of Form CRS. This wording assumes Commission adoption of Regulation Best Interest. As noted above (*see supra* note 29 and accompanying text), the proposed definition of "retail customer," to whom Regulation Best Interest would apply, differs from the proposed definition of "retail investor" under Form CRS. The relationship summary is intended for a broader range of investors than the intended focus of Regulation Best Interest. Accordingly, the proposed Regulation Best Interest standard may not apply to the recommendations of all retail investors receiving the relationship summary from broker-dealers. The Instructions for proposed Item 3.B.1 recognizes this possibility and seeks to ensure that broker-dealers provide accurate disclosure to their retail investors, even if the broker-dealer is not providing a recommendation subject to Regulation Best Interest.

obligations and standards to which they must adhere.[118]

Finally, broker-dealers would be required to state, "Unless we agree otherwise, we are not required to monitor your portfolio or investments on an ongoing basis." This sentence reflects that neither Regulation Best Interest nor existing broker-dealer standards oblige the broker-dealer to monitor the performance of retail investor's accounts,[119] while making clear that broker-dealers could agree to provide monitoring as an additional service. We are proposing this wording because we believe that the episodic, rather than ongoing, nature of broker-dealers' standard of conduct in Regulation Best Interest is a distinction from investment advisers' obligations to clients that retail investors should be aware of from the outset of a relationship.

After the description of the standard of conduct, broker-dealers would be required to state: "Our interests can conflict with your interests." If the broker-dealer provides to retail investors recommendations that are subject to Regulation Best Interest, it would also include the language, "When we provide recommendations, we must eliminate these conflicts or tell you

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118 *See* Report of the Special Study of Securities Markets of the Securities and Exchange Commission, H.R. Doc. No. 88-95, at 238 (1st Sess. 1963); In the Matters of Richard N. Cea, *et al.*, Exchange Act Release No. 8662 (Aug. 6, 1969), at 18 ("Release 8662") (involving excessive trading and recommendations of speculative securities without a reasonable basis); In the Matter of Mac Robbins & Co. Inc., Exchange Act Release No. 6846 (Jul. 11, 1962). *See also* FINRA Rule 2111.01 (Suitability) ("Implicit in all member and associated person relationships with customers and others is the fundamental responsibility for fair dealing. Sales efforts must therefore be undertaken only on a basis that can be judged as being within the ethical standards of [FINRA's] Rules, with particular emphasis on the requirement to deal fairly with the public. The suitability rule is fundamental to fair dealing and is intended to promote ethical sales practices and high standards of professional conduct"); *see also* FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade) (requiring a member, in the conduct of its business, to observe high standards of commercial honor and just and equitable principles of trade).

119 References to "monitoring" relate to monitoring the performance of a portfolio or investments, and are not intended to alter or diminish broker-dealers' current supervisory obligations under the Exchange Act and detailed self-regulatory organization rules, including the establishment of policies and procedures reasonably designed to prevent and detect violations of, and to achieve compliance with, the federal securities laws and regulations, as well as applicable self-regulatory rules. *See* section 15(b)(4)(E) of the Exchange Act; FINRA Rule 3110.

about them and in some cases reduce them."[120] These statements reflect proposed requirements in Regulation Best Interest that broker-dealer would need to establish, maintain, and enforce reasonably designed policies and procedures relating to material conflicts of interest, including those arising from financial incentives, associated with recommendations to retail customers. While we are not using the exact words of the proposed standard, we believe that this information, in combination with the conflicts section below, can make the retail investor aware that conflicts exist and that the broker-dealer has obligations regarding disclosure, mitigation, or elimination of conflicts when the broker-dealer is subject to Regulation Best Interest. We believe this could help prompt a conversation between retail investors and their financial professionals about both the conflicts the firm and financial professional have and what steps the firm takes to reduce the conflicts.[121]

Investment Advisers. We propose to require that investment advisers state the standard of conduct that applies to them as an investment adviser by including the following wording: "We are held to a fiduciary standard that covers our entire investment advisory relationship with you." In addition, unless the investment adviser does not provide ongoing advice (for example, provides only a one-time financial plan), the investment adviser would also state, "For example, we are required to monitor your portfolio, investment strategy and investments on an ongoing basis."[122] While we are not proposing to include a specific definition of fiduciary, we believe that the proposed wording that the relationship covers the "entire investment advisory relationship" and wording regarding the ongoing duty to monitor would provide retail investors

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120 Proposed Item 3.B.2. of Form CRS. This wording assumes Commission adoption of the Regulation Best Interest.

121 *See* discussion of the proposed conflicts of interest disclosure in the relationship summary, *infra* Section II.B.6.

122 Proposed Item 3.C.1. of Form CRS.

with information about aspects of the fiduciary duty that can help the retail investor understand the standard.[123] Additionally, as with the proposed standard of conduct disclosure for broker-dealers, we believe that the ongoing, as opposed to episodic, nature of investment advisers' standard of conduct is a distinction from broker-dealers' typical obligations when providing recommendations that retail investors should be aware of from the outset of a relationship.

After the description of the standard of conduct, investment advisers would then be required to state, "Our interests can conflict with your interests. We must eliminate these conflicts or tell you about them in a way you can understand, so that you can decide whether or not to agree to them." As with broker-dealers, we believe that this information, in combination with the conflicts section below, can make retail investors aware that conflicts exist and that investment advisers, as part of their fiduciary duty, have obligations regarding conflicts.[124] We believe this could help prompt a conversation between retail investors and their financial professionals about both the conflicts the firm and financial professional have and what steps the firm takes to reduce the conflicts.

We request comment generally on the proposed standard of conduct descriptions, and in particular on the following issues:

- Should we require, as proposed, that all firms include a brief prescribed statement about the legal standards of conduct that apply to them under the federal securities laws, including the new standard proposed in Regulation Best Interest and an investment adviser's fiduciary duty? Is such disclosure likely to be meaningful to

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123 We are concurrently publishing for comment a proposed interpretation of the standard of conduct for investment advisers under the Advisers Act. *See* Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation, Investment Advisers Act Release No. IA-4889 (Apr. 18, 2018) ("Fiduciary Duty Interpretive Release").

124 *See, e.g.*, General Instruction 3 to Form ADV, Part 2,

retail investors? Does the prescribed wording capture what retail investors should or want to understand about broker-dealers' and investment advisers' standards of conduct? Would the prescribed wording require any firm to provide any inaccurate information? Are there modifications to the proposed wording or alternative wording that would make the legal standards more clear in a succinct way? Should we require or permit additional information, and if so, what? Alternatively, would a briefer statement be appropriate? Are there any common misconceptions about broker-dealers' and investment advisers' standard of conduct that the relationship summary should specifically seek to clarify or correct?

- Should we require or permit broker-dealers to include additional detail about the best interest standard proposed in Regulation Best Interest or their duty of fair dealing? Would this or other disclosure provide retail investors with useful information? Should we provide flexibility in how broker-dealers describe the best interest standard or duty of fair dealing?
- We are proposing to require that broker-dealers state that they must comply with a number of specific obligations when providing any service to customers. Should we permit or require more detailed disclosure about these obligations? For example, should we permit or require broker-dealers to disclose their obligations to make sure that the prices a customer receives when a trade is executed are fair and reasonable, and to make sure that the commissions and fees the customer pays are not excessive?

- Should we require disclosure that further describes the investment adviser fiduciary standard, including any additional details described in the proposed interpretation? If so, what wording should we require? Should we provide flexibility in describing the fiduciary standard?
- For dual registrants, would the side-by-side descriptions of the standards of conduct for broker-dealers and investment advisers assist retail investors in understanding the differences between these standards? Are there modifications we can make to the wording or the presentation to facilitate this comparison?
- Should we permit or require firms to disclose additional information about the legal differences between broker-dealers and investment advisers, such as explaining that broker-dealers are subject to regulation by self-regulatory organizations in addition to the SEC? Should we permit or require firms to disclose the differences in licensing requirements for financial professionals of broker-dealers and investment advisers, such as the frequency of licensing or qualifications examinations? Would such disclosure about financial professionals fit within this section of the relationship summary that focuses on the firm? What information would be most relevant to retail investors?
- We understand that state laws and other regulations,[125] also may require broker-dealers and advisers to affirmatively acknowledge fiduciary status. Should we provide firms flexibility to include language in a relationship summary consistent with or to satisfy these other regulatory requirements? Would such flexibility enhance or potentially reduce the effectiveness of the relationship summary?

[125] *See. e.g., supra* note 114.

4. Summary of Fees and Costs

We are proposing to require broker-dealers and investment advisers to include an overview of specified types of fees and expenses that retail investors will pay in connection with their brokerage and investment advisory accounts. This section would include a description of the principal type of fees that the firm will charge retail investors as compensation for the firm's advisory or brokerage services, including whether the firm's fees vary and are negotiable, and the key factors that would help a reasonable retail investor understand the fees that he or she is likely to pay.[126] Investment advisers that provide advice to retail investors about investing in "wrap fee programs" would include an overview of the fees associated with those wrap fee programs.[127] Both broker-dealers and investment advisers would state that some investments impose fees that will reduce the value of a retail investor's investment over time, and would provide examples relevant to the firm's business.[128] In addition, each firm would include the incentives it and its financial professionals have to put their own interests ahead of their retail investors' interests based on the account fee structure,[129] and would state that depending on an investor's investment strategy, retail investors may prefer paying a different type of fee in certain

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126 Proposed Item 4 of Form CRS. A broker-dealer would describe transaction-based fees as its principal type of fee, using prescribed wording. *See* proposed Item 4.B.1 of Form CRS. We use the term "transaction-based fees" in the relationship summary for plain language purposes to refer generally to broker-dealer compensation such as commissions, mark-ups, mark-downs, sales loads or similar fees, including 12b-1 fees, tied to specific transactions. An investment adviser would summarize the principal fees and costs that align with the type of fee(s) the adviser reports in response to Item 5.E. of Form ADV Part 1A that are applicable to retail investors. *See* proposed Item 4.C. of Form CRS. Investment advisers and associated persons that receive compensation in connection with the purchase or sale of securities should carefully consider the applicability of the broker-dealer registration requirements of the Exchange Act.

127 Proposed Items 4.C.3., 4.C.7., 4.C.9. and 4.C.10. of Form CRS.

128 Proposed Items 4.B.2.b. and 4.C.4. of Form CRS.

129 Proposed Items 4.B.5. and 4.C.8. of Form CRS.

specified circumstances.[130] Having a clear, simple explanation of the fees a retail investor would pay firms for advisory accounts versus brokerage accounts, and the incentives that such fees create, would help the retail investor to understand the types of fees that they will pay and make a more informed choice about which account is right for them. As with other sections of the relationship summary, dual registrants would provide this information in tabular format to facilitate comparison.[131]

Fees and costs are important to retail investors,[132] but many retail investors are uncertain about the fees they will pay.[133] Many commenters have stressed the importance of clear fee disclosure to retail investors, including disclosure about differences between advisory and brokerage fees.[134] Accordingly, the proposed relationship summary is intended to provide investors greater clarity concerning certain categories of fees they should expect to pay, how the

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130 Proposed Items 4.B.6. and 4.C.10. of Form CRS. Dual registrants would make these disclosures under the heading "Fees and Costs," whereas standalone investment advisers and broker-dealers would make certain of these disclosures under the heading "Fees and Costs," and certain of these disclosures under the heading, as applicable "Compare with Brokerage Accounts" or "Compare with Advisory Accounts," as described below. Proposed Items 5.A.4. and 5.B.6. of Form CRS.

131 Proposed General Instruction 1.(e) to Form CRS.

132 *See* 917 Financial Literacy Study, *supra* note 20, at iv ("With respect to financial intermediaries, investors consider information about fees, disciplinary history, investment strategy, conflicts of interest to be absolutely essential.").

133 *See* Rand Study, *supra* note 5, at xix ("In fact, focus-group participants with investments acknowledged uncertainty about the fees they pay for their investments, and survey responses also indicate confusion about the fees."). In addition, we have brought enforcement actions against advisers providing inaccurate disclosure of all of the fees and costs that retail investors pay. *See, e.g.*, In the Matter of Robert W. Baird & Co. Inc., Investment Advisers Act Release No. 4526 (Sept. 8, 2016) (settled action) ("In re Robert W. Baird"); In the Matter of Raymond James & Associates, Inc., Investment Advisers Act Release No. 4525 (Sept. 8, 2016) (settled action) ("In re Raymond James"); In the Matter of Barclays Capital Inc., Investment Advisers Act Release No. 3929 (Sep. 23, 2014) (settled action) ("Release 3929").

134 *See*, *e.g.*, Kiley 2017 Letter (recommending that investors receive disclosures about the differences in advisory and brokerage fees, and brokers' specific fee and commission structure); Stifel 2017 Letter (recommending that firms explain the differences between brokerage and advisory accounts with the goal of improving understanding of a firm's different service models, compensation arrangements, and conflicts of interests); Equity Dealers of America 2017 Letter (recommending disclosure of aspects of advisory and brokerage accounts, including the type of fees charged, to facilitate investors' selection of an account type); Wells Fargo 2017 Letter; ACLI 2017 Letter; FSR 2017 Letter; SIFMA 2017 Letter; UBS 2017 Letter; Comment letter of the Investment Company Institute (Aug. 7, 2017) ("ICI 2017 Letter"); State Farm 2017 Letter; IAA 2017 Letter; Bernardi Securities 2017 Letter; Fidelity 2017 Letter; Vanguard 2017 Letter.

types of fees affect the incentives of the firm and their financial professionals, and certain other fees and expenses that will reduce the value of the retail investor's investment. The proposed relationship summary would focus on certain general types of fees, rather than describe all fees or provide a comprehensive schedule of fees. Specifically, the proposal would highlight certain differences in how broker-dealers and investment advisers charge for their services.

We are not proposing a requirement that firms personalize the fee disclosure for their retail customers, or provide a comprehensive fee schedule, as some commenters had proposed.[135] A personalized fee disclosure could be expensive and complex for firms to provide in a standardized presentation across all of their accounts and in a way that captures all fees, including embedded fees in various investments (which will vary for each investor depending on their portfolio). Many firms likely would seek to implement systems to automate the disclosure for each of their existing and prospective retail investors, and if such systems were expensive, some firms could choose to reduce the products and services that they offer as a result of the additional costs. Our proposal would encourage retail investors to ask financial professionals about their fees and request personalized information about the specific fees and expenses associated with their current or prospective accounts. As further discussed in Section II.B.8 below, one of the proposed questions for a retail investor to ask a financial professional is to "do the math for me," and specifically encourages retail investors to ask about the amount that they would pay per year for the account, what would make the fees more or less, and the services included in those fees.[136] Additionally, the beginning of the Fees and Costs section of the

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135 *See, e.g.*, Comment letter of Mark J. Flannery, BankAmerica Professor of Finance, University of Florida (Jul. 27, 2017) ("Flannery 2017 Letter"); Pefin 2017 Letter (recommending that clients should receive information on a quarterly basis on fees charged to their account, the calculation used to determine fees, and a breakdown of the charges by category).

136 *See infra* Section II.B.8.; *infra* notes 299 – 303 and accompanying text; proposed Item 8 of Form CRS.

relationship summary would state: "Please ask your financial professional to give you personalized information on fees and costs that you will pay."[137] We believe that financial professionals are well positioned to provide individualized fee information to their retail investors upon request. During the account opening process, for example, generally the relevant financial professional would have access to personalized information about the retail investor's account and can put together personalized fee information estimates during the process.

Likewise, we believe that requiring a comprehensive fee schedule in the relationship summary also could be more complex than a retail investor would find useful for an overview disclosure such as this. However, we believe our proposed layered disclosure would achieve similar results in a less costly and complex manner. The relationship summary would provide required information about fees, and a later section titled "Additional Information" would provide references and links to other disclosures where interested investors can find more detailed information.[138] As discussed below, investment advisers would be required to direct retail investors to additional information in the firm's Form ADV Part 2 brochure and any brochure supplement provided by a financial professional to the retail investor.[139] An adviser's Form ADV Part 2 contains more detailed information about the firm's fees. Broker-dealers would likewise be required to direct retail investors to additional information at BrokerCheck, the firm's website, and the retail investor's account agreement.[140] Up-to-date fee disclosures may

137 Proposed Item 4.A. of Form CRS.

138 Proposed Item 7 of Form CRS.

139 Proposed Item 7.E.2. of Form CRS. Investment advisers that do not have a public firm website or do not maintain their current Form ADV brochure on its public website would be required to include a link to adviserinfo.sec.gov. Advisers that do not have a public firm website would also be required to include a toll-free telephone number where retail investors can request up-to-date information.

140 Proposed Item 7.E.1. of Form CRS. Broker-dealers that do not have a public firm website would be required to include a toll-free telephone number where retail investors can request up-to-date information.

appear on broker-dealers' websites or in the retail investors' account agreements, if applicable, where we understand broker-dealers typically provide information about fees, including, in some cases, comprehensive fee schedules.[141]

We are also not proposing to require firms to include examples of how fees could affect a retail investor's investment returns. We recognize that the Commission has required firms to disclose examples showing the effects of fees and other costs in certain contexts. For example, we have required mutual funds to provide in their summary prospectuses an example that is intended to help investors compare the cost of investing in the mutual fund with the cost of investing in other mutual funds.[142] While we continue to believe that examples of the effect of fees on returns could be helpful to retail investors, they could also fail to capture the effect of a firm's fees on a particular retail investor's account. Transactional fees, in particular, can vary widely based on a number of circumstances, and it could be potentially misleading to present a typical example showing how sample transaction fees apply to a sample account over time. We believe requiring firms to provide an example for each type of account that would show the effect of fees on a sample account could overwhelm investors due to the number and variability of assumptions that would need to incorporated, explained, and understood in order for the example to be meaningful, and would not necessarily promote comparability. If the assumptions were standardized, such examples might not be useful, or might even be potentially misleading, to the retail investor, whose circumstances may be different from the assumptions used.

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141 Under Regulation Best Interest, broker-dealers would also be required to disclose the material facts relating to the scope and terms of the relationship, which would include disclosure of fees and charges that apply to a customer's transactions, holdings and accounts. Regulation Best Interest Proposal, *supra* note 24, at section II.D.1.a.

142 *See* Item 3 of Mutual Fund Summary Prospectus; Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47, at section III.A.3.b ("The fee table and example are designed to help investors understand the costs of investing in a fund and compare those costs with the costs of other funds.").

Some commenters suggested requiring that a firm disclose the types of compensation firms and their financial professionals receive, including from third parties, in connection with providing investment recommendations.[143] A few commenters suggested requiring disclosure of how much the firm and its financial professionals receive in fees, including commissions and fees from third parties.[144] We agree with commenters that it is important to make investors aware of such fees and compensation because they create conflicts of interest for firms and financial professionals making investment recommendations for retail investors. We are proposing to require that firms disclose commissions and certain third-party fees related to mutual funds in this section, and certain compensation-related conflicts (*e.g.*, conflicts related to revenue sharing) in the conflicts section of the relationship summary, as discussed in Section II.B.6 below.

Heading. To emphasize the importance of fees, all firms would be required to include the following statement at the beginning of this section under the heading "Fees and Costs": "Fees and costs affect the value of your account over time. Please ask your financial professional to give you personalized information on the fees and costs that you will pay."[145] We are proposing this precise wording because we believe it is applicable to retail investors regardless of any differences among the accounts and their fees. Understanding that fees and costs affect investment value over time would help retail investors to understand why they should review and understand this information. This introductory language also would highlight

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143 *See, e.g.*, SIFMA 2017 Letter; UBS 2017 Letter; ICI 2017 Letter; State Farm 2017 Letter; Bernardi Securities 2017 Letter; Fidelity 2017 Letter.

144 *See, e.g.*, Flannery 2017 Letter; Pefin 2017 Letter.

145 Proposed Item 4.A. of Form CRS.

that retail investors could get more personalized information from the firm's financial professionals.

Brokerage Account Fees and Costs. Broker-dealers would be required to summarize the principal fees and costs that retail investors will incur.[146] First, we are proposing prescribed language that describes the transactional nature of many brokerage fees.[147] We are proposing different wording for dual registrants than for standalone broker-dealers to facilitate the side-by-side comparison with the description of the advisory fee in the dual registrant's relationship summary. Specifically, dual registrants that offer retail investors both investment advisory accounts and brokerage accounts would include the following wording to assist with the side-by-side comparison with investment advisers: "*Transaction-based fees*. You will pay us a fee every time you buy or sell an investment. This fee, commonly referred to as a commission, is based on the specific transaction and not the value of your account."[148] A standalone broker-dealer would include the following: "The fee you pay is based on the specific transaction and not the value of your account."[149]

In addition, both standalone and dual registrant broker-dealers would include the following (emphasis required): "With stocks or exchange-traded funds, this fee is usually a separate commission. With other investments, such as bonds, this fee might be part of the price you pay for the investment (called a "***mark-up***" or "***mark down***"). With mutual funds, this fee

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146 Proposed Item 4.B. of Form CRS.

147 As discussed above, we use the term "transaction-based fees" to refer to broker-dealer compensation such as commissions, mark-ups, mark-downs, sales loads or similar fees, including 12b-1 fees, tied to specific transactions. *See supra* note126.

148 Proposed Item 4.B.1. of Form CRS. As discussed further below, dual registrants would include a parallel statement regarding their investment advisory account fees. Proposed Item 4.C.1. of Form CRS.

149 Proposed Item 4.B.1. of Form CRS. As discussed above, standalone broker-dealers would be required to include wording that a transaction-based fee is generally referred to as a commission in the Relationships and Services section of the relationship summary. *See* proposed Item 2.B.1. of Form CRS.

(typically called a "***load***") reduces the value of your investment."[150] Because of the importance of these transaction-based fees to brokerage services, as well as the variety of forms that such fees can take, we believe it will benefit investors to have specific examples to illustrate transaction-based fees with standardized, concise wording. We are proposing to require the example of mutual fund loads because they are common indirect fees associated with investments that compensate the broker-dealer.

We are not proposing to require broker-dealers to provide the range of their transaction-based fees. We understand that these fees vary widely based on the specific circumstances of a transaction. For example, a broker-dealer that transacts in only one type of security – such as equities – can have a wide range of transaction fees for such securities, depending on factors such as the size of the transaction, the type of investment purchased, the type of account and services provided, and how retail investors place their orders (for example, online, telephone or with the assistance of a financial professional). A broker-dealer that transacts in multiple types of securities – for example, equities and real estate investment trusts (REITs) – could have an even wider range of transaction fees. Given this variability, and our intent that the relationship summary be short and that it be provided in addition to, and not in lieu of, other disclosure, we believe that requiring firms to provide a range of transaction-based fees in the relationship summary could be confusing or provide limited benefit to retail investors.

Following the examples of transaction-based fees, broker-dealers would be required to state that some investments impose additional fees that will reduce the value of retail investors' investments over time, and provide examples of such investments that they offer to retail

[150] Proposed Item 4.B.2.a. of Form CRS.

investors.[151] Mutual funds, variable annuities and exchange-traded funds are common examples, as well as any other investment that incurs fund management, 12b-1, custodial or transfer agent fees, or any other fees and expenses that reduce the value of the investment over time.[152] Broker-dealers also would be required to state that a retail investor could be required to pay fees when certain investments are sold, for example, surrender charges for selling variable annuities.[153] We believe that it is important to highlight for investors the costs associated with particular investments in addition to describing the transaction-based fee for brokerage services. Retail investors may not appreciate that they will bear costs for some investments in addition to the transaction-based brokerage fee they pay to their financial professional or firm.[154] In addition, the investment fees and expenses we are proposing to require that firms disclose are ones that we believe are among the most common and can have a substantial impact on an investor's return from a particular investment.

Requiring the disclosure of these investment fees and expenses, sometimes described as "indirect fees," follows commenters' recommendations that investment advisers and broker-

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151 Proposed Item 4.B.2.b. of Form CRS. Investment advisers would also be required to make this disclosure. *See* proposed Item 4.C.4. of Form CRS.

152 We acknowledge that some fees, such as 12b-1 fees, could be a broker-dealer's principal fee for their brokerage services and are also fees that reduce the return on an investment. In such a case, the broker-dealer would describe transaction-based fees as its principal fees and costs pursuant to proposed Item 4.B.1, and would also describe these fees as additional fees that will reduce the return on an investor's investments pursuant to proposed Item 4.B.2.b. of Form CRS.

153 Proposed Item 4.B.2.b. of Form CRS. Investment advisers would also be required to make this disclosure. *See* proposed Item 4.C.4. of Form CRS.

154 *See*, *e.g.*, Enhanced Disclosure and New Prospectus Delivery Option For Registered Open-End Management Investment Companies, Investment Company Act Release No. 28064 (Nov. 21, 2007) [72 FR 67790 (Nov. 30, 2007)], at n.49 and accompanying text ("In recent years, we have taken significant steps to address concerns that investors do not understand that they pay ongoing costs every year when they invest in mutual funds, including requiring disclosure of ongoing costs in shareholder reports.").

dealers disclose certain indirect costs to retail investors.[155] We are not proposing a requirement that firms disclose the amount or range of mutual fund fees or other third-party fees that retail investors may pay related to their underlying investments, as a few commenters recommended.[156] These expenses vary so greatly that attempts to quantify them or describe their range likely would not be useful to retail investors or would provide limited benefit to retail investors given that the relationship summary is designed to be short disclosure provided in addition to, and not in lieu of, other disclosures.[157] Instead, we intend that our proposed summary disclosure would effectively highlight these costs in a simple, understandable way.

Additionally, broker-dealers would be required to state whether or not the fees they charge retail investors for their brokerage accounts vary and are negotiable, including a description of the key factors that they believe would help a reasonable retail investor understand the fee that he or she is likely to pay for the firm's services.[158] Such factors could include, for example, how much the retail investor buys or sells, what type of investment the retail investor buys or sells, and what kind of account the retail investor has with the broker-dealer. We believe investors would benefit from knowing at account opening whether they have the ability to negotiate the fees they pay.

Broker-dealers would next be required to state, if applicable, that a retail investor will also pay other fees in addition to the firm's transaction-based fee, and to list those fees, including

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155 *See, e.g.*, State Farm 2017 Letter; Bernardi Securities 2017 Letter; Pefin 2017 Letter; Flannery 2017 Letter; Comment letter of Dan Keppel (Jun. 5, 2017); Comment letter of Edward H. Weyler (Jun. 8, 2017).

156 *See* Flannery 2017 Letter; Pefin 2017 Letter.

157 *See* Amendments to Form ADV, Investment Advisers Act Release No. 3060 (Jul. 28, 2010) [75 FR 49233 (Aug. 12, 2010)] ("Brochure Adopting Release"); Amendments to Form ADV, Investment Advisers Act Release No. 2711 (Mar. 3, 2008) [73 FR 13958 (Mar. 14, 2008)] ("2008 Brochure Proposing Release").

158 Proposed Item 4.B.3. of Form CRS.

account maintenance fees, account inactivity fees, and custodian fees.[159] We believe that it is important to highlight for investors the fees associated with an account that they will pay in addition to the principal type of fee that the firm charges retail investors for their brokerage account because these fees are common and they can have an impact on a retail investor's return.

Broker-dealers would then be required to disclose certain specified incentives they have to put their own interests ahead of retail investors' interests based on charging transaction-based fees for brokerage accounts.[160] They would be required to include the following: "The more transactions in your account, the more fees we charge you. We therefore have an incentive to encourage you to engage in transactions."[161] We believe this information would help retail investors understand how the fee structures for brokerage accounts could affect their investments and the incentives that firms and financial professionals have to place their interests ahead of retail investors' interests by encouraging retail investors to engage in transactions to increase their fees.[162] We are proposing to prescribe wording because we believe these particular incentives and considerations generally apply to most brokers that offer retail investors brokerage accounts, and using uniform wording would promote consistency. We believe that retail investors would benefit from understanding these incentives when they are considering

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159 Proposed Item 4.B.4. of Form CRS.

160 Proposed Item 4.B.5. of Form CRS.

161 *Id.*

162 Pursuant to the federal securities laws, broker-dealers can violate the federal antifraud provisions by engaging in excessive trading that amounts to churning, switching, or unsuitable recommendations. Churning occurs when a broker-dealer, exercising control over the volume and frequency of trading in a customer account, abuses the customer's confidence for personal gain by initiating transactions that are excessive in view of the character of the account and the customer's investment objectives. Excessive trading is an excessive level of trading unjustified in light of the customer's investment objectives. *See Mihara v. Dean Witter & Co., Inc.*, 619 F.2d 814, 821 (9th Cir. 1980); *Carras v. Burns*, 516 F.2d 251, 258 (4th Cir. 1975). *See also* Regulation Best Interest Proposal, *supra* note 24, at section II.D.2.c.

broker-dealers. Additionally, we believe this disclosure would reinforce a key theme of the relationship summary, which is choice across account types and services.

Finally, dual registrants would be required to include the following with respect to brokerage services: "From a cost perspective, you may prefer a transaction-based fee if you do not trade often or if you plan to buy and hold investments for longer periods of time."[163] We believe that these factors – cost, trading frequency, and the desire to "buy and hold" – are important for retail investors to consider when determining whether to use brokerage services or advisory services.[164] We are proposing to prescribe the wording because we believe these factors reflect common circumstances in which a brokerage account could be more cost-effective for a retail investor than an advisory account, and using uniform wording would promote consistency. We believe this disclosure, in conjunction with the corresponding disclosure regarding advisory accounts that would appear next to it, would help retail investors to compare the two services and make an informed choice about the account type that is the right fit for them based on their goals and preferences.

Investment Advisory Account Fees and Costs. Investment advisers that offer advisory accounts to retail investors would be required to summarize the principal fees and costs that retail investors will incur.[165] Dual registrants that charge ongoing asset-based fees for their

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163 Proposed Item 4.B.6. of Form CRS.

164 *See e.g.*, Comment letter of The Capital Group Companies, Inc. (Mar. 12, 2018) (discussing considerations for buy and hold investors choosing among commission-based and fee-based arrangements). Standalone broker-dealers and standalone investment advisers would also be required to include similar wording under the headings "Compare with Typical Advisory Accounts" and "Compare with Typical Brokerage Accounts," as applicable. *See* proposed Items 5.B.5 and 5.A.4 of Form CRS. Dual-registrants, standalone broker-dealers, and standalone investment advisers would also be required to include a statement that retail investors may prefer an asset-based fee in certain circumstances, and that an asset-based fee may cost more than a transaction-based fee. *See* proposed Items 4.C.10, 5.B.5 and 5.A.4 of Form CRS.

165 Proposed Item 4.C. of Form CRS. An investment adviser would summarize the principal fees and costs that align with the type of fee(s) the adviser reports in response to Item 5.E. of Form ADV Part 1A that are applicable to retail investors.

advisory services would state the following: "*Asset-based fees*. You will pay an on-going fee [at the end of each quarter] based on the value of the cash and investments in your advisory account."[166] replacing, as needed, the bracketed wording with how often they assess the fee. If the dual registrant charges another type of fee for advisory services, it would briefly describe that fee and how often it is assessed.[167] Standalone investment advisers would state the following: "The amount paid to our firm and your financial professional generally does not vary based on the type of investments we select on your behalf."[168] Standalone investment advisers that charge an ongoing asset-based fee would also state "The asset-based fee reduces the value of your account and will be deducted from your account."[169] Standalone investment advisers that charge another type of fee would succinctly describe how the fee is assessed and the impact it has on the value of the retail investor's account.[170]

These requirements are consistent with the current fee disclosure requirements for the Form ADV brochure and how investment advisers typically describe asset-based fees, and we

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166 Proposed Item 4.C.1. of Form CRS.

167 *Id*. Some investment advisers report on Form ADV Item 5.E that they receive "commissions." These "commissions" may include deferred sales loads, including fees for marketing and service, as well as commissions as understood in the broker-dealer context. As a form of deferred sales load, all payments of ongoing sales charges to intermediaries would constitute transaction-based compensation. Intermediaries receiving those payments should consider whether they need to register as broker-dealers under section 15 of the Exchange Act.

168 Proposed Item 4.C.2. of Form CRS. We recognize that, in some cases, the amount paid to the advisory firm and the financial professional can vary based on the type of investment selected (*e.g.*, advisory firms and financial professionals may recommend certain mutual funds that pay the adviser or the financial professional 12b-1 fees out of fund assets).

169 *Id*.

170 Proposed Item 4.C.2. of Form CRS. Investment advisers that offer retail investors advisory accounts sometimes charge fees that are not ongoing, asset based fees. A financial planner, for example, sometimes charges a one-time fixed fee to prepare a plan.

believe that retail investors would find this type of disclosure helpful.[171] We are not proposing to require that investment advisers provide the range of fees, as ranges an investment adviser charges can vary based on a number of factors individual to the retail investor and the services they choose. Additionally, although we do not believe that ranges for investment advisers' asset based fees vary as much as broker-dealers' transaction-based fees, we recognize that requiring firms to provide a fee range for advisory accounts and not brokerage accounts could cause confusion among retail investors and be of limited benefit when comparing advisory and brokerage services. However, we recognize that providing such a range could promote comparability between different advisers, and we request comment below on whether we should require disclosure of the adviser's range of principal fees charged.

An investment adviser that provides advice to retail investors about investing in a wrap fee program would be required to include specified language about the program fees.[172] A "wrap fee program" would be defined as an advisory program that charges a specified fee not based directly upon transactions in the account for investment advisory services and the execution of transactions.[173] The advisory services may include portfolio management or advice concerning selection of other advisers.[174] An investment adviser that provides advice to retail investors about investing in a wrap fee program and does not also offer another type of advisory account would be required to include the following (emphasis required): "We offer advisory account

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171 As discussed above, when completing Form CRS, investment advisers should generally consider achieving consistency with the type(s) of fee(s) that the investment adviser reports on Item 5.E. of Form ADV Part 1A. *See supra* note 126.

172 Proposed Items 4.C.3., 4.C.6., 4.C.9. and 4.C.10. of Form CRS. We also refer to these types of investment advisers as "client-facing firms."

173 Proposed General Instruction 9.(g) to Form CRS. This proposed definition is identical to the definition already used in Form ADV.

174 Proposed General Instruction 9.(g) to Form CRS.

programs called ***wrap fee programs***. In a ***wrap fee program***, the asset-based fee will include most transaction costs and fees to a broker-dealer or bank that will hold your assets (known as "***custody***"), and as a result wrap fees are typically higher than non-wrap advisory fees."[175] An investment adviser that provides advice about investing in a wrap fee program and offers another type of advisory account would be required to include similar prescribed wording, modified as applicable to reflect that the adviser also offers other types of advisory accounts.[176]

Many retail investors participate in wrap fee programs.[177] We believe that retail investors would benefit from receiving information about certain characteristics of wrap fee programs, particularly with respect to their fees. Requiring investment advisers to describe the asset-based fee, what it includes, and that it is typically higher than non-wrap advisory fees would help a retail investor to distinguish wrap fee programs from other types of advisory accounts that charge or incur separate transaction fees.

Next, investment advisers would be required to state that some investments impose additional fees that will reduce the value of a retail investor's investment over time, and provide examples of such investments that the firm offers to retail investors.[178] Investment advisers also

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175 Proposed Item 4.C.3. of Form CRS. The asset-based fee in a wrap program does not always include all transaction costs. For example, in some cases retail investors pay mark-ups, mark-downs, or spreads, and mutual fund fees and expenses in addition to the wrap fee program's asset-based fee. In addition, as discussed below, an investment adviser may select a broker-dealer outside of the wrap fee program to execute certain trades in a retail investor's account—a practice sometimes referred to as "trading away"—that results in the retail investor's account incurring separate brokerage fees. *See infra* note 187 and accompanying text.

176 Such investment advisers would be required to include the following (emphasis required): "For some advisory accounts, known as ***wrap fee programs***, the asset-based fee will include most transaction costs and custody services, and as a result wrap fees are typically higher than non-wrap advisory fees." Proposed Item 4.C.3. of Form CRS.

177 Based on IARD data as of December 31, 2017, of the 12,667 SEC-registered investment advisers, 1,035 (8.17%) sponsor a wrap fee program, and 1,597 (12.61%) act as a portfolio manager for one or more wrap fee programs.

178 Proposed Item 4.C.4 of Form CRS. *See supra* notes 151 – 155 and accompanying text for a discussion of this requirement applicable to both investment advisers and broker-dealers.

would state that a retail investor could be required to pay fees when certain investments are sold, for example, surrender charges for selling variable annuities.[179] These proposed requirements are identical to the disclosure that broker-dealers would provide.[180]

In addition, investment advisers would be required to state whether or not the fees they charge retail investors for their advisory accounts vary and are negotiable.[181] They would be required to describe the key factors that they believe would help a reasonable retail investor understand the fee that he or she is likely to pay for the firm's services.[182] Such factors could include, for example, the services the retail investor receives and the amount of assets in the account. As discussed above with regard to broker-dealers, we believe investors would benefit from knowing at account opening whether they have the ability to negotiate the fees they pay.

Investment advisers would next be required to state, if applicable, that a retail investor will pay transaction-based fees when the firm buys and sells an investment for the retail investor (*e.g.*, commissions paid to broker-dealers for buying or selling investments) in addition to the firm's principal fee it charges retail investors for the firm's advisory accounts.[183] Investment advisers would also be required to state, if applicable, that a retail investor will pay fees to a broker-dealer or bank that will hold the retail investor's assets and that this is called "custody," and would be required to list other fees the retail investor will pay.[184] Examples could include fees for account maintenance services. These other fees we are proposing to require firms to disclose are ones that we believe are among the most common or can have an impact on a retail

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179 Proposed Item 4.C.4. of Form CRS.

180 *See* proposed Item 4.B.2.b. of Form CRS.

181 Proposed Item 4.C.5. of Form CRS.

182 *Id.*

183 Proposed Item 4.C.6. of Form CRS.

184 *Id.*

investor's return.[185] As discussed above, we believe that investors would benefit from being aware of the fees associated with an account that they will pay in addition to the principal fee that the firm charges retail investors for their brokerage or advisory account.

An investment adviser that provides advice to retail investors about investing in a wrap fee program also would be required to state: "Although transaction fees are usually included in the wrap program fee, sometimes you will pay an additional transaction fee (for investments bought and sold outside the wrap fee program)."[186] The Commission is aware that wrap fee program portfolio managers employ, to varying degrees, "trading away" practices, in which they use a broker other than the sponsoring broker to execute trades for which a commission or other transaction-based fee is charged, in addition to the wrap fee, to the retail investor.[187] The Commission has identified instances in which firms participating in wrap fee programs had poor disclosure about the overall cost of selecting a wrap fee program, including the effect of their trade away practices.[188] We believe that investors would benefit from the relationship summary highlighting that, even in a wrap fee program, they sometimes will pay an additional transaction fee.

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185 *See, e.g.*, Advisers Act rule 204-3; Item 5 of Form ADV Part 2A (requiring each adviser to describe the types of other costs, such as brokerage, custody fees and fund expenses that clients may pay in connection with the advisory services provided to them by the adviser).

186 Proposed Item 4.C.7. of Form CRS.

187 A wrap fee program portfolio manager may trade away because, for example, it believes that doing so will allow it to seek best execution of clients' transactions, as investment advisers have an obligation to seek best execution of clients' securities transactions where they have the responsibility to select broker-dealers to execute client trades (typically in the case of discretionary accounts). *See* Advisers Act rule 206(3)-2(c) (referring to adviser's duty of best execution of client transactions). *See also* Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934, Exchange Act Release No. 54165 (Jul. 18, 2006) (stating that investment advisers have "best execution obligations") ("Release 54165"). *See also* Brochure Adopting Release at 9.

188 The Commission has brought enforcement actions in these circumstances. *See, e.g.*, In re Robert W. Baird, *supra* note 133; In re Raymond James, *supra* note 133; In the Matter of Riverfront Investment Group, LLC, Investment Advisers Act Release No. 4453 (Jul. 14, 2016) (settled action); In the Matter of Stifel, Nicolaus & Company, Inc., Investment Advisers Act Release No. 4665 (Mar. 13, 2017) (settled action).

As with broker-dealers, investment advisers that charge an ongoing asset-based fee for advisory services would next be required to address the incentives they have to put their own interests ahead of their retail investors' interests based on the type of fee charged for investment advisory services.[189] These advisers would be required to include the following statement: "The more assets you have in the advisory account, including cash, the more you will pay us. We therefore have an incentive to increase the assets in your account in order to increase our fees. You pay our fee [insert frequency of fee (*e.g.*, quarterly)] even if you do not buy or sell," replacing the brackets with the frequency of their fee.[190] Investment advisers that provide advice to retail investors about participating in a wrap fee program would, in addition, be required to include the following: "Paying for a wrap fee program could cost more than separately paying for advice and for transactions if there are infrequent trades in your account."[191] We are proposing to require prescribed wording to promote consistency and because we believe these particular incentives and considerations generally apply to all advisers that charge retail investors ongoing asset-based fees or provide advice about participating in a wrap fee program. While we are not proposing any prescribed language for other fee types, such as fixed fees, we request comment, below, on whether advisers that charge other types of fees for their advisory services have incentives to act in their own interest based on the type of fee charged, and whether we should require disclosure of such incentives.

These disclosures would help retail investors understand how the fee structures for advisory accounts could affect their investments and the incentives that firms and financial professionals have to place their interests ahead of retail investors' interests. The disclosures for

189 Proposed Item 4.C.8. of Form CRS.

190 Proposed Item 4.C.8. of Form CRS.

191 Proposed Item 4.C.9. of Form CRS.

investment advisers that provide advice about investing in a wrap fee program also would help retail investors to understand that in certain circumstances a wrap fee would cost them more than separately paying for advice and for transactions in a different type of advisory account. Similarly, wrap fee sponsors that complete the Form ADV Wrap Fee Program Brochure are required to explain that the wrap fee program may cost the client more or less than purchasing such services separately and describe the factors that bear upon the relative cost of the program, such as the cost of the services if provided separately and the trading activity in the client's account.[192] As with some of the proposed requirements described above, we are proposing to prescribe wording because we believe these particular considerations generally apply to any investment in a wrap fee program and would promote consistency. Also, as discussed above, we believe this disclosure would reinforce a key theme of the relationship summary, which is choice across account types and services.

Finally, dual registrants that charge ongoing asset-based fees for advisory accounts would be required to include the following with respect to their investment advisory services: "An asset-based fee may cost more than a transaction-based fee, but you may prefer an asset-based fee if you want continuing advice or want someone to make investment decisions for you."[193] Dual registrants that provide advice to retail investors about investing in wrap fee programs would also be required to include the following with respect to wrap fee program accounts: "You may prefer a wrap fee program if you prefer the certainty of a [insert frequency of the wrap fee

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192 *See* Item 4.B. of Form ADV Part 2A; Appendix 1 of Form ADV: *Wrap Fee Program Brochure*.

193 Proposed Item 4.C.10. of Form CRS. Standalone investment advisers and standalone broker-dealers would also be required to include similar wording under the headings "Compare with Typical Brokerage Based Accounts," and "Compare with Typical Advisory Accounts," as applicable. Proposed Items 5.A.4 and 5.B.5. of Form CRS.

(*e.g.*, quarterly)] fee regardless of the number of transactions you have."[194] We believe that these features – ongoing advice, discretion, standards of conduct, and, for wrap fee programs, certainty in pricing – distinguish advisory accounts and wrap fee programs from brokerage accounts. We also believe it is important to highlight how costs relate to the services included.[195] We are proposing to prescribe wording because we believe these particular considerations generally apply to all advisory accounts and wrap fee programs, and using uniform wording would promote consistency. We believe these disclosures, in conjunction with the corresponding disclosure regarding broker-dealer accounts that would appear next to it for dual registrants, would help retail investors to compare the two types of services and combinations of those services and make an informed choice about the account type that is the right fit for them based on their goals and preferences.

We request comment generally on the proposed fees and costs disclosures, and in particular on the following issues:

- Is the proposed disclosure discussing fees and expenses useful to investors?
- Do the proposed requirements encourage disclosure that is simple, clear and useful to retail investors? Would the proposed disclosure help investors to understand and compare the fees and costs associated with a firm's advisory services and brokerage services? Are there any revisions to the descriptions of fees that would make the proposed disclosure more useful to investors? Is it clear

194 Proposed Item 4.C.10. of Form CRS.

195 We also propose to require dual registrants to include the following with respect to broker-dealer services: "From a cost perspective, you may prefer a transaction-based fee if you do not trade often or if you plan to buy and hold investments for longer periods of time." *See* proposed Items 4.B.6. *See also* Items 5.A.4. and 5.B.5 of Form CRS (including similar disclosures to be made by standalone investment advisers and broker-dealers).

that retail investors would incur different costs for different types of accounts and advice services? Are there common assumptions or misconceptions regarding account fees and services that firms should be required to discuss, clarify, or address?

- Is the proposed order of the information appropriate, or should it be modified? If so, how should it be modified?
- Do the proposed requirements strike the right balance between requiring specific wording and allowing firms to draft their own responses? Why or why not? Should the Commission permit or require a more open-ended narrative or require more prescribed wording? Do the proposed Instructions cover the range of business models and fee structures that investment advisers and broker-dealers offer fully and accurately? Are there other fees that should be required to be disclosed for broker-dealers or investment advisers?
- Is the proposed format useful for retail investors to understand and compare fees and costs as between broker-dealers and investment advisers? Should we require further use of bullet points, tables, charts, graphs or other illustrative format? Should we require, as proposed, that dual registrants present the fee and cost information in a tabular format, comparing advisory services and brokerage services side-by-side, or permit other formats such as in a bulleted format?
- How would the required disclosures contribute to readability and length of the proposed relationship summary? Should each of these disclosures be required? Should any of these disclosures not be required but instead permitted? Should

any of these disclosures be required to appear in the relationship summary, but outside the proposed summary of fees and costs?

- Should any additional disclosures about fees and costs be included for investment advisers? In particular, should we require any disclosures from an investment adviser's Form ADV Part 2A narrative brochure, such as more details about an investment adviser's fees? Some other disclosures about fees that are included in Form ADV Part 2A, but that we have not included in the proposed relationship summary, include an adviser's fee schedule; whether the adviser bills clients or deducts fees directly from clients' accounts; and an explanation of how an adviser calculates and refunds prepaid fees when a client contract terminates (for an adviser charging fees in advance). Should we require some or all of such disclosures, or other disclosures about fees?
- Should we require or permit advisers to disclose whether they charge performance-based fees, which is a type of compensation investment advisers may charge to "qualified clients," that is based on a share of capital gains on, or capital appreciation of, such clients' assets?[196] Advisers are required to disclose their receipt of performance-based fees on Form ADV, and they provide an incentive for the adviser to take additional investment risks with the account.
- Should we permit or require each firm to provide the range of its fees? If so, should broker-dealers be required to include a range for each type of transaction-based fee it charges or the aggregate range for all of the firm's transaction-based fees? Should investment advisers be required to include a range for each type of

196 *See* Advisers Act rule 205-3.

principal fee they charge retail investors for advisory services, or the aggregate range for all of its principal advisory fees? Do broker-dealers and investment advisers currently compute or have the ability to compute such aggregated fee information? What factors determine the type or amount of fee that firms charge (*e.g.*, for broker-dealers, such factors could include the: means of placing an order, such as online, by telephone or in person; type of account, such as full-service or discount brokerage, and; type of product)? Do commenters have suggestions for how best to convey one or more ranges in a space-limited disclosure in light of the different fee structures? Are there other ways to give retail investors a better sense of the amount of fees they will pay without providing account-specific disclosures?

- Should we require firms to state whether their fees are "negotiable," as we have proposed? At firms that offer negotiable fees, are retail investors generally able to negotiate their fees, and if not, would they find this disclosure helpful or could it be confusing? Will firms be able to succinctly describe the key factors they believe would help a reasonable retail investor understand the fee that he or she is likely to pay for a firm's services (*e.g.*, the size of the transaction, the type of investment purchased, and the type of account and services he or she receives)?
- Will any of the required disclosures be misleading or make it more difficult for investors to select the right type of account for them?
- Should we make the proposed relationship summary more personalized to individual retail investors, such as by requiring or permitting estimates for each retail investor, reflecting the fees and charges incurred for the retail investor's

brokerage or advisory account? Is personalization feasible for this type of relationship summary disclosure? If so, what information should be included in the personalized fees and cost disclosure, and how should such information be presented? How would firms calculate those estimates? How often should we require firms to update the personalized fees and compensation disclosure, and how should the personalized fee disclosure updates be delivered or made available to retail investors? What would be the costs to firms to prepare and update personalized fee and compensation disclosures?

- Should we require firms to provide investors with personalized fee information in a different disclosure, such as an account statement? What would be the cost and benefits, including the costs of books and records requirements, of personalizing information to investors relative to the proposal? Do firms currently provide retail investors with personalized fee disclosure estimates at or before account opening? Do they provide personalized fee disclosures in periodic account statements? For firms that provide personalized fee disclosures, do they include all fees paid by the retail investor as well as compensation received by the firm and financial professionals, even if such compensation is not paid directly or indirectly by the retail investor, such as commissions, mark-ups, mark-downs, other fees embedded in the investment or fees from third parties? What other types of fee information do firms include? Do they automate such disclosures? How expensive and complex a process is creating and delivering such personalized fee disclosures?

- Should we require firms to state where retail investors can find personalized information about account fees and costs, such as on account statements and trade confirmations? What other source of such information might be available for prospective customers and clients? Should we require firms to include hyperlinks to fee and cost calculators on investor.gov?
- Should we require firms to provide an example showing how sample fees and charges apply to a hypothetical advisory account and a hypothetical brokerage account, as applicable? Should we require a more general example that shows the impact of hypothetical fees on an account? If so, what assumptions should we require firms to make in preparing such an example? For example, should we specify assumptions such as the kinds of assets that are most typical for a broker-dealer's customers, stated commission schedules, and aggregate third-party compensation? If the assumptions were standardized, would such examples be useful to the retail investor, whose circumstances may be different from the assumptions used or would they help give an investor a better idea about what kind of fees are being charged? Would such examples provide retail investors with a clear understanding of the application of ongoing asset-based, transaction-based and product-level fees to an account? Should we require one example for an advisory account and one example for a brokerage account? How should the information be presented *(e.g.*, mandated graphical presentation)? Should we require firms to present more than one hypothetical example showing a range of fees instead (*e.g.*, based on representative holdings or recommendations)? Should specific assumptions be included in calculating the hypothetical example? What

disclosures would need to accompany the example? Should the example(s) track the effect of the fees over time, and if so, over what time period (*e.g.*, over one, five and 10 years)? Or should firms describe the impact of different amounts or types of fees over a longer period of time, such as 20 years?

- Should firms be permitted or required to include in the relationship summary a detailed fee table or schedule? Should we permit or require firms to create a fee schedule as separate disclosure, and then include it as an attachment (or cross reference it with a website address and hyperlink) to the relationship summary? What should be included in such a fee table or schedule? Should it include compensation received by the firm and financial professionals, even if such compensation is not paid directly or indirectly by the retail investor, such as commissions or fees from third parties?
- Regarding fees related to funds and other investments that reduce the value of the investment over time, would the required disclosures by investment advisers and broker-dealers be clear and understandable to retail investors? Should we, as proposed, permit firms to select their own example that they offer to retail investors? Are there other considerations related to fees for funds and other investments that we should require firms to highlight for retail investors? Would our proposed requirement that firms disclose the existence of such fees, along with examples of investments that impose such fees, adequately inform retail investors of these costs? Should we require an example showing how investment fees and expenses and other account fees and expenses may affect a retail investor's investment over time? Should we require a reference to such an

example if available elsewhere (*e.g.*, in mutual fund, ETF or variable annuity prospectuses)?

- Should firms describe the types of compensation they and their financial professionals receive from sources other than the retail investor in the description of their conflicts of interest, as we have proposed (for example, with respect to revenue sharing arrangements, such as payments for "shelf space," *i.e.*, product distribution by broker-dealers)? Or, should we require firms to state in the fees and costs section of the relationship summary that they and their financial professionals receive such compensation? If so, what types of additional compensation should we require firms to disclose in the summary of fees and costs? Should we require firms to disclose how the amount of fees received from retail investors relates to the amount of fees received from others in connection with recommendations or other services to those investors? Would such disclosure be confusing to retail investors? Should we require firms only to disclose which source of fees is greater or to provide a reasonable estimate of the relative magnitude of the categories of such fees (*e.g.*, that on average for retail customers that the amount the firm receives from third parties is twice as much as the firm charges investors)?
- Should we require firms to state, as proposed, that a retail investor will also pay other fees in addition to the firm's principal fee for brokerage or advisory services, and to list such fees? Should we also require firms to state ranges for such fees?

- We are proposing disclosures that are intended to help retail investors understand how the principal types of fees firms charge for advisory and brokerage accounts affect the incentives of the firm and their financial professionals. Are these disclosures clear? Do they capture all incentives that broker-dealers or investment advisers may have from their fee structures? Are there other considerations related to fees and compensation that we should require firms to highlight for retail investors that are not captured here or elsewhere in the relationship summary? Should we require firms to include the prescribed wording, as proposed, or should we allow more flexibility in the words they use? Should we modify the prescribed wording? For example, should we expressly permit or require broker-dealers to modify the prescribed wording regarding their incentive to encourage retail investors to engage in transactions, to the extent they also receive compensation that might lower such incentive, such as asset-based compensation *(e.g.*, rule 12b-1 fees, sub-transfer agent or other similar service fees)?
- For our prescribed wording for investment advisers regarding the adviser's incentive to increase the assets in a retail investor's advisory account, would different wording better reflect this incentive? Does the proposed wording capture the conflict of interest, or does the wording suggest that advisers will increase retail investors' assets by generating higher investment returns? Because many advisers do not charge ongoing asset-based fees as their principal fees for retail investor advisory accounts, and instead charge fixed fees, hourly fees, commissions or other types of fees, should we require these firms to state the

incentives they have as a result of receiving such other types of fees? If so, what are the incentives that such firms have that are important for retail investors to understand and would be relevant to the relationship summary?

- These proposed disclosures about a firm's incentives can also be considered to involve conflicts, as they address the incentives that investment advisers and broker-dealers have as a result of receiving certain types of fees. Should we require this disclosure in the conflicts of interest disclosure instead of the summary of fees and costs? Should we require firms to include in the summary of fees and costs any other fee-related conflicts that we propose to include in the conflicts of interest disclosure, as discussed in Section II.B.6 below? Should we require firms to include other fee-related conflicts in these sections that are not included elsewhere in the relationship summary?
- Would our proposed disclosure for advisers and broker-dealers, that retail investors may, in certain circumstances, prefer one type of fee over another, be useful to retail investors? Are these proposed disclosures clear? Do they adequately capture the typical circumstances in which retail investors would prefer one fee type over another? Are there other considerations related to fees and compensation that we should require or permit firms to highlight for retail investors that are not captured here or elsewhere in the relationship summary? Should we require firms to include the prescribed wording, as proposed, or should we allow more flexibility in the words they use? Should we modify the prescribed wording? Does the proposed prescribed wording capture the range of business models among investment advisers and broker-dealers? Would the

prescribed wording require a firm to provide any inaccurate information given that particular firm's circumstances?

- Should we require firms to make disclosures about wrap fee programs, as proposed? Would the proposed disclosures help investors to understand the fees and costs associated with a wrap fee program as compared to unbundled advisory accounts and brokerage accounts? Would the proposed disclosures help retail investors to make informed choices about whether a wrap fee program suits their needs, as compared with unbundled investment advisory or brokerage services? If not, how could we revise it? Are there any revisions to the descriptions of wrap fee programs that would make the proposed disclosures more useful to investors?
- Are there other differences between wrap fee programs, unbundled advisory accounts, and brokerage accounts that we should require firms to include, such as other differences in fees and services? Would more or less information about wrap fee programs be helpful for retail investors? For instance, should we require firms to disclose information about the firms that participate in the wrap fee programs they recommend (e.g., the wrap fee program sponsors or managers), and any particular conflicts relevant to investors in wrap fee programs? Should we require more or less disclosure, or different disclosure, about the amount and frequency of additional transaction fees retail investors incur in wrap fee programs? Are there any elements of the proposed requirements that we should exclude? If so, why? Should any of the required disclosures be included in a different section of or an appendix to the relationship summary?

- Have we appropriately tailored the information required for advisers that provide advice about investing in both a wrap fee and a non-wrap fee program, and advisers that only provide advice about investing in a wrap fee program? Should we require firms that provide advice about investing in both a wrap fee and a non-wrap fee program to prepare a separate relationship summary for the wrap fee program? Should we instead require firms to prepare an appendix with information about the wrap fee program, in addition to the relationship summary, as we do for the Form ADV brochure? If so, what types of information should we require firms to include about wrap fee programs in a separate relationship summary or appendix, and why should we require such disclosure?
- Should we require broker-dealers that sponsor wrap fee programs to include any additional disclosures about wrap fee programs, other than the disclosures that would be made by dual registrants?
- We understand that client-facing firms – or advisers that provide advice to retail investors about investing in wrap fee programs – are not necessarily the same firms that sponsor wrap fee programs (we define a wrap fee program sponsor in Form ADV General Instructions as a firm that sponsors, organizes, or administers the program or selects, or provides advice to clients regarding the selection of, other investment advisers in the program). Should we require each client-facing firm to include the proposed wrap fee disclosures in its relationship summary, even if the firm is not the wrap fee program sponsor, as proposed? Please describe how this information is currently provided to wrap fee program clients.

- Should we require only sponsors of wrap fee programs (and not all client-facing firms) to include the proposed wrap fee disclosures in the relationship summary, similar to the Form ADV wrap fee brochure delivery requirement, which requires only investment advisers that sponsor wrap fee programs to deliver to their wrap fee clients the Form ADV wrap fee brochure? If so, should we permit only one sponsor of a wrap fee program that has multiple sponsors to include the proposed wrap fee disclosures in the relationship summary, similar to the delivery requirements for the Form ADV wrap fee brochure?
- In addition to wrap fee programs, are there other types of retail investor programs and services for which it would be useful to require investment advisers and broker-dealers to disclose additional information about the nature and scope of services, fees and conflicts of interest? If so, which programs and services, and why should we require such disclosure?
- Are there any common misconceptions about broker-dealers' and investment advisers' compensation that the relationship summary should specifically seek to clarify or correct (*e.g.*, that the firm or financial professional will only be compensated if the retail investor makes money on the investment)?

5. Comparisons

We are proposing to require standalone investment advisers and standalone broker-dealers to prepare this section under the following headings: "Compare with Typical Brokerage Accounts" (for standalone investment advisers) or "Compare with Typical Advisory Accounts"

(for standalone broker-dealers).[197] Specifically, standalone broker-dealers would include the following information about a generalized retail investment adviser: (i) the principal type of fee for investment advisory services; (ii) services investment advisers generally provide, (iii) advisers' standard of conduct; and (iv) certain incentives advisers have based on the investment adviser's asset-based fee structure.[198] For investment advisers, this section would include parallel categories of information regarding broker-dealers.[199]

We are proposing to require these disclosures to help retail investors choose among different account types and services. Having a clear explanation of differences in the fees, scope of services, standard of conduct, and incentives that are generally relevant to advisory and brokerage accounts would help retail investors that are considering one such type of relationship to compare whether their needs might be better met with the other type of relationship. In addition, we are proposing to prescribe wording in this section because it is intended to provide a general comparison of what we believe is a typical brokerage or investment adviser account that is offered to retail investors. Moreover, we believe prescribing language will promote

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197 Proposed Items 5.A. and 5.B. of Form CRS. As discussed above, for purposes of the relationship summary, we propose to define a standalone investment adviser as a registered investment adviser that offers services to retail investors and (i) is not dually registered as a broker-dealer or (ii) is dually registered as a broker-dealer but does not offer services to retail investors as a broker-dealer. We propose to define a standalone broker-dealer as a registered broker-dealer that offers services to retail investors and (i) is not dually registered as an investment adviser or (ii) is dually registered as an investment adviser but does not offer services to retail investors as an investment adviser. Proposed General Instruction 9.(f) to Form CRS. *See supra* note 51. A dually registered firm that offers retail investors only advisory or brokerage services (but not both) may in the future decide to offer retail investors both services. We would expect a firm to update its relationship summary within 30 days whenever any information in the relationship summary becomes materially inaccurate. *See* proposed General Instruction 6.(a). to Form CRS and *infra* note 350 and accompanying text. In addition, the firm would communicate the information in its amended relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge. *See* proposed General Instruction 6.(b) to Form CRS and *infra* note 354 and accompanying text.

198 Proposed Item 5.B. of Form CRS.

199 Proposed Item 5.A. of Form CRS.

uniformity and allow retail investors to receive the same information to use in comparing choices from different standalone firms.

Standalone investment advisers would be required to include the following prescribed language (emphasis required): "You could also open a brokerage account with a ***broker-dealer***, where you will pay a ***transaction-based fee***, generally referred to as a commission, when the broker-dealer buys or sells an investment for you."[200] They would be required to include prescribed statements in bullet point format (except as otherwise specified) under the lead-in "Features of a typical brokerage account include:"[201] First, there would be a general description of brokerage accounts: "With a broker-dealer, you may select investments or the broker-dealer may recommend investments for your account, but the ultimate decision as to your investment strategy and the purchase and sale of investments will be yours."[202] This statement would highlight for the retail investor two aspects of a typical broker-dealer's services that differ from that of an investment adviser – specifically, that an investor may select investments without advice or he or she may receive recommendations from the broker-dealer, and that the investor will make the ultimate investment decision.

Standalone investment advisers would then include the following information about the standard of conduct applicable to broker-dealers: "A broker-dealer must act in your best interest and not place its interests ahead of yours when the broker-dealer recommends an investment or an investment strategy involving securities. When a broker-dealer provides any service to you, the broker-dealer must treat you fairly and comply with a number of specific obligations. Unless you and the broker-dealer agree otherwise, the broker-dealer is not required to monitor your

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200 *Id.*

201 *Id.*

202 Proposed Item 5.A.1. of Form CRS.

portfolio or investments on an ongoing basis."[203] As discussed above in Section II.B.3, above, the applicable standard of conduct for financial professionals has been a source of confusion among retail investors. This statement would provide information to retail investors about the obligations of broker-dealers, including some differences from investment advisers' obligations so that they can consider this factor when determining whether brokerage services might better suit their needs.

Standalone investment advisers would then include the following statement discussing incentives created by a typical broker-dealer's fee: "If you were to pay a transaction-based fee in a brokerage account, the more trades in your account, the more fees the broker-dealer charges you. So it has an incentive to encourage you to trade often."[204] This disclosure is substantially similar to the disclosure we propose a broker-dealer would be required to include in the "Fees and Costs" section of its relationship summary.[205] As discussed above, we believe this information would help retail investors understand how the fee structures for brokerage accounts could affect their investments, which they could compare with the incentives advisers have based on their fee structure.[206]

Finally, a tabular chart would compare certain specified characteristics of a transaction-based fee and an ongoing asset-based fee side-by-side, set off by the wording "You can receive advice in either type of account, but you may prefer paying:"[207] One column would include the following (emphasis required): "***a transaction-based fee*** from a cost perspective, if you do not

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203 Proposed Item 5.A.2. of Form CRS.

204 Proposed Item 5.A.3. of Form CRS.

205 *See supra* Section II.B.4.

206 *Id.*

207 Proposed Item 5.A.4. of Form CRS.

trade often or if you plan to buy and hold investments for longer periods of time."[208] The other column would include the following (emphasis required): "***an asset-based fee*** if you want continuing advice or want someone to make investment decisions for you, even though it may cost more than a transaction-based fee."[209] This disclosure is substantially similar to the disclosure we propose that each dual registrant would include in the "Fees and Costs" section of its relationship summary.[210] For the reasons discussed above, we are proposing this requirement to encourage choice across account types and services.[211] We are also proposing that advisers include this information in the specified side-by-side manner in order to promote comparisons between the relevant considerations for both types of relationships.

Standalone broker-dealers would be required to include the following prescribed language (emphasis required), which would highlight for the retail investor the different fee structure of many investment advisers: "You could also open an advisory account with an ***investment adviser***, where you will pay an ongoing ***asset-based fee*** that is based on the value of the cash and investments in your advisory account."[212] Standalone broker-dealers would list prescribed statements describing certain differences from investment advisers in bullet point format (except as otherwise specified) under the lead-in "Features of a typical advisory account include:".[213] First, there would be a general description of investment advisory accounts as

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208 *Id.*

209 *Id.*

210 *See supra* Section II.B.4.

211 *Id.*

212 Proposed Item 5.B. of Form CRS. We recognize that some investment advisers charge other types of fees for their advisory services, including fixed fees for one-time services such as financial planning. However, because asset-based fees are a common type of fee for advisory services, we think it would be useful for firms to describe asset-based fees in this section of the relationship summary for comparison with broker-dealers' transaction-based fees.

213 Proposed Item 5.B. of Form CRS.

follows: "Advisers provide advice on a regular basis. They discuss your investment goals, design with you a strategy to achieve your investment goals, and regularly monitor your account."[214] The next bullet would highlight that investment advisers offer discretionary accounts and non-discretionary accounts by including the following (emphasis included): "You can choose an account that allows the adviser to buy and sell investments in your account without asking you in advance (a "***discretionary account***") or the adviser may give you advice and you decide what investments to buy and sell (a "***non-discretionary account***")."[215] Together, these statements would highlight for the retail investor two aspects of a typical investment adviser's services that differ from the typical services of a broker-dealer – specifically, ongoing advice and monitoring and discretionary accounts.

Standalone broker-dealers would then include the following disclosure about an investment adviser's standard of conduct: "Advisers are held to a fiduciary standard that covers the entire relationship. For example, advisers are required to monitor your portfolio, investment strategy and investments on an ongoing basis."[216] As discussed above, the applicable standard of conduct for financial professionals has been a source of confusion among retail investors. This statement would provide information to retail investors about the obligations of investment advisers so that they can consider this factor when determining whether investment advisory services might better suit their needs.

Standalone broker-dealers would then include the following disclosure about a typical investment advisory asset-based fee, as follows: "If you were to pay an asset-based fee in an

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214 Proposed Item 5.B.1. of Form CRS.

215 Proposed Item 5.B.2. of Form CRS.

216 Proposed Item 5.B.3. of Form CRS.

advisory account, you would pay the fee periodically, even if you do not buy or sell."[217] They would also be required to include the following prescribed disclosure about hourly fees and one-time flat fees, which are common among investment advisers that offer financial planning services and other advisory services to retail investors: "You may also choose to work with an investment adviser who provides investment advice for an hourly fee, or provides a financial plan for a one-time fee."[218]

The next statement would note certain incentives created by an investment adviser's ongoing asset-based fee. Broker-dealers would include the following: "For an adviser that charges an asset-based fee, the more assets you have in an advisory account, including cash, the more you will pay the adviser. So the adviser has an incentive to increase the assets in your account in order to increase its fees."[219] This statement is substantially similar to the disclosure an investment adviser would be required to include in the "Fees and Costs" section of its relationship summary.[220] For the reasons discussed above, we believe this information would help retail investors understand how the principal fee structures for typical advisory accounts could affect their investments and the incentives financial professionals may have based on charging ongoing asset-based fees for investment advisory services. This proposed disclosure would encourage retail investors to compare these incentives with certain incentives broker-dealers have based on their fee structure, which broker-dealers would describe under "Fees and Costs."[221]

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217 Proposed Item 5.B.4. of Form CRS.

218 *Id.*

219 Proposed Item 5.B.5. of Form CRS.

220 *See supra* Section II.B.4.

221 *Id.*

Finally, standalone broker-dealers would be required to include the same tabular chart that standalone investment advisers would include.[222] As discussed above, requiring this information side-by-side would promote comparisons of typical advisory and brokerage relationships.

We request comment generally on the proposed comparison disclosures to be provided by standalone investment advisers and broker-dealers, and in particular on the following issues:

- Is it useful to require firms to include disclosures about services and fees they do not offer, so that investors know other choices are available and are better able to compare different types of firms?
- Is it clear from the headings that the information provided in this section describes a typical investment adviser and broker-dealer, and does not describe the circumstances of all investment advisers and broker-dealers? Why or why not? Should we modify the headings or provide additional information at the beginning of this section?
- Do the proposed requirements encourage disclosure that is simple, clear, and useful to retail investors? Would the proposed disclosure help investors to understand and compare the fees, services and standard of conduct associated with a firm's advisory services and brokerage services? Are there any revisions to the descriptions of fees, services, standard of conduct, and incentives that would make the proposed disclosure more useful to investors?
- Is the proposed order of the information appropriate, or should it be modified? If so, how should it be modified?

[222] Proposed Item 5.B.6. of Form CRS.

- Is the proposed disclosure about how often a typical advisory firm monitors retail investors' accounts useful to retail investors, given that different firms may view "ongoing monitoring" differently?
- Is the proposed format useful for retail investors to understand and compare fees, services, standard of conduct and incentives among broker-dealers and investment advisers? Should we permit or require further use of tables, charts, graphs or other graphics or text features?
- Should we require firms to include the prescribed wording, as proposed, or should we allow more flexibility in the words they use? Does the proposed prescribed wording capture the range of typical business models and fee structures that investment advisers and broker-dealers offer? Would the prescribed wording require a firm to provide any inaccurate information given that particular firm's circumstances? If so, how should it be modified? Instead of the proposed prescriptive wording, should the Commission permit or require a more open-ended narrative?
- How would the required explanations and various disclosures contribute to readability and length of the proposed relationship summary? Should each of these explanations be required, permitted, or prohibited? Should any of these explanations be required to appear in the relationship summary, but outside the comparisons section?
- Are there other considerations related to investment advisers and broker-dealers that we should require or permit firms to highlight for retail investors? For example, should we require advisers to state that broker-dealers sometimes offer

both full-service and discount brokerage accounts, and the differences between them, including fees? Are there any disclosures that we should omit?

- Is the proposed prescriptive wording describing the standard of conduct required for investment advisers and broker-dealers clear and useful to retail investors? Would the proposed disclosure help investors to understand the standard of conduct associated with a firm's advisory services and brokerage services? Should such disclosure be modified? If so, how should it be modified?
- Should we amend the proposed wording that describes the standard of conduct for broker-dealers to incorporate or refer to any fiduciary obligations that certain broker-dealers have under state law or other laws or regulations?
- Our proposal would require a standalone investment adviser to include prescribed disclosure about a broker-dealer's incentives based on a typical broker-dealer's principal fee structure, and vice versa. Should these disclosures be substantially similar to the disclosures we propose certain dual registrants to include, as proposed?[223] Or should we modify these disclosures for firms that do not offer retail investors both brokerage and advisory services? If so, how should these disclosures be modified?
- Our proposal would require a standalone investment adviser and a standalone broker-dealer to include prescribed disclosure that a retail investor may prefer one type of fee over another in certain circumstances. Should these disclosures be substantially similar to the disclosures we propose certain dual registrants to include, as proposed? Or should we modify these disclosures for firms that do not

[223] *See supra* Section II.B.4.

offer retail investors both brokerage and advisory services? If so, how should these disclosures be modified?

6. Conflicts of Interest

We are proposing to require that investment advisers and broker-dealers summarize their conflicts of interest related to certain financial incentives. Specifically, firms would be required to disclose conflicts relating to: (i) financial incentives to offer to, or recommend that the retail investor invest in, certain investments because (a) they are issued, sponsored or managed by the firm or its affiliates, (b) third parties compensate the firm when it recommends or sells the investments, or (c) both; (ii) financial incentives to offer to, or recommend that the retail investor invest in, certain investments because the manager or sponsor of those investments or another third party (such as an intermediary) shares revenue it earns on those products with the firm; and (iii) the firm buying investments from and selling investments to a retail investor for the firm's own account (*i.e.*, principal trading).[224]

Investment advisers, broker-dealers, and their financial professionals have incentives to put their interests ahead of the interests of their retail investor clients and customers. The federal securities laws do not preclude broker-dealers or investment advisers from having conflicts of interest that might adversely affect the objectivity of the advice they provide; however, firms and financial professionals have obligations regarding their conflicts. Investment advisers are required to eliminate, or, at a minimum, fully and fairly disclose conflicts of interest clearly

[224] Proposed Item 6 of Form CRS. Studies have shown, for example, that for broker-dealers, the most frequently identified disclosures concerned issues of compensation — e.g., how clients compensate the firm, how other firms compensate it, and how employees are compensated. *See, e.g.*, Rand Study, *supra* note 5, at xviii. We sometimes refer interchangeably to payments, compensation and benefits that firms and financial professionals receive. These terms are all meant to capture the various ways through which firms and financial professionals have financial incentives to favor a product, service, account type, investor, or provider over another.

enough for a client to make an informed decision to consent to such conflicts and practices, or reject them.[225] For broker-dealers, the federal securities laws and rules and self-regulatory organization rules address broker-dealer conflicts in one (or more) of the following ways: express prohibitions,[226] mitigation,[227] or disclosure.[228] Under Regulation Best Interest, broker-dealers would be required to establish, maintain and enforce written policies and procedures reasonably designed to identify and disclose and mitigate, or eliminate, material conflicts of interest arising from financial incentives associated with such recommendation,[229] as well as to disclose, in writing, all material conflicts of interest that are associated with the recommendation.[230]

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225 *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963) (An adviser must deal fairly with clients and prospective clients, seek to avoid conflicts with its clients and, at a minimum, make full disclosure of any material conflict or potential conflict.); *see also* Instruction 3 of General Instructions to Part 2 of Form ADV. *See* Fiduciary Duty Interpretive Release, *supra* note 123.

226 For example, FINRA rules establish restrictions on the use of non-cash compensation in connection with the sale and distribution of mutual funds, variable annuities, direct participation program securities, public offerings of debt and equity securities, and real estate investment trust programs. These rules generally limit the manner in which members can pay for or accept non-cash compensation and detail the types of non-cash compensation that are permissible. *See* FINRA Rules 2310, 2320, 2341, and 5110.

227 *See, e.g.*, FINRA Rule 3110(c)(3) (firm must have procedures to prevent the effectiveness of an internal inspection from being compromised due to conflicts of interest); FINRA Rule 3110(b)(6)(C) (supervisory personnel generally cannot supervise their own activities); FINRA Rule 3110(b)(6)(D) (firm must have procedures reasonably designed to prevent the required supervisory system from being compromised due to conflicts of interest).

228 For example, when engaging in transactions directly with customers on a principal basis, a broker-dealer violates Exchange Act rule 10b-5 when it knowingly or recklessly sells a security to a customer at a price not reasonably related to the prevailing market price and charges excessive mark-ups, without disclosing the fact to the customer. *See, e.g., Grandon v. Merrill Lynch & Co.*, 147 F.3d 184, 189-90 (2d. Cir. 1998). *See also* Exchange Act rule 10b-10 (requiring a broker-dealer effecting transactions in securities to provide written notice to the customer of certain information specific to the transaction at or before completion of the transaction, including the capacity in which the broker-dealer is acting (*i.e.*, agent or principal) and any third party remuneration it has received or will receive.

229 Broker-dealers would also be required to establish, maintain, and enforce written policies and procedures reasonably designed to identify and at a minimum disclose, or eliminate, all material conflicts of interest that are associated with such recommendation. *See* Regulation Best Interest Proposal, supra note 24, section II.D.3.

230 *See* Regulation Best Interest Proposal, supra note 24, section II.D.1.

Conflicts of interest with retail investors often arise when firms and/or their financial professionals recommend or sell proprietary products or products offered by third parties, recommend products that have revenue sharing arrangements, and engage in principal trading.[231] For example, a firm could have a financial incentive to recommend proprietary products because the firm (or its affiliate) would receive additional revenue or an affiliate could pay a firm for recommending affiliate products. A broker-dealer making a platform available for self-directed transactions may select investments available for purchase on the platform based on financial incentives the broker-dealer receives. Similarly, a financial professional could be paid for recommending affiliated products or could get a bonus or greater promotion potential for recommending certain investments.[232] These conflicts create an incentive for firms and their financial professionals to make available for sale or base investment recommendations on the compensation or profit that firms will receive, rather than on the client's best interests.[233] The

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231 *See, e.g.*, Rand Study, *supra* note 5, at 13 ("Examples of such conflicts include various practices in which an adviser may have pecuniary interest (through, *e.g.*, fees or profits generated in another commercial relationship, finder's fees, outside commissions or bonuses) in recommending a transaction to a client.") and 15 (noting that the formation of the Committee on Compensation Practices was, in part, motivated by concerns that commission-based compensation may encourage registered representatives to churn accounts or make unsuitable recommendations).

232 Jason Zweig & Anne Tergesen, *Advisers at Leading Discount Brokers Win Bonuses to Push Higher-Priced Products*, Wall Street Journal (Jan. 10, 2018), *available at* https://www.wsj.com/articles/advisers-at-leading-discount-brokers-win-bonuses-to-push-higher-priced-products-1515604130.

233 *See, e.g.*, Brochure Adopting Release, *supra* note 157, at n.62 and accompanying text and n.132; Report of the Committee on Compensation Practices (Apr. 10, 1995), at 3, *available at* https://www.sec.gov/news/studies/bkrcomp.txt ("The prevailing commission-based compensation system inevitably leads to conflicts of interest among the parties involved."). *See also* FINRA Report on Conflicts of Interest (Oct. 2013), *available at* https://www.finra.org/sites/default/files/Industry/p359971.pdf (discussing conflicts of interest in the broker-dealer industry and highlighting effective conflicts management practices); *SEC v. Capital Gains Research Bureau Inc.*, 375 U.S. at 191, 196-97 ("The Investment Advisers Act of 1940 thus reflects a congressional recognition of the delicate fiduciary nature of an investment advisory relationship . . . . An investor seeking the advice of a registered investment adviser must, if the legislative purpose is to be served, be permitted to evaluate such overlapping motivations, through appropriate disclosure, in deciding whether the adviser is serving two masters or only one, especially if one happens to be economic self-interest."); In the Matter of Feeley & Willcox Asset Management Corp., Investment Advisers Act Release No. 2143 (Jul. 10, 2003) (Commission opinion) ("It is the client, not the adviser, who is entitled to make the determination whether to waive the adviser's

Commission's enforcement actions underscore how these types of compensation arrangements and activities may produce conflicts of interest that can lead firms and their financial professionals to act in their own interests, rather than the interests of their retail investors.[234]

We are not proposing to require or permit the relationship summary disclosure to include specific information about all of the conflicts of interests that are or could be present in a firm's relationship with retail investors. For example, conflicts that can be applicable to investment advisers include using certain affiliated service providers,[235] charging performance-based fees to some accounts but not others,[236] personal trading by an adviser's personnel,[237] receipt of soft dollar products and services provided by brokers in connection with client transactions,[238] and

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conflict. Of course, if the adviser does not disclose the conflict, the client has no opportunity to evaluate, much less waive, the conflict.").

234 *See infra* notes 243, 255, 256, 260 and 267, citing examples of where we have brought enforcement actions regarding conflicts of interest arising from one or more of the following categories of compensation practices and activities: the compensation of the firm's financial professionals; payments from others; incentives for selling the firm's own products, and principal trading.

235 Item 10.C. of Form ADV Part 2A. Item 10 requires an investment adviser to describe in its brochure material relationships or arrangements the adviser (or any of its management persons) has with related financial industry participants, any material conflicts of interest that these relationships or arrangements create, and how the adviser addresses the conflicts. The disclosure that Item 10 requires highlights for clients their adviser's other financial industry activities and affiliations that can create conflicts of interest and may impair the objectivity of the adviser's investment advice. *See* Brochure Adopting Release, *supra* note 157, at 29.

236 Item 6 of Form ADV Part 2A. An adviser faces a variety of conflicts of interest that it is required to address in its Form ADV brochure, including that the adviser can potentially receive greater fees from its accounts having a performance-based compensation structure than from those accounts it charges a fee unrelated to performance (*e.g.*, an asset-based fee). *See* Brochure Adopting Release, *supra* note 157, at n.64 and accompanying text; 2008 Brochure Proposing Release, *supra* note 157, at n.51 and accompanying text.

237 Items 11.C. and 11.D. of Form ADV Part 2A. For example, because of the information they have, advisers and broker-dealers and their personnel are in a position to abuse clients' positions by, for example, placing their own trades before or after client trades are executed in order to benefit from any price movements due to the clients' trades. An investment adviser is required to address this conflict in its Form ADV brochure. *See* Brochure Adopting Release, *supra* note 157, at n.83 and accompanying text.

238 Item 12 of Form ADV Part 2A. Use of client commissions to pay for research and brokerage services presents money managers with significant conflicts of interest, and may give incentives for managers to disregard their best execution obligations when directing orders to obtain client commission services as well as to trade client securities inappropriately in order to earn credits for client commission services. *See* Brochure Adopting Release, *supra* note 157, at n.128 (citing Release 54165, *supra* note 187).

voting client securities.[239] Likewise, a broker-dealer may have several conflicts of interest with its retail investors that we are not proposing to include in the relationship summary. These include, for example, a broker-dealer's incentive to favor its institutional customers over its retail customers when making available proprietary research or certain investment opportunities, such as widely anticipated initial public offerings, acting as a market maker for a recommended security, using certain service providers, or voting client securities.[240] In addition, broker-dealers are subject to Exchange Act rules that require them to disclose in writing to the customer if they have any control, affiliation, or interest in a security they are offering or the issuer of such security.[241]

It is important for firms to disclose information about each of these conflicts to retail investors; however, we believe that requiring an exhaustive discussion of all conflicts in the relationship summary would make the relationship summary too long for its intended purpose – that is, focusing on key aspects of a firm and its services, as well as helping retail investors to make an informed choice between receiving the services of a broker-dealer or an investment adviser or among different broker-dealers or investment advisers. Since investment advisers already report conflicts of interest in Form ADV Part 2, a more exhaustive discussion of conflicts by investment advisers would be duplicative of certain disclosures provided in Form ADV

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239 Item 17 of Form ADV Part 2A. Each adviser must describe how the adviser addresses conflicts of interest when it votes securities pursuant to its proxy voting authority, as applicable. *See* Brochure Adopting Release, *supra* note 157, at n.172 and accompanying text.

240 *See* 913 Study, *supra* note 3, at nn.251 and 254 and accompanying text (discussing that courts have found that broker-dealers should have disclosed these conflicts).

241 *See* Exchange Act rules 15c1-1, 15c1-5, and 15c1-6. Similarly, rule 15c1-6 requires written disclosure of the broker-dealer's interest in a security it is offering at or before the completion of the transaction. Self-regulatory organizations require similar disclosures. *See, e.g.*, FINRA Rules 2262 and 2269; and MSRB Rule G-22.

Part 2, which is provided to clients of investment advisers, including retail investors.[242] While we are not proposing to require such detailed disclosures for broker-dealers in the relationship summary, Regulation Best Interest would require broker-dealers to disclose, in writing, all material conflicts of interest that are associated with a recommendation to a retail customer.[243]

We are proposing to require specific information about conflicts of interest related to financial incentives for recommending or selling proprietary products or products offered by third parties, and from revenue sharing arrangements. Such incentives could include, for example, the firm earning more money or the financial professional receiving compensation or other benefits, including an increase in compensation such as a bonus, when a retail investor invests in the product. Disclosure of these conflicts would highlight for retail investors that firms and financial professionals have financial incentives to place their own interests first when making investment recommendations. Including these disclosures prominently, in one place, at or before the start of a retail investor's relationship with a firm or financial professional would facilitate retail investors' understanding of the incentives that may be present throughout the

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242 For investment advisers, the Form ADV Part 2 brochure and the brochure supplement address many of the conflicts an adviser *may* have. Items in Part 2 of Form ADV may not address all conflicts an adviser may have, and may not identify all material disclosure that an adviser may be required to provide clients. As a result, delivering a brochure prepared under Form ADV's requirements may not fully satisfy an adviser's disclosure obligations under the Advisers Act. *See* Brochure Adopting Release, *supra* note 157, at n.7. Broker-dealers also must make a variety of disclosures, but the extent, form and timing of the disclosures are different. *See* 913 Study, *supra* note 3, at 55 – 58. In accordance with the Instructions to Form CRS, if a relationship summary is posted on a firm's website or otherwise provided electronically, the firm must use hyperlinks for any document that is cross-referenced in the relationship summary if the document is available online. *See* proposed General Instruction 1.(g) to Form CRS.

243 *See supra* notes 229– 230 and accompanying text. When recommending a security, broker-dealers generally are liable under the antifraud provisions if they do not give "honest and complete information" or disclose any material adverse facts or material conflicts of interest, including any economic self-interest. *See, e.g., De Kwiatkowski v. Bear, Stearns & Co.*, 306 F.3d 1293, 1302 (2d Cir. 2002); *Chasins v. Smith, Barney & Co.*, 438 F.2d 1167, 1172 (2d Cir. 1970); In the Matter of Richmark Capital Corp., Exchange Act Release No. 48758 (Nov. 7, 2003) (Commission opinion) ("Release 48758") ("When a securities dealer recommends stock to a customer, it is not only obligated to avoid affirmative misstatements, but also must disclose material adverse facts of which it is aware. That includes disclosure of "adverse interests" such as "economic self interest" that could have influenced its recommendation.") (citations omitted).

course of the relationship. Retail investors also have indicated they find information about the sources and amount of compensation from third parties useful and relevant to making informed financial decisions before engaging a firm.[244] In addition, a number of commenters responding to Chairman Clayton's Request for Comment suggested disclosure that would focus on incentives associated with the products and services offered and how associated persons are compensated.[245]

We are also proposing to require disclosures about conflicts relating to principal transactions. Commenters recognized the importance of principal trading, with appropriate safeguards, including disclosure.[246] As we explain further below, we believe that investors should be aware of and understand this conflict at or before the start of the relationship.

Specifically, we are proposing that firms use the heading "Conflicts of Interest" under which a broker-dealer, investment adviser or dual registrant would describe three categories of conflicts, as applicable to the firm.[247] To emphasize the importance of conflicts, broker-dealers would be required to state the following language after the heading: "We benefit from our

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244 *See* 917 Financial Literacy Study, *supra* note 20, at xxi. ("The most useful and relevant information that the online survey respondents indicated that they favored to make informed financial decisions before engaging a financial intermediary includes information about… [s]ources and amount of compensation that a financial intermediary may receive from third parties in connection with and [*sic*] investment transaction…").

245 *See, e.g.*, SIFMA 2017 Letter; UBS 2017 Letter; ICI 2017 Letter; State Farm 2017 Letter; IAA 2017 Letter; Bernardi Securities 2017 Letter; Fidelity 2017 Letter.

246 *See, e.g.*, SIFMA 2017 Letter (recommending that a best interest standard of conduct for broker-dealers would not prohibit principal trading, provided that such transactions be accompanied by written disclosure and corresponding client consent); Wells Fargo 2017 Letter. *See also* ICI 2017 Letter (recommending that a broker-dealer would be able to engage in principal trading, subject to appropriate limitations, disclosure, and customer consent); Bernardi Securities 2017 Letter (recommending that any revised standard of conduct for broker-dealers permit principal transactions, and suggesting that firms could implement disclosures and policies and procedures to protect investors from the related potential conflicts).

247 Proposed Items 6.A. and 6.B. of Form CRS.

recommendations to you."[248] Similarly, investment advisers would be required to state: "We benefit from the advisory services we provide you."[249] Dual registrants would be required to state: "We benefit from the services we provide you."[250] If all or a portion of a conflict is not applicable to the firm's business, the firm should omit that conflict or portion thereof.[251] If a conflict only applies to a dual registrant's brokerage accounts or investment advisory accounts, the firm would include that conflict in the applicable column.[252]

First, we propose that a firm be required to state, as applicable, that it has a financial incentive to offer or recommend to the retail investor certain investments because: (a) they are issued, sponsored or managed by the firm or the firm's affiliates, (b) third parties compensate the firm when it recommends or sells the investments, or (c) both.[253] The firm also would provide examples of such types of investments, and state if its financial professionals receive additional compensation if the retail investor buys these investments.[254]

This conflict disclosure would highlight that a variety of financial incentives affects the incentives of the firm or its financial professional to offer or recommend certain investments to the retail investor.[255] These financial incentives can range from cash and non-cash compensation

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248 Proposed Item 6.A. of Form CRS..

249 *Id.*

250 *Id.*

251 Proposed Item 6.B. of Form CRS.

252 *Id.*

253 Proposed Item 6.B.1. of Form CRS. We are not prescribing the specific language that firms must use to discuss each of these conflicts, which would give firms some flexibility to structure their disclosure, particularly if they offer proprietary products and receive compensation from third parties.

254 Proposed Items 6.B.1. of Form CRS.

255 The Commission has brought enforcement actions against firms that the Commission alleged to have failed to disclose fees, such as referral fees, that financial professionals receive as a result of recommending certain investments to retail investors. *See, e.g.*, In the Matter of Financial Design Associates, Inc. and Albert Coles Jr., Investment Advisers Act Release No. 2654 (Sept. 25, 2007) (settled action) (respondents failed to disclose to investment advisory clients payments received from a company in which clients were

that a firm or financial professional receives for selling those investments as well as less direct financial incentives. In particular, investors might not be aware that the firm or its affiliate offers proprietary products that provide a financial incentive to the firm to recommend those products, that a third party provides incentives for a firm to recommend investments, or that the firm's financial professional will receive additional compensation if the retail investor buys certain investments. We believe that requiring this disclosure is consistent with indications that retail investors find information about sources and amount of compensation that firms receive from third parties useful to make informed financial decisions.[256] Additionally, we believe that it is important for firms to separately and explicitly disclose if the financial professionals benefit from these payments because these individuals are making the recommendations to the retail investors and their compensation is an incentive that could affect their advice.

We are also proposing to require examples of the types of investments associated with each of these conflicts (*e.g.*, mutual funds and variable annuities) because we believe it would be helpful for investors to be aware of the types of products for which firms and financial professionals have these incentives.[257] We considered whether to require a complete list of investments; however, we believe that a long list of the names of each of the affected products

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advised to invest); In the Matter of Energy Equities, Inc. and David G. Snow, Investment Advisers Act Release No. 1811 (Aug. 2, 1999) (settled action) (respondents received finder's fees or other compensation from issuers, the securities of which were recommended to clients or prospective clients); *Vernazza v. SEC*, 327 F.3d 851 (9th Cir. 2003).

256 *See* 917 Financial Literacy Study, *supra* note 20, at xxi. The Commission's enforcement actions also have underscored how these types of compensation and benefits from third parties for recommending certain investments may produce conflicts of interest that lead firms and their financial professionals to favor those investments over others. *See, e.g.*, In the Matter of the Robare Group, LTD., Investment Advisers Act Release No. 3907 (Sep. 2, 2014) (Commission opinion) (investment adviser failed to disclose compensation it received through agreements with a registered broker-dealer and conflicts arising from that compensation).

257 *See* proposed Items 6.B.1. of Form CRS.

would not necessarily benefit investors or be helpful to them in their review of the firm's conflicts and could detract from the other information in the relationship summary.

Next, we propose that firms disclose revenue sharing arrangements by stating that the firm has an incentive to offer or recommend the retail investor to invest in certain investments because the manager or sponsor of those investments or another third party (such as an intermediary) shares with the firm revenue it earns on those investments.[258] The firm also would provide examples of such types of investments.[259] This disclosure would highlight another type of compensation firms receive that affects their incentives to offer or recommend certain investments to the retail investor, and like the disclosures regarding proprietary products and third party payments, would provide retail investors with information about sources of compensation the firm receives from third parties.[260] This requirement is intended to capture arrangements pursuant to which a firm receives payments or other benefits from third parties for recommending certain investments, including, for example, conflicts related to payment for distribution support or ongoing services from distributors or advisers of mutual funds, annuity products or other products. We are proposing that firms would be required to describe these and

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258 Proposed Item 6.B.2. of Form CRS.

259 *Id.*

260 The Commission has pursued enforcement actions against firms that the Commission alleged to have failed to disclose revenue sharing arrangements. *See, e.g.*, In re Edward D. Jones & Co, Securities Act Release No. 8520 (Dec. 22, 2004) (broker-dealer violated antifraud provisions of Securities Act and Exchange Act by failing to disclose conflicts of interest arising from receipt of revenue sharing, directed brokerage payments and other payments from "preferred" fund families that were exclusively promoted by broker-dealer); In re Morgan Stanley DW Inc., Securities Act Release No. 8339 (Nov. 17, 2003) ("Release 8339") (broker-dealer violated antifraud provisions of Securities Act by failing to disclose special promotion of funds from fund families that paid revenue sharing and portfolio brokerage); In the Matter of KMS Financial Services, Inc., Investment Advisers Act Release No. 4730 (Jul. 19, 2017) (dually-registered investment adviser and broker-dealer that failed, in its capacity as an investment adviser, to disclose to its advisory clients compensation it received from a third party broker-dealer for certain investments it selected for its advisory clients); In the Matter of Voya Financial Advisors, Inc., Investment Advisers Act Release No. 4661 (Mar. 8, 2017) (registered investment adviser failed to disclose to its clients compensation it received through an arrangement with a third party broker-dealer and conflicts arising from that compensation).

other conflicts of interest even if the compensation the firm receives is not shared with the firm's financial professionals, as the compensation can create incentives for the firm to promote certain investments over others. These types of distribution-related arrangements may give broker-dealers heightened incentives to market the shares of particular mutual funds, or particular classes of fund shares. Those incentives may be reflected in a broker-dealer's use of "preferred lists" that explicitly favor the distribution of certain funds, or they may be reflected in other ways, including incentives or instructions that the broker-dealer provides to its managers or its salespersons.[261]

Finally, we propose that firms address principal trading by stating that the firm can buy investments from a retail investor, and sell investments to a retail investor, from its account (called "acting as principal").[262] Firms must state that they can earn a profit on those trades, and disclose that the firm has an incentive to encourage the retail investor to trade with it.[263] If this activity is part of the firm's investment advisory business, it must state that the retail investor's specific approval is required on each transaction.[264]

While access to securities that are traded on a principal basis, such as certain types of municipal bonds, is important to many investors, principal trades by broker-dealers and investment advisers raise potential conflicts of interest.[265] Principal trading raises concerns because of the risks of price manipulation or the placing of unwanted securities into client

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261 *See, e.g.*, Release 8339, *supra* note 260.

262 Proposed Item 6.B.3. of Form CRS.

263 *Id.*

264 Section 206(3) of the Advisers Act. Proposed Item 6.B.3. of Form CRS.

265 *See* 913 Study, *supra* note 3, at 120.

accounts (*i.e.*, "dumping").[266] Under the Advisers Act, an adviser may not engage in a principal trade with an advisory client unless it discloses to the client in writing, before completion of the transaction, the capacity in which the adviser is acting, and obtains the consent of the client to the transaction.[267] Broker-dealers also are subject to a number of requirements when they engage in principal transactions with customers, including disclosure of such capacity on the trade confirmation.[268] There is no specific requirement for broker-dealers, however, to provide written disclosure prior to the trade or obtain consent for each principal transaction.[269] Our proposal to require firms to disclose, if applicable, that they engage in principal transactions, and to summarize the conflict of interest raised by principal transactions, would not replace the disclosure and consent requirements under the Advisers Act or any other requirement, such as under the Exchange Act. Rather, our disclosure requirement would supplement such disclosures by alerting retail investors to this practice and the related conflicts of interest at the start of the relationship.

We request comment generally on the conflicts of interest disclosures proposed to be included in the relationship summary, and in particular on the following issues:

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266 *See id*., at 118.

267 Section 206(3) of the Advisers Act. *See also* Opinion of Director of Trading and Exchange Division interpreting the reference to "the transaction" to require separate disclosure and consent for each transaction. Investment Advisers Act Release No. 40 (Feb. 5, 1945) ("[T]he requirements of written disclosure and of consent contained in this clause must be satisfied before the completion of each separate transaction. A blanket disclosure and consent in a general agreement between investment adviser and client would not suffice."); 913 Study, *supra* note 3, at n.534 and accompanying text. An investment adviser must provide written disclosure to a client and obtain the client's consent at or prior to the completion of each transaction. 913 Study, *supra* note 3, at n.535 and accompanying text. *See also, e.g.*, Release 3929, *supra* note 133; In the Matter of JSK Associates, *et al.*, Investment Advisers Act Release No. 3175 (Mar. 14, 2011) (settled action).

268 As an example of one such requirement, broker-dealers must disclose their capacity in the transactions (typically on the confirmation statement). *See* Exchange Act rule 10b-10.

269 *See* 913 Study, *supra* note 3, at n.540 and accompanying text.

- Do the proposed conflicts of interest disclosures encourage firms to provide information that is simple, clear, and useful to retail investors? Would the proposed disclosures help retail investors to compare the conflicts of interest associated with advisory services and brokerage services and the conflicts among firms? Does the relationship summary help retail investors understand that compensation to firms and financial professionals creates incentives that could impact the advice or recommendations that they provide? If not, should it do so and if so, what modifications should be made to the summary to address this concern?
- Should we require brief statements about particular conflicts of interest, as proposed, or should we require a more open-ended narrative or more prescribed wording? Would an open-ended narrative permit firms to tailor the disclosure and describe all of the conflicts they believe retail investors should know? Or would firms seek to provide so much information about their conflicts that the proposed page limit (or equivalent limit in electronic format) would not provide enough space for all of the disclosures? How would the required explanations of various items contribute to the readability and length of the relationship summary?
- Our intent in using layered disclosure for conflicts (*i.e.*, short summaries of certain types of conflicts of interest with information later in the relationship summary on where retail investors can find more information) is to highlight these conflicts and encourage retail investors to ask questions and seek more information about the firm's and its financial professionals' conflicts of interest. Do our proposed requirements achieve this goal? In light of our objective of

keeping the relationship summary short, should we instead prescribe general language concerning the importance of understanding conflicts, while simply requiring cross-references to the relevant sections of Form ADV Part 2 brochure or brochure supplement (for investment advisers) and relevant disclosures typically included in account opening documents or websites (for broker-dealers)? Should we provide wording to encourage retail investors to ask questions about conflicts, including advising customers to go through all of the firm's and financial professional's conflicts with the financial professional? Are there other modifications or alternatives we should consider?

- Should we instead require firms to make the conflicts of interest disclosure more detailed, even if it results in a lengthier relationship summary?
- Are the proposed conflicts of interest disclosures too limited? Are there other types of conflicts we should include, such as additional disclosure currently required in the Form ADV Part 2 brochure or brochure supplement (for investment advisers), or disclosure typically included in account opening documents or websites (for broker-dealers)? Should we, for example, require firms to describe all of their conflicts and how they address them, such as specific information about incentives to favor certain clients over others, agency cross-trades, relationships with certain clients, personal trading by personnel, soft dollar practices, directed brokerage, proxy voting practices, or acting as a market maker for a recommended security? Or should we require firms to list all of their conflicts and provide cross references to where additional information about each conflict can be found (i.e., cross referencing the relevant sections of Form ADV

Part 2 and analogous broker-dealer disclosures)? Would this detract from the brevity of the disclosure? Is there another way to provide additional information about conflicts to retail investors in a way that would be meaningful to them and would facilitate their ability to obtain additional information?

- Are there certain types of investments that should be disclosed by firms as ones that the firm "issues, sponsors, or manages?" For example, should we require firms to disclose that any investment with a firm's name in the title is generally an investment that the firm issues, sponsors, or manages? If a firm uses a name other than its own name to market proprietary investments, should we require firms disclose such other names?
- Should we require firms to disclose whether they provide ancillary services to retail investors themselves or through their affiliates so that retail investors better understand that the firm has incentives to select its affiliates over third parties?
- With respect to the required disclosure regarding financial incentives a firm has to offer or recommend investment in certain investments because they are offered by the firm's affiliates, or third parties compensate the firm for selling their investments, or both, would firms understand what types of financial incentives would be covered by this item – and what would not be covered? Should the Commission provide additional guidance or instructions to clarify?
- Should we require firms to disclose that they use third-party service providers that offer the firms or their financial professionals additional compensation? For example, some investment advisers select broker-dealers to execute their clients' transactions that provide the adviser or financial professionals with compensation

or other benefits, including in the form of client referrals. Should we highlight that compensation can be in the form of advisory client referrals?

- Firms would be required to provide examples of investments that firms have a financial incentive to offer. Are these requirements clear? Should we provide additional guidance? Should firms also be required to identify specific account types for which financial professionals receive incentives? Or should firms list all of their services or products that create the stated conflicts (or cross-reference to such disclosure elsewhere)? Should additional information be provided in this section of the relationship summary or should it be provided in an attachment?
- Should firms explicitly state that other firms offer similar products that could be less expensive for the retail investor? Should we require firms to disclose if the firm engages in principal trading, as proposed, including that the firm can earn a profit on these trades and may have an incentive to encourage the retail investor to trade with the firm? Should we require investment advisers to state the retail investor's specific approval on each principal transaction is required? Are there additional disclosures that we should require for broker-dealers?
- Should we require firms to disclose any additional conflicts of interest related to the compensation of financial professionals? For example, should firms be required to include any specific conflicts related to financial professionals' outside business activities? Should we require firms to include additional disclosure on compensation that a financial professional receives from third parties, such as compensation that an investment adviser representative receives in his or her capacity as a registered representative of an unrelated broker-dealer?

- Should we allow firms to choose the order they present the conflicts? For example, should firms be permitted to base the order on the conflicts they believe are most relevant in their business, or is a standardized order preferable to increase the comparability of the disclosures among different firms? If a firm does not engage in any practices that would be required to be disclosed, should we permit or require a firm to state that it does not have that conflict, or should we require firms to say nothing, as proposed? Would it be confusing to investors if, as proposed, the order was prescribed but some firms omit certain conflicts because they do not have the particular conflict? Would such presentation lessen the ability to compare conflicts across firms?
- Is the proposed format useful for retail investors in understanding and comparing conflicts of interest among firms? Would the use of tables, charts, graphs or other graphics or text features be helpful in explaining all or any particular conflict? If so, how could firms structure that disclosure?
- Should any of the conflicts be required to appear in the relationship summary, but outside of the conflicts of interest section?

7. Additional Information

We are proposing to require that firms include information on where retail investors can find more information about the firm's disciplinary events, services, fees, and conflicts, which facilitates the layered disclosure that the relationship summary provides.[270] This section would be titled "Additional Information" and firms would include the following after the title: "We

[270] *See supra* notes 37, 48 – 50 and 139 – 141 and accompanying text (regarding the use of layered disclosure and alternative approaches to presentation).

encourage you to seek out additional information." First, firms would be required to state whether or not they or their financial professionals currently disclose or are currently required to disclose certain legal or disciplinary events to the Commission, self-regulatory organizations, state securities regulators or other jurisdictions, as applicable. We are including information about a firm's and its financial professionals' disciplinary information because this information may assist retail investors in evaluating the integrity of a firm and its financial professionals.[271] For example, a prior disciplinary event could reflect upon the firm's integrity, affect the degree of trust and confidence a client would place in the firm, or impose limitations on the firm's activities.[272] Knowledge of a firm's and financial professional's disciplinary history is among the most important items for retail investors when deciding whether to receive financial services from a particular firm, according to one study.[273] Approximately 67.5% of the online survey respondents considered information about an adviser's disciplinary history to be absolutely essential, and about 20.0% deemed it important, but not essential.[274] But despite its importance,

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271 *See* Brochure Adopting Release, *supra* note 157, at n.81 and accompanying text. *See also* Electronic Filing by Investment Advisers; Proposed Amendments to Form ADV, Investment Advisers Act Release No. 1862 (Apr. 5, 2000) [65 FR 20524 (Apr. 17, 2000)], at nn.148 – 149 and accompanying text ("2000 Brochure Proposing Release") ("When assessing whether an adviser will fulfill its obligations to clients, an investor would likely give great weight to whether the adviser has met its fiduciary and other legal obligations in the past."); Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving a Proposed Rule Change to Amend FINRA Rule 8312 (FINRA BrokerCheck Disclosure) to Expand the Categories of Civil Judicial Disclosures Permanently Included in BrokerCheck, Release No. 34-71196 (Dec. 27, 2013) [79 FR 417 (Jan. 3, 2014)] ("By making certain of this information publicly available, BrokerCheck, among other things, helps investors make informed choices about the individuals and firms with which they conduct business.").

272 *See* Brochure Adopting Release, *supra* note 157, at n.85.

273 *See* 917 Financial Literacy Study, *supra* note 20, at nn.308 and 498 and accompanying text ("When asked how important certain factors would be to them if they were to search for comparative information on investment advisers, the majority of online survey respondents identified the fees charged and the adviser's disciplinary history as the most important factors.").

274 *Id.*

many investors do not review this information prior to engaging a firm.[275] A study also found that many retail investors would check the Investment Adviser Public Disclosure site ("IAPD") for comparative information on investment advisers, including disciplinary history, if they were made aware of its existence.[276] We believe that requiring firms to state the existence of disciplinary events, provide specific questions for retail investors to ask, and provide information on where retail investors can find more information, would cause more retail investors to seek out this information and would make them better informed when they choose a firm and a financial professional.[277]

Specifically, in the relationship summary, firms would state "We have legal and disciplinary events" if they are required to disclose (i) disciplinary information per Item 11 of

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275 917 Financial Literacy Study, *supra* note 20, at n.770 (citing Applied Research Consulting LLC for FINRA Investor Education Foundation, *Financial Capability in the United States: Initial Report of Research Findings from the 2009 National Survey* (Dec. 1, 2009), *available at* http://www.usfinancialcapability.org/downloads/NFCS_2009_Natl_Full_Report.pdf ("2009 National Survey Initial Report"), which revealed that only 15% of respondents claimed that they had checked a financial professional's background or credentials with a state or federal regulator, although the Commission notes that the study encompasses a wide group of advisors, such as debt counselors and tax professionals.). In addition, the FINRA 2015 Investor Survey found that only 24% of investors were aware of Investor.gov; only 16% were aware of BrokerCheck; only 14% were aware of the IAPD website, and only 7% had used BrokerCheck. FINRA, *Investors in the United States 2016* (Dec. 2016), *available at* http://www.usfinancialcapability.org/downloads/NFCS_2015_Inv_Survey_Full_Report.pdf).

276 *See* 917 Financial Literacy Study, *supra* note 20, at nn.317 – 319 and accompanying text ([A]bout 76.5% of the online survey respondents reported that, in selecting their current adviser, they did not use an SEC-sponsored website to find information about the adviser. 73% of respondents stated that they would check IAPD if they were made aware of its existence. Of that subset—those who reported not using an SEC-sponsored website—approximately 85.2% indicated that they did not know that such a website was available for that purpose. Of that majority (i.e., a further subset) – those who were unaware of such a website – approximately 73.5% reported that they would review information about their adviser on an SEC-sponsored website if they knew it were available).

277 In addition, this would address an issue that was highlighted by the Commission's Investor Advisory Committee, which, among other things, encouraged the Commission to develop an enhanced approach to the disclosure of disciplinary events. Broker-Dealer Fiduciary Duty Recommendations, *supra* note 10 (recommending a summary disclosure document that includes, among other disclosures, basic information about a firm's disciplinary record).

Part 1A or Item 9 of Part 2A of Form ADV,[278] or (ii) legal or disciplinary events per Items 11A-K of Form BD ("Uniform Application for Broker-Dealer Registration")[279] except to the extent such information is not released through BrokerCheck pursuant to FINRA Rule 8312 or in IAPD.[280] Regarding their financial professionals, firms would determine whether they need to include the statement based on legal and disciplinary information on Form U4,[281] Form U5[282] and Form

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278 Proposed Item 7.B. of Form CRS. Generally, investment advisers are required to disclose on Form ADV Part 2A any legal or disciplinary event, including pending or resolved criminal, civil and regulatory actions, if it occurred in the previous 10 years, that is material to a client's (or prospective client's) evaluation of the integrity of the adviser or its management personnel, and include events of the firm and its personnel. *See* Brochure Adopting Release, *supra* note 157, at 22 – 27. Items 9.A., 9.B., and 9.C. provide a list of disciplinary events that are presumptively material if they occurred in the previous 10 years. However, Item 9 requires that disciplinary events more than 10 years old be disclosed if the event is so serious that it remains material to a client's or prospective client's evaluation of the adviser and the integrity of its management.

279 Item 11 of Form BD requires disclosure on the relevant Disclosure Reporting Page ("DRP") with respect to: (A) felony convictions, guilty pleas, "no contest" pleas or charges in the past ten years; (B) investment-related misdemeanor convictions, guilty pleas, "no contest" pleas or charges in the past ten years; (C) certain SEC or the Commodity Futures Trading Commission (CFTC) findings, orders or other regulatory actions (D) other federal regulatory agency, state regulatory agency, or foreign financial regulatory authority findings, orders or other regulatory actions; (E) self-regulatory organization or commodity exchange findings or disciplinary actions; (F) revocation or suspension of certain authorizations; (G) current regulatory proceedings that could result in "yes" answers to items (C), (D) and (E) above; (H) domestic or foreign court investment-related injunctions, findings, settlements or related civil proceedings; (I) bankruptcy petitions or SIPC trustee appointment; (J) denial, pay out or revocation of a bond; and (K) unsatisfied judgments or liens. Some of these disclosures are only required if the relevant action occurred within the past ten years, while others must be disclosed if they occurred at any time.

280 FINRA Rule 8312 governs the information FINRA releases to the public via BrokerCheck. FINRA established BrokerCheck in 1988 (then known as the Public Disclosure Program) to provide the public with information on the professional background, business practices, and conduct of FINRA member firms and their associated natural persons. The information that FINRA releases to the public through BrokerCheck is derived from the CRD system, the securities industry online registration and licensing database. Firms, their associated natural persons and regulators report information to the CRD system via the uniform registration forms (Form U4 (Uniform Application for Securities Industry Registration or Transfer), Form U5 (Uniform Termination Notice for Securities Industry Registration), Form U6 (Uniform Disciplinary Action Reporting Form), Form BD (Uniform Application for Broker-Dealer Registration), Form BDW (Uniform Request for Broker-Dealer Withdrawal), and Form BR ("Uniform Branch Office Registration Form")). Under FINRA Rule 8312, FINRA limits the information that is released to BrokerCheck in certain respects. For example, pursuant to FINRA Rule 8312(d)(2), FINRA shall not release "information reported on Registration Forms relating to regulatory investigations or proceedings if the reported regulatory investigation or proceeding was vacated or withdrawn by the instituting authority." We believe it is appropriate to limit disclosure in the relationship summary to disciplinary information or history that would be released to BrokerCheck.

281 Form U4 (Uniform Application for Securities Industry Registration or Transfer) requires disclosure of registered representatives' criminal, regulatory, and civil actions similar to those reported on Form BD as well as certain customer-initiated complaints, arbitration, and civil litigation cases. *See generally* Form U4.

U6.[283] In particular, firms would be required to state, "We have legal and disciplinary events" if they have financial professionals for whom disciplinary events are reported per Items 14 A-M on Form U4, Items 7(a) and 7(c) – (f) on Form U5,[284] and Form U6 except to the extent such information is not released through BrokerCheck pursuant to FINRA Rule 8312 or in IAPD.[285]

We considered requiring firms to provide additional details about the reported legal and disciplinary events of the firms and their financial professionals. For example, we could have proposed to require firms to include details about the type and number of the reported events. Broker-dealers and investment advisers do not report all of the same types of disciplinary events. We also considered whether to require firms to only discuss the types of disciplinary events that both broker-dealers and investment advisers report, require investment advisers to disclose complaints and other disciplinary events that only broker-dealers report, or create separate requirements to require firms to disclose certain types of events in the relationship summary without reference to information in other disclosures.

We are not proposing to take any of these approaches because this is summary disclosure rather than a comprehensive discussion of a firm's legal and disciplinary history. We believe that for many firms, requiring additional information would include too much detail for short summary disclosure, and updating these details in the relationship summary on an ongoing basis

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282 Form U5 (Uniform Termination Notice for Securities Industry Registration) requires information about representatives' termination from their employers. *See* Form U5.

283 Form U6 (Uniform Disciplinary Action Reporting Form) is used by SROs, regulators, and jurisdictions to report disciplinary actions against broker-dealers and associated persons. This form is also used by FINRA to report final arbitration awards against broker-dealers and associated persons. *See* Form U6.

284 The disclosure would be triggered by reportable information on Items 7(a) and 7(c) through (f). Item 7(b) (Internal Review Disclosure) is not released to BrokerCheck by FINRA, pursuant to FINRA Rule 8312(d)(3). As noted above (*see supra* note 280), we believe it is appropriate to limit disclosure in the relationship summary to disciplinary information or history that would be released to BrokerCheck.

285 Proposed Item 7.B.3. of Form CRS.

would add significant costs without compensating benefit. The information already is required to be disclosed elsewhere, and the relationship summary as proposed would direct retail investors to those resources. We believe that requiring an affirmative statement that the firm and its financial professionals have reportable legal or disciplinary events, if applicable, will flag this important issue for retail investors and help them to determine whether they want additional information in other disclosures. By proposing to base the new disclosure on information that is already reported elsewhere and also to include details about where to find more information, we would give retail investors the tools to learn more.[286] Furthermore, as discussed below, the statement encouraging retail investors to visit Investor.gov for more information would help retail investors to more easily learn additional details from the firms themselves and from their existing disclosures.[287]

Next, all firms would be required to include the following wording to highlight where retail investors can find more information about the disciplinary history of the firm and its financial professionals, whether or not the firm is required to state the existence of legal or disciplinary events in the relationship summary: "Visit Investor.gov for a free and simple search tool to research our firm and our financial professionals."[288]

Retail investors would further benefit from understanding how to report problems and complaints to the firm and regulators. Accordingly, we propose to require that firms include the following wording next in this section:

> " To report a problem to the SEC, visit Investor.gov or call the SEC's toll-free investor assistance line at (800) 732-0330. [To report a problem to FINRA, [ ].] If you have a

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286 Proposed Item 7.D. of Form CRS.

287 *Id.*

288 Proposed Item 7.C. of Form CRS.

problem with your investments, account or financial professional, contact us in writing at [insert your primary business address].[289]

Broker-dealers and dual registrants also would include the bracketed language regarding how to report a problem to FINRA. Firms would be required to review and update (if needed) the current telephone numbers for the SEC and FINRA at least annually.[290]

Firms would be required to state where the retail investor can find additional information about their brokerage and investment advisory services, as applicable. Broker-dealers would be required to direct retail investors to additional information about their brokers and services on BrokerCheck (https://brokercheck.finra.org), their firm websites (including a link to the portion of the website that provides up-to-date information for retail investors), and the retail investor's account agreement.[291] Broker-dealers that do not have public websites would be required to state where retail investors can find up-to-date information.[292]

Investment advisers likewise would be required to direct retail investors to additional information in the firm's Form ADV Part 2 brochure and any brochure supplement provided by a financial professional to the retail investor.[293] If an adviser has a public website and maintains a current version of its firm brochure on the website, the firm would be required to provide the website address.[294] If an adviser does not have a public website or does not maintain its current

289 Proposed Item 7.D. of Form CRS.

290 *Id.*

291 Proposed Item 7.E.1. of Form CRS.

292 *Id.*

293 Proposed Item 7.E.2. of Form CRS.

294 *Id.*

brochure on its public website, then the adviser would provide the IAPD website address (https://adviserinfo.sec.gov).[295]

Unlike investment advisers, which deliver brochures and brochure supplements to clients, broker-dealers are not currently required to deliver to their retail investors written disclosures covering their services, fees, conflicts, and disciplinary history in one place.[296] However, under Regulation Best Interest, broker-dealers would be required to disclose, in writing, the material facts relating to the scope and terms of the relationship with the retail customer including all material conflicts of interest that are associated with the recommendation.[297] We understand that, under current practice, broker-dealers typically provide information about some or all of the categories of disclosure included in this relationship summary on their firm websites and in their account opening agreements. We recognize that the different disclosure requirements for investment advisers and broker-dealers may result in retail investors having access to more information about investment advisers on a particular topic as compared to information about broker-dealers and *vice versa*. We request comment on whether we should take additional steps to ensure that retail investors have access to a similar amount of additional information about each of the topics covered by the relationship summary, such as by requiring firms to include appendices or hyperlinks with specific information.

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295 *Id*. SEC- and state-registered investment advisers are required to file their brochures and brochure amendments through the IARD system. *See* rules 203-1 and 204-1 of the Advisers Act and similar state rules. Members of the public can view an adviser's most recent Form ADV online at the IAPD website: www.adviserinfo.sec.gov.

296 Broker-dealers are required under certain circumstances, such as when effecting certain types of transactions, to disclose certain conflicts of interest to their customers in writing, in some cases at or before the time of the completion of the transaction. *See, e.g.*, *supra* notes 228 and 241 and accompanying text. *See also* 913 Study, *supra* note 3, at nn.256 – 259 and accompanying text; *supra* notes 230 and 243 – 243 and accompanying text (describing broker-dealer obligations under proposed Regulation Best Interest).

297 *See* Regulation Best Interest Proposal, *supra* note 24, at section II.D.1.

We request comment generally on the disclosure about where to find additional information, and in particular on the following issues:

- Do commenters agree that it is important for retail investors to know of a firm and its financial professionals' legal and disciplinary events before entering into an agreement with a firm? Why or why not?
- Is including the disciplinary history disclosure in the additional information section sufficient to draw a retail investors' attention or encourage retail investors to ask follow-up questions on this topic?
- Would the proposed format with prescribed wording effectively communicate information about disciplinary events to retail investors? Or should we use a table with yes/no check boxes or another graphical format to describe this information, or should we permit a firm to state in its own words whether it has reported any events? What approach would permit easier comparison by retail investors across firms, including dual registrants?
- Would more detail about these events be more beneficial and easily understandable for retail investors? For example, should firms be required to provide background about the types of events that would trigger the disclosure (such as criminal, civil, and regulatory actions and, for broker-dealers and financial professionals, customer complaints, arbitrations and bankruptcies)? Should we require separate disclosures for firms and their financial professionals? Should we consider requiring a more specific list of the types of disciplinary events that firms and financial professionals report and require firms to state whether there are reported disclosures for each type? For example, should firms be required to state they have reported disclosures for criminal actions, civil actions and

administrative proceedings, and for broker-dealers specifically, arbitrations and complaints? Should we instead require firms to disclose the total number of the legal and disciplinary events that are reported on Form BD, Form ADV, and/or Forms U4, U5, and U6, as applicable? Or should we require firms to report the total number of all reported criminal actions, civil actions, administrative proceedings, arbitrations, and complaints for them and their financial professionals, as applicable? Would this information be confusing for retail investors without more information about each reported event? If we do require this information, should we require firms to disclose the percentage of a firm's total financial professionals that have reported disciplinary events? As part of this approach, should we require a firm to disclose its total number of financial professionals to provide additional context for the percentage?

- Should we require firms to include specific wording directing retail investors to ask them questions about these events and to review more detailed disclosures by searching Investor.gov?
- Should firms be required or permitted to state that they do not currently have reportable legal and/or disciplinary events, if that is the case? Should we require firms to distinguish whether they or their financial professionals have reportable disciplinary events, for example by stating "Our firm has legal and disciplinary events" or "We have financial professionals who have legal and disciplinary events"?
- Do commenters agree with requiring disclosure if firms or financial professionals have reported legal and/or disciplinary events on Form BD, Forms U4, U5 or U6, and Form ADV, as applicable? Do commenters agree with the specific items on those forms that we have identified as triggering reportable events? Should we only require disclosure of

the types of legal events that both broker-dealers and investment advisers report? For example, should we require all firms to disclose financial information, which broker-dealers are required to report pursuant to Items 11 (I, J, and K) on Form BD but investment advisers do not report? Or, in the alternative, should we exclude financial disclosures from a broker-dealer's reportable legal or disciplinary events? Do commenters agree that the legal or disciplinary events triggering disclosure on the relationship summary should be the same for financial professionals working for broker-dealers as for investment advisers? If not, why not?

- Do commenters agree that, for broker-dealers and financial professionals of broker-dealers and investment advisers, we should exclude information that is not released to BrokerCheck or IAPD pursuant to FINRA Rule 8312? BrokerCheck and IAPD include additional information, including summary information about certain arbitration awards against a financial professional, or against a firm in BrokerCheck, involving a securities or commodities dispute with a public customer. Although broker-dealers are not required to report arbitrations on Form BD, should we include arbitrations as reportable events in light of the BrokerCheck disclosures? If so, how would commenters suggest articulating the required disclosure?
- Pursuant to FINRA Rule 4530, broker-dealers are required to disclose certain information to FINRA that is not reported on Form BD (e.g., customer complaints and arbitrations). Should we include disclosures made to FINRA pursuant to FINRA Rule 4530 as reportable events? If so, should we require disclosure of similar events by investment advisers? Why or why not?

- Do commenters believe that stating whether a firm has legal and disciplinary events and then providing hyperlinks on where to find additional information is the correct approach? Should we explicitly require deep links? Why or why not? Do commenters believe that retail investors will check Investor.gov? Should we require firms to cross reference other sources of disciplinary information, including providing direct links to the IAPD or BrokerCheck? Why or why not?
- Rather than asking firms to identify whether they have legal and disciplinary events, should the relationship summary note that retail investors may want to consider this information and then encourage retail investors to ask their financial professional for more details and include cross references to where further information can be found? Why or why not? With respect to robo-advisers or broker-dealers providing online services, will a financial professional be available to answer these types of questions?[298]
- Should we adopt a definition of "financial professional" for purposes of this disclosure? If so, how would commenters suggest formulating the definition?
- Our intent in using layered disclosure, with short summaries of selected disclosures and information on where retail investors can find more information, is to encourage retail investors to ask questions and seek more information about the firm's and their financial professionals' services, fees, conflicts of interest and disciplinary events. Does the proposed relationship summary, in general, and this additional information section, in

[298] Robo-advisers should also keep in mind the considerations set forth in the robo-adviser guidance update specifically as it relates to the substance and presentation of disclosures. *See* Robo-Advisers, IM Guidance Update No. 2017-02 (Feb. 23, 2017), *available at* https://www.sec.gov/investment/im-guidance-2017-02.pdf.

particular, achieve this goal? Are there modifications or alternatives we should consider to achieve this goal?

- In addition or as an alternative to the proposed cross references to an investment adviser's Form ADV brochure and brochure supplement(s) and account agreement, and to a broker-dealer's public website, account agreement and BrokerCheck, should the relationship summary direct retail investors to other sources of information? Should we require firms to include public website addresses and hyperlinks to the sources of additional information, if available? Do firms' websites typically include additional information about topics included in the relationship summary? Given that not all firms have a public website or maintain current information on a public website (e.g., its current brochure or other current information), are there other places to which firms should direct retail investors to look for up-to-date information? Should we require firms that do not already maintain a public website to establish one for purposes of making the relationship summary publicly available?

8. Key Questions

We are proposing to require that firms include questions for retail investors to ask their financial professionals in the relationship summary. By requiring these questions, we intend to encourage retail investors to have conversations with their financial professionals about how the firm's services, fees, conflicts and disciplinary events affect them. We encourage financial professionals to engage in balanced and meaningful conversations with their retail investors to facilitate investors making informed decisions, using these key questions as a guide. Firms should use formatting to make the questions more noticeable and prominent (for example, by using a larger font, a text box, different font, or lines to offset the questions from the other

sections).[299] Firms would be required to include ten questions, as applicable to their particular business, under the heading "Key Questions to Ask" after stating the following: "Ask our financial professionals these key questions about our investment services and accounts." The required questions would be:

1. Given my financial situation, why should I choose an advisory account? Why should I choose a brokerage account?

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

3. What additional costs should I expect in connection with my account?

4. Tell me how you and your firm make money in connection with my account. Do you or your firm receive any payments from anyone besides me in connection with my investments?

5. What are the most common conflicts of interest in your advisory and brokerage accounts? Explain how you will address those conflicts when providing services to my account.

6. How will you choose investments to recommend for my account?

7. How often will you monitor my account's performance and offer investment advice?

8. Do you or your firm have a disciplinary history? For what type of conduct?

9. What is your relevant experience, including your licenses, education, and other qualifications? Please explain what the abbreviations in your licenses are and what they mean.

10. Who is the primary contact person for my account, and is he or she a representative of an investment adviser or a broker-dealer? What can you tell me about his or her legal obligations to me? If I have concerns about how this person is treating me, who can I talk to?[300]

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299 Proposed Item 8 of Form CRS.

300 Proposed Item 8 of Form CRS.

We are proposing to allow firms to modify or omit portions of these questions, as applicable to their business.[301] We are also proposing to require a standalone broker-dealer and a standalone investment adviser, to modify the questions to reflect the type of account they offer to retail investors (*e.g.*, advisory or brokerage account).[302] In addition, we are proposing that firms could include any other frequently asked questions they receive following these questions. Firms would not, however, be permitted to exceed fourteen questions in total in order to limit the length of the relationship summary.[303]

We recognize that advisers providing computer-generated, automated advice, often referred to as "robo-advisers," and online-only broker-dealers may employ business models that offer varying levels of interaction or no interaction with a financial professional. We are proposing to require advisers providing automated advice or broker-dealers providing online-only services without a particular individual with whom a retail investor can discuss these questions to include a section or page on their website that answers each of the above questions, and provide a hyperlink in the relationship summary to that section or page.[304] If the firm provides automated advice, but makes a financial professional available to discuss the existing account with a retail investor, that firm generally should also make the financial professional available to discuss these questions with the retail investor.

We believe that many of these questions would help retail investors to elicit more detail concerning the items discussed in the relationship summary. For example, the questions asking why an investor should choose an advisory or brokerage account and how much the investor can

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301 *Id.*

302 *Id.*

303 *Id.*

304 *Id.*

expect to pay are intended to help the retail investor receive information about services and fees that are tailored to that particular investor's circumstances. We believe that the financial professional generally would have access to the information needed to provide this information to a particular retail investor during the account opening process.[305] Questions about how the financial professional and the firm make money and about conflicts of interest would assist investors in understanding the extent to which compensation creates incentives for a financial professional to take his or her own interests into account in providing services. Similarly, the last question in the list of questions, which asks about a retail investor's primary contact at the firm and that financial professional's legal obligations, is intended to elicit a conversation about the different legal obligations of firms and financial professionals acting in an investment advisory capacity and in a brokerage capacity. Other items allow the investor to learn more specific information about the firms and financial professional, such as additional conflicts the firms or its financial professionals might have or disciplinary history.

The proposed questions cover all of the sections in the relationship summary. They also include one additional topic about the financial professional's relevant experience, including licenses and other qualifications. In our experience, the relevant experience, including licenses, education, and other qualifications for a particular financial professional are important to retail investors.[306] However, if we required firms to disclose the educational and professional certifications of each financial professional, firms would have to attach a separate disclosure for

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305 *See supra* Section II.B.4, "Summary of Fees and Costs."

306 *See* 917 Financial Literacy Study, *supra* note 20, at 24 ("Some examples of information that commenters indicated should be included in a summary disclosure document for an investment product or service include descriptions of…any eligibility requirements."); Brochure Adopting Release, *supra* note 157, at nn.213 – 216 and accompanying text (discussing commenters that supported the brochure supplement, which contains information about the educational background, business experience, and disciplinary history (if any) of the supervised persons who provide advisory services to the client).

each particular financial professional (similar to the Form ADV brochure supplement or the information about financial professionals provided on BrokerCheck and IAPD) or would have to include lengthy disclosure with information about all of their financial professionals. We believe this would be more burdensome than prompting retail investors to ask their financial professionals these questions to encourage a conversation about these topics, if such a conversation is important to that investor. We understand that including "Key Questions to Ask" would result in some firms creating policies and procedures, including supervision and compliance reviews, relating to how their financial professionals respond to the questions.

We request comment generally on the questions proposed to be included in the relationship summary, and in particular on the following issues:

- Would our proposed questions encourage discussions between retail investors and their financial professionals? Would they help retail investors become informed about how a firm's services, fees, conflicts, and disciplinary events affect them? Would they help investors to compare investment advisers and broker-dealers?
- Would financial professionals be able to answer these "Key Questions to Ask"? Do they have access to personalized information about the retail investor and the retail investor's account to be able to, for example, put together personalized fee information and estimates during the account opening process? To the extent responses would require information about the particular retail investor, would firms need to change the account opening process in order to obtain that information and provide responses?
- Should we require or permit firms to include these questions throughout the relationship summary rather than, or in addition to, including the questions in the "Key Questions to Ask"? In our proposal, for example, the fees and costs section of the relationship

summary directs retail investors to ask their financial professionals for personalized fee information. Are there other disclosures in the relationship summary for which we should require or permit firms to also include a question to ask as part of the disclosure? If so, which disclosures? Could firms use technology such as pop-ups or hovers, or internal links, to connect the relevant question(s) in the key questions to ask to the disclosure in the relationship summary?

- Would firms create policies and procedures, including supervision and compliance reviews, relating to how their financial professionals respond to these questions? Would implementing and maintaining such processes be burdensome or costly for firms? Why or why not? Do investment advisers and broker-dealers currently have systems in place to answer these questions, particularly the request to "do the math for me" and provide not only fee information related to the relationship and certain externalized fees, but also information about fees that are implicit to a given product?
- Do firms anticipate that they would implement recordkeeping policies and procedures to address communications between financial professionals and retail investors about the "Key Questions to Ask"? What kind of recordkeeping policies and procedures would firms anticipate implementing in order to address such communications? Should we require financial professionals to highlight these key questions when they deliver a relationship summary to a retail investor? How could the questions be highlighted when the relationship summary is delivered electronically?

- Should we require financial professionals to initiate a conversation about these key questions if the retail investor does not raise these questions?

- Should we, as proposed, permit firms to omit any of the proposed questions that are not applicable to their business, and permit firms to add additional questions for retail investors to ask about the disclosures in their relationship summaries? For example, should robo-advisers and online broker-dealers be allowed to omit the questions concerning the financial professional's relevant experience and whether the investor's primary contact is an investment adviser or broker-dealer? Should we add questions specific to investment advisers offering automated advice, such as how the robo-adviser's models are designed, including the underlying assumptions?

- Should we include any additional questions in our proposed list of questions, or remove any proposed questions? If so, what additional questions should we add, and which questions should we remove, and why? For example, instead of including a question about a financial professional's licenses and other qualifications in this section, should we instead require firms to discuss information about licensing and other qualifications in the relationship summary, including educational background, designations held, and examinations passed? Should we add a question comparing services offered with financial planning and wrap fee programs?

- Do commenters agree that including a question about a financial professional's licenses and other qualifications would provide useful information to retail investors, given the expansive list of professional designations? Should we instead permit or require financial professionals to include a list of certain licenses or other qualifications in a separate disclosure and, if so, which designations should be included?

- We are proposing to permit firms to include up to fourteen questions. Do commenters agree with this approach? Should we allow firms to include more or fewer questions?

- We are proposing to require that robo-advisers and online-only brokers include a section or page on their websites that answers each of these proposed questions, and include a hyperlink in the relationship summary to where the answers are posted. How will these advisers and broker-dealers be able to answer the fact specific questions in a generalized format on the website? Are there alternative ways in which such advisers or broker-dealers should be required to provide answers to these proposed questions? For example, should robo-advisers use a chat or other message function, or answer questions by email? Would this work for robo-advisers that offer recommendations to retail investors without providing them any way to reach a financial professional at the firm? Should we require all advisers to include the responses to these questions on their websites, including robo-advisers that make available financial professionals to answer retail investors' questions?

- Should we require the order of the questions to be fixed? Does the proposed order advance our goal? What changes, if any, should be made to the proposed order? Should there be sub-categories of questions?

C. Delivery, Updating, and Filing Requirements

Our proposal would require registered investment advisers, registered broker-dealers that serve retail customers and dual registrants to deliver a relationship summary.[307] Delivery of the relationship summary would not necessarily relieve the firm of any other disclosure obligations it

[307] *See* Advisers Act proposed rule 204-5 and Exchange Act proposed rule 17a-14.

has to its retail investors or prospective retail investors under any federal or state laws or regulations.

The relationship summary requirement would be in addition to, and not in lieu of, current disclosure and reporting requirements or other obligations for broker-dealers and investment advisers.[308] Broker-dealers are liable under the antifraud provisions of the federal securities laws for failure to disclose material information to their customers when they have a duty to make such disclosure.[309] When recommending a security, broker-dealers may be liable under the antifraud provisions if they do not give "honest and complete information" or disclose any material adverse facts or material conflicts of interest, including any economic self-interest.[310] Among other specific disclosure obligations, broker-dealers are required to disclose certain potential conflicts to their customers under certain circumstances, such as disclosing at or before the time of the completion of the transaction whether the broker-dealer is acting as agent or principal, and its compensation and any third-party remuneration it has received or will receive.[311] Broker-dealers typically provide information about their services, fees, and conflicts on their websites and in their account opening agreements. Disciplinary history on broker-

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308 For example, the relationship summary would not necessarily satisfy the disclosure requirements under proposed Regulation Best Interest. Regulation Best Interest would require broker-dealers to disclose in writing, before or at the time of a recommendation, the material facts related to the scope and terms of the relationship with the retail customer, including all material conflicts of interest that are associated with the recommendation. Regulation Best Interest Proposal, *supra* note 24, at section II.D.1 (noting that the relationship summary would reflect initial layers of disclosure, and the disclosure obligation of proposed Regulation Best Interest would reflect more specific and additional, detailed layers of disclosure).

309 *See Basic v. Levinson*, 485 U.S. 224, 239 n.17 (1988) ("Silence, absent a duty to disclose, is not misleading under Rule 10b-5."); *Chiarella v. U.S.*, 445 U.S. 222, 228 (1980) (explaining that a failure to disclose material information is only fraudulent if there is a duty to make such disclosure arising out of "a fiduciary or other similar relation of trust and confidence"); *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999) (explaining that defendant is liable under section 10(b) and rule 10b-5 for material omissions "as to which he had a duty to speak").

310 *See, e.g., De Kwiatkowski v. Bear, Stearns & Co.*, 306 F.3d at 1302; *Chasins v. Smith, Barney & Co.*, 438 F.2d at 1172.

311 17 CFR 240.10b-10(a)(2).

dealers, details on the background, qualifications, and disciplinary history of financial professionals associated with broker-dealers, and customer complaints and arbitrations against them, are available on FINRA's BrokerCheck website.[312]

Investment advisers deliver to clients a "brochure" (and/or a "wrap fee program brochure," as applicable) and "brochure supplement" required by Form ADV Part 2.[313] The brochure is a plain language, narrative document that addresses, among other things, an investment adviser's advisory business, conflicts of interest with its clients, fees, and disciplinary history.[314] The brochure supplement contains information about the advisory personnel providing clients with investment advice.[315] The wrap fee program brochure provides prospective wrap fee program clients with important information regarding the cost of the programs and the services provided. The current Form ADV Parts 1 and 2A are filed by investment advisers, and details about the background qualifications, registrations and disciplinary history of financial professionals supervised by the investment adviser, are available on IAPD.[316]

The current disclosure requirements and obligations result in varying degrees and kinds of information to investors, but we believe that all retail investors would benefit from a short

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312 *See* https://brokercheck.finra.org.

313 *See* Advisers Act rule 204-3; Instructions 1 and 2 of Instructions for Part 2A of Form ADV; Instructions 2 and 3 of Instructions for Part 2B of Form ADV. An investment adviser that sponsors a wrap fee program is generally required to complete a wrap fee program brochure. *See* Appendix 1 to Form ADV Part 2A.

314 Much of the disclosure in Part 2A addresses an investment adviser's conflicts of interest with its clients, and is disclosure that the adviser, as a fiduciary, must make to clients in some manner regardless of the form requirements. *See* Brochure Adopting Release, *supra* note 157, at 9.

315 Form ADV Part 2B includes information about certain advisory personnel on whom clients may rely for investment advice, including their educational background, disciplinary history, and the adviser's supervision of the advisory activities of its personnel. Investment advisers are not required to file with the Commission the brochure supplements required by Form ADV Part 2B. Advisers Act rules 203-1(a), 204-1(b).

316 IAPD is available at https://www.adviserinfo.sec.gov.

summary that focuses on certain key aspects of the firm and its services. By requiring both investment advisers and broker-dealers to deliver a relationship summary that discusses both types of services and their differences, the relationship summary would help all retail investors, whether they are considering an investment adviser or a broker-dealer. A relationship summary would help retail investors to understand key aspects of a particular firm, to compare different types of accounts, and to compare that firm with other firms. While the information required by the relationship summary is generally already provided in greater detail for investment advisers by Form ADV Part 2, the relationship summary would provide in one place, for the first time, summary information about the services, fees, conflicts, and disciplinary history for broker-dealers.

1. Filing Requirements

As proposed, firms would be required to file their relationship summary with the Commission, and the relationship summary will be available on the Commission's public disclosure website. The essential purpose of the relationship summary is to provide information to retail investors to help them decide whether to engage a particular firm or financial professional and open an investment advisory or brokerage account. If a firm does not have retail investor clients or customers and is not required to deliver a relationship summary to any clients or customers, the firm would not be required to prepare or file a relationship summary.[317] Broker-dealers would file their relationship summaries electronically in a text-searchable format with the Commission on EDGAR. Investment advisers would file their relationship summaries electronically in a text-searchable format through IARD in the same manner as they currently file

317 *See* proposed amended Advisers Act rule 203-1 note to paragraph (a)(1); proposed Exchange Act rule 17a-14(a), (b). *See infra* Section II.C.2 for a discussion of the delivery requirements.

Form ADV Parts 1A and 2A. Dual registrants would file on both EDGAR and IARD. All previously filed versions of relationship summaries filed via EDGAR will remain available to the public. Although previously filed versions of an adviser's relationship summary would remain stored as Commission records in IARD, only the most recent version of an adviser's relationship summary will be available through the Commission's public disclosure website.

We considered proposing other electronic filing platforms, either maintained by the Commission or by a third-party contractor. We are proposing IARD and EDGAR because they are familiar filing systems for investment advisers and broker-dealers. Investment advisers registered with the Commission file Form ADV on IARD.[318] Many broker-dealers submit documents to the Commission on EDGAR and all broker-dealers have an EDGAR CIK number.[319] As mentioned above, a dual registrant would be required to file the relationship summary on EDGAR and IARD. The information for dual registrants would be accessible through IARD or EDGAR, which are both available through the Commission's website www.Investor.gov. Exact processes for firms to follow in filing under each system is specified on the IARD system website and in the EDGAR filer manual, respectively.

There are several reasons we propose having the relationship summaries filed with the Commission. First, every relationship summary would be easily accessible through the Commission's website. The public would benefit by being able to use a central location to find any firm's relationship summary. Easy access to various relationship summaries through one source may facilitate simpler comparison across firms. Second, some firms may not maintain a

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318 Investment advisers may instead file a paper copy of the Form ADV with the Commission if they apply for a hardship exemption by filing Form ADV-H.

319 During fiscal year 2017, approximately 1,100 broker-dealers submitted documents to the Commission using EDGAR. Broker-dealers can file their annual reports on EDGAR and broker-dealers that also conduct another business activity (*e.g.*, broker-dealers that are also municipal advisers or large traders) use EDGAR for other required filings.

website, and therefore their relationship summaries would not otherwise be accessible to the public. Although we are proposing that firms without a website include a toll-free telephone number in their relationship summaries that retail investors can call to obtain up-to-date information,[320] requiring filing with the Commission will allow the public to access any firm's relationship summary. Lastly, by having firms file the relationship summaries with the Commission, the Commission can more easily monitor the filings for compliance with Form CRS.

2. Delivery Requirements

We propose to require that a firm deliver the relationship summary to each retail investor, in the case of an investment adviser, before or at the time the firm enters into an investment advisory agreement or, in the case of a broker-dealer, before or at the time the retail investor first engages the firm's services.[321] A dual registrant should deliver the relationship summary at the earlier of entering into an investment advisory agreement with the retail investor or the retail investor engaging the firm's services.[322] We encourage delivery of the relationship summary far enough in advance of a final decision to engage the firm to allow for meaningful discussion between the financial professional and retail investor, including by using the Key Questions, and for the retail investor to understand the information and weigh the available options. The delivery requirement applies to investment advisers even if the investment advisory agreement is

320 Proposed General Instruction 8.(a) to Form CRS.

321 Advisers Act proposed rule 204-5(b)(1) and Exchange Act proposed rule 17a-14(c)(1); proposed General Instruction 5.(b) to Form CRS.

322 Advisers Act proposed rule 204-5(b)(1) (investment advisers or their supervised persons must deliver to each retail investor a current Form CRS before or at the time the investment adviser enters into an investment advisory contract with the retail investors) and Exchange Act proposed rule 17a-14(c)(1) (broker-dealers must deliver to each retail investor a current Form CRS before or at the time the retail investor first engages the broker-dealer's services). *See also* proposed General Instruction 5.(b) to Form CRS.

oral, and to broker-dealers even if a transaction is executed outside of an account or without an account opening agreement, as further discussed below. In the case of paper delivery, if firms do not deliver the relationship summary as the sole document, firms should ensure that it is the first among any documents that are delivered at that time.[323] A firm would be permitted to deliver the relationship summary (including updates) electronically, consistent with the Commission's guidance regarding electronic delivery.[324] We are also proposing a requirement for firms that maintain a public website to post their relationship summaries on their websites in a way that is easy for retail investors to find.[325] Firms that do not maintain a website would be required to include in their relationship summaries a toll-free number for investors to call to obtain documents.[326]

The timing of the initial delivery of the relationship summary for investment advisers generally tracks that of Form ADV Part 2A.[327] The requirement for broker-dealers is intended to capture the earliest point in time at which a retail investor engages the services of a broker-dealer, including instances when a customer opens an account with the broker-dealer, or effects a transaction through the broker-dealer in the absence of an account, for example, by purchasing a

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323 Proposed General Instruction 8.(c) to Form CRS.

324 *See* Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information; Additional Examples Under the Securities Act of 1933, Securities Exchange Act of 1934, and Investment Company Act of 1940, Exchange Act Release No. 37182 (May 9, 1996) [61 FR 24644 (May 15, 1996)] ("96 Guidance"). *See also* Use of Electronic Media, Exchange Act Release No. 42728 (Apr. 28, 2000) [65 FR 25843 (May 4, 2000)] ("2000 Guidance"); and Use of Electronic Media for Delivery Purposes, Exchange Act Release No. 36345 (Oct. 6, 1995) [60 FR 53458 (Oct. 13, 1995)] ("95 Guidance").

325 Advisers Act proposed rule 204-5(b)(3) and Exchange Act proposed rule 17a-14(c)(3); proposed General Instruction 8.(a) to Form CRS.

326 Proposed General Instruction 8.(a) to Form CRS.

327 *See* Instruction 1 of General Instructions for Part 2A of Form ADV.

mutual fund through the broker-dealer via "check and application."[328] We believe that providing the retail investor the relationship summary at this first juncture would better assist the retail investor in making a determination whether to open an account with a broker-dealer. The rule does not require delivery to a retail investor to whom a broker-dealer makes a recommendation, if that retail investor does not open or have an account with the broker-dealer, or that recommendation does not lead to a transaction with that broker-dealer. If the recommendation leads to a transaction with the broker-dealer who made the recommendation, we would consider the retail investor to be "engaging the services" of that broker-dealer at the time the customer places the order or an account is opened, whichever occurs first.

In addition, a firm would be required to provide a relationship summary to an existing client or customer who is a retail investor before or at the time a new account is opened or changes are made to the retail investor's account(s) that would materially change the nature and scope of the firm's relationship with the retail investor.[329] Such changes would include a recommendation that the retail investor transfer from an investment advisory account to a brokerage account or from a brokerage account to an investment advisory account, or move assets from one type of account to another in a transaction that is not in the normal, customary, or already agreed course of dealing.[330] A move of assets from one type of account to another in a

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328 The obligation for a broker-dealer to deliver a relationship summary is broader than the proposed application of Regulation Best Interest, which would apply when a broker-dealer provides a recommendation. *See supra* note 29. Broker-dealers and investment advisers that offer online services would be required to provide the relationship summary to retail investors even if the only services provided to the customer or client is to offer a choice of investment options from an online menu of products, *i.e.*, even if the broker-dealer does not provide a recommendation, provided that the retail investor engages its services. *See also infra* note 337 and accompanying text.

329 Advisers Act proposed rule 204-5(b)(2) and Exchange Act proposed rule 17a-14(c)(2); proposed General Instruction 7.(a) to Form CRS.

330 Advisers Act proposed rule 204-5(b)(2) and Exchange Act proposed rule 17a-14(c)(2); proposed General Instruction 7.(a) to Form CRS.

transaction not in the normal, customary, or already agreed course of dealing could include, for example, asset transfers due to an IRA rollover; deposits or the investment of monies based on infrequent events or unusual size, such as an inheritance or receipt from a property sale; or a significant migration of funds from savings to an investment account. If a firm does not have any retail investors to whom it must deliver a relationship summary, it would not be required to prepare one.[331] A firm would be required to deliver the relationship summary to a retail investor within 30 days upon request.[332]

We are proposing different triggers for initial delivery of the relationship summary by investment advisers (before or at the time the firm enters into an investment advisory agreement with the retail investor) and by broker-dealers (before or at the time the retail investor first engages the firm's services). These proposed requirements are intended to make the relationship summary readily accessible to retail investors at the time when they are choosing investment services and are generally consistent with the approach many commenters recommended.[333] In addition, the trigger for investment advisers is consistent with current requirements for investment advisers to deliver the Form ADV Part 2 brochure.[334] A few commenters suggested that disclosures be delivered before a broker-dealer first executes a transaction based on a recommendation to a retail investor.[335] Along these lines, we believe that retail investors should

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331 Proposed General Instruction 5.(a) to Form CRS.

332 Advisers Act proposed rule 204-5(b)(5) and Exchange Act proposed rule 17a-14(c)(5); proposed General Instruction 7.(b) to Form CRS.

333 Many commenters suggested that the document be provided at the beginning of the relationship with a firm; such as before or at the time the retail investor enters into the agreement. *See, e.g.*, Stifel 2017 Letter; Equity Dealers of America 2017 Letter; Fidelity 2017 Letter; AARP 2017 Letter; State Farm 2017 Letter; AFL-CIO 2017 Letter; CFA 2017 Letter; Wells Fargo 2017 Letter.

334 An investment adviser is required to give a firm brochure to each client before or at the time the adviser enter into an advisory agreement with that client. *See* Advisers Act rule 204-3(b).

335 *See, e.g.*, SIFMA 2017 Letter.

receive the relationship summary as part of the process of engaging the services of a financial professional or firm so the retail investor has the relevant information to make that decision.[336] In particular, because broker-dealers are not required to enter into a formal agreement with a customer in order to provide services, there may be instances in which retail investors engage the services of a broker-dealer without (or before) formally opening a brokerage account (*e.g.*, by entering an agreement with the broker-dealer). For example, some broker-dealers assist their customers in purchasing mutual funds or variable insurance products to be held with the mutual fund or variable insurance product issuer, by sending checks and applications directly to the fund or issuer (this is sometimes referred to as "check and application," "application-way," "subscription-way" or "direct application" business; we use the term "check and application" for simplicity).[337] In light of these types of circumstances, we are proposing to require broker-dealers to deliver the relationship summary before or at the time the retail investor first engages the firm's services. As noted above, we would not interpret the term "engage the firm's services" to capture a recommendation by a broker-dealer to a retail investor who does not

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336 *See, e.g.*, 917 Financial Literacy Study, *supra* note 20, at iv ("Generally, retail investors prefer to receive disclosures before making a decision on whether to engage a financial intermediary or purchase an investment product or service."); Equity Dealers of America 2017 Letter, at 2 ("[W]e believe that [a relationship summary] should be a pillar to any new standard when establishing a new brokerage or advisory account relationship… Whether a client wants incidental advice, the ability to provide their own investment ideas or to direct their own transactions as associated with a brokerage account or whether a client wants ongoing advice, monitoring, and a level fee as associated with an advisory account will determine the type of account they choose."); State Farm 2017 Letter; AARP 2017 Letter; AFL-CIO 2017 Letter, at 3 ("If [a proposed enhanced standard of conduct] were supplemented by pre-engagement disclosures that briefly and clearly describe the sales nature of the broker's services, . . . investors would be modestly better off than they are today."); Fidelity 2017 Letter; Kiley 2017 Letter; CFA 2017 Letter.

337 The broker-dealer is typically listed as the broker-dealer of record on the retail investor's account application, and generally receives fees or commissions resulting from the retail investor's transactions in the account. *See, e.g.*, Transfers of Mutual Funds and Variable Annuities, FINRA Notice to Members 04-72 (Oct. 2004), *available at* http://www.finra.org/sites/default/files/NoticeDocument/p011634.pdf. *See also supra* note 328 and accompanying text.

already have an account with that broker-dealer, if that recommendation does not lead to a transaction with that broker-dealer.

We also believe that retail investors who are existing clients and customers should be reminded of the information highlighted in the relationship summary before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's existing accounts that would materially change the nature and scope of the firm's relationship with the retail investor.[338] For example, firms would be required to provide a current version of the relationship summary before or at the time a recommendation is made that the retail investor transfers from an investment advisory account to a brokerage account, transfers from a brokerage account to an investment advisory account, or moves assets from one type of account to another in a transaction not in the normal, customary or already agreed course of dealing.[339] In these instances, retail investors are again making decisions about whether to invest through an advisory account or a brokerage account and would benefit from information about the different services and fees that the firm offers to make an informed choice. Therefore, we are proposing that firms be required to deliver the relationship summary to existing retail investors before or at the time these changes occur. Whether a change would require delivery of the relationship summary would depend on the specific facts and circumstances.[340] For example, transfers among accounts that occur in the ordinary course of

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338 Advisers Act proposed rule 204-5(b)(2) and Exchange Act proposed rule 17a-14(c)(2); proposed General Instruction 7.(a) to Form CRS.

339 *Id.*

340 *Id.*

business, such as a periodic rebalancing of assets among two accounts or quarterly investments in a retirement account, would not require the delivery of a relationship summary.[341]

As with other disclosures firms must deliver, firms would be able to deliver the relationship summary (including updates) electronically, within the framework of the Commission's guidance regarding electronic delivery of documents.[342] The Commission's previously issued guidance applicable to electronic delivery of certain documents by investment advisers and broker-dealers consists of the following elements: (i) notice to the investor that information is available electronically; (ii) access to information comparable to that which would have been provided in paper form and that is not so burdensome that the intended recipients cannot effectively access it; and (iii) evidence to show delivery, *i.e.* reason to believe that electronically delivered information will result in the satisfaction of the delivery requirements under the federal securities laws.[343]

We believe that retail investors who are prospective clients or customers of a firm would benefit from receiving the relationship summary as early as possible when engaging the services of a financial professional or firm, so the retail investor has the relevant information to make that decision. Further to that goal, and in an effort to provide flexibility and recognize the proliferation of means of electronic communications that firms and retail investors may utilize, a firm would be able to deliver the relationship summary to new or prospective clients or customers in a manner that is consistent with how the retail investor requested information about

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341 *Id.*

342 Proposed General Instruction 8.(b) to Form CRS. *See* 96 Guidance, *supra* note 324.

343 96 Guidance, *supra* note 324.

the firm or financial professional.[344] This method of initial delivery for the relationship summary would be consistent with the Commission guidance.[345] With respect to existing clients or customers, firms should deliver the relationship summary in a manner consistent with the firm's existing arrangement with that client or customer and with the Commission guidance.

In connection with account openings conducted online, the Commission previously stated in its 2000 Guidance that broker-dealers could obtain consent from a new customer to electronic delivery of documents through an account-opening agreement that contains a separate section with a separate e-delivery authorization, or through a separate document altogether.[346] The Commission noted that a global consent to e-delivery would not be an informed consent if the opening of a brokerage account were conditioned upon providing the consent; in such cases other evidence of delivery would be required.[347] However, the 2000 Guidance made an exception for brokerage firms that require accounts to be opened online and all account transactions to be initiated and conducted online, stating, "In these instances only, the opening of a brokerage account may be conditioned upon providing global consent to electronic delivery."[348] We understand that for some robo-advisers, the account opening process and subsequent investment decisions and transactions may involve similarly limited interaction with a financial professional.

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344 For example, a retail investor without access to a computer or email would likely request information in person or by telephone, and the financial professional would deliver a hard copy of the relationship summary in person or by mail.

345 Firms could meet the elements of the Commission's electronic delivery guidance in other ways as well when delivering the relationship summary to new or prospective clients or customers. *See* 2000 Guidance, *supra* note 324, at 65 FR 25845-46; 96 Guidance, *supra* note 324, at 61 FR at 24647; 95 Guidance, *supra* note 324, at 60 FR at 53461.

346 2000 Guidance, *supra* note 324, at 65 FR 25846.

347 *Id*. Evidence of delivery could include, for example: obtaining evidence that an investor actually received the information such as by electronic mail return receipt or confirmation of access, downloading, or printing; an investor's accessing a document with hyperlinking to a required document; or using other forms or material available only by accessing the information. *See* 1995 Guidance, *supra* note 324, at section II.C.

348 *Id.* at n.27.

Therefore, it would be consistent with the Commission's prior guidance if firms that offer only online account openings and account transactions, including robo-advisers and online broker-dealers, made global consent to electronic delivery a condition of account opening, for purposes of delivering the relationship summary.

We request comment on whether the Commission should provide additional guidance with respect to electronic delivery of the relationship summary to new and prospective or existing clients and customers.

3. Updating Requirements

The relationship summary is designed to provide information to assist retail investors in making a decision about whether to engage a firm and open a particular type of account, but it is also important for retail investors to know when there have been changes to this information to inform their continuing choice to keep their account with the firm. For example, as noted above, the staff's 917 Financial Literacy Study indicates that retail investors find the nature and scope of a firm's services, its fees and conflicts of interest, and the disciplinary history of financial professionals to be important in choosing financial intermediaries.[349] To the extent that this information changes in a material way, existing clients and customers should be made aware so that they can decide whether the choice of that particular firm or financial professional remains appropriate and consistent with their decision-making criteria. Therefore, we are proposing to require a firm to update its relationship summary within 30 days whenever the relationship summary becomes materially inaccurate.[350] Firms also would be required to post the latest version on their websites (if they have one), and electronically file the relationship summary with

349 *See* 917 Financial Literacy Study, *supra* notes 20-21 and accompanying text.

350 Advisers Act proposed rule 204-1(a)(2) and Exchange Act proposed rule 17a-14(b)(3); proposed General Instruction 6.(a) to Form CRS.

the Commission.[351] We believe this approach is consistent with the current requirements for investment advisers to update the Form ADV Part 2 brochure,[352] and with broker-dealers' current obligations, including to update Form BD if its information is or becomes inaccurate for any reason, which information generally would be made available through EDGAR.[353] We believe allowing 30 days for firms to make updates provides sufficient time for firms to make the necessary changes and gives the benefit of certainty of when the updates must be made.

Our proposal would also require firms to communicate without charge the information in an amended relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made.[354] Firms could communicate this information by delivering the amended relationship summary or by communicating the information another way to the retail investor.[355] For example, if an investment adviser communicated a material change to information contained in its relationship summary to a retail investor by delivering an amended Form ADV brochure or Form ADV summary of material changes containing the updated information, this would support a reasonable belief that the information had been communicated to the retail investor, and the investment adviser would not be required to deliver an updated relationship summary to that retail investor. This requirement provides firms the ability to disclose changes without requiring them to duplicate disclosures and

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351 Advisers Act proposed rules 203-1(a)(1), 204-5(b)(3) and Exchange Act proposed rule 17a-14(b)(2), 17a-14(c)(3); proposed General Instructions 5.(a), 6.(c) and 8 to Form CRS.

352 *See, e.g.,* Advisers Act proposed rule 204-5(b)(4) and Exchange Act proposed rule 17a-14(a)(3); proposed General Instruction 6 to Form CRS. Generally, an investment adviser registered with the SEC or a state securities authority is required to amend its Form ADV promptly if information it provided in its brochure becomes materially inaccurate. *See* Advisers Act rule 204-1(a)(2); Instruction 4 of General Instructions to Form ADV.

353 *See, e.g.,* Exchange Act rule 15b3-1.

354 Advisers Act proposed rule 204-5(b)(4) and Exchange Act proposed rule 17a-14(c)(4); proposed General Instruction 6.(b) to Form CRS.

355 *Id.*

incur additional costs. A retail investor also would be able to find the latest version of the relationship summary on the firm's website, if it has one, and firms would be required to deliver it upon the retail investor's request.[356]

For purposes of this requirement, it is important that broker-dealers identify their existing customers who are retail investors and recognize that a customer relationship may take many forms. For example, under this requirement, a broker-dealer would be required to provide the relationship summary to customers who have so-called "check and application" arrangements with the broker-dealer, under which a broker-dealer directs the customer to send the application and check directly to the issuer. We believe this approach would facilitate broker-dealers building upon their current compliance infrastructure in identifying existing customers[357] and would enhance investor protections to retail investors engaging the financial services of broker-dealers.

Finally, our proposal would require a firm to file its relationship summary with the Commission and to maintain the relationship summary and all updates as part of its books and records and make it available to Commission staff upon request, as discussed in Section IV below.[358]

We request comment on filing, delivery, and updating requirements generally, and on the following areas specifically:

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356 Advisers Act proposed rules 204-5(b)(3) and 204-5(b)(5) and Exchange Act proposed rules 17a-14(c)(3) and 17a-14(c)(5); proposed General Instructions 7 and 8 to Form CRS.

357 For example, broker-dealers may already have compliance infrastructure to identify customers pursuant to FINRA's suitability rule, which applies to dealings with a person (other than a broker or dealer) who opens a brokerage account at a broker-dealer or who purchases a security for which the broker-dealer receives or will receive, directly or indirectly, compensation even though the security is held at an issuer, the issuer's affiliate or custodial agent, or using another similar arrangement. *See* Guidance on FINRA's Suitability Rule, FINRA Regulatory Notice 12-55 (Dec. 2012), at Q6(a), *available at* http://finra.complinet.com/net_file_store/new_rulebooks/f/i/FINRANotice12_55.pdf.

358 *See* Advisers Act proposed rule 204-2(a)(14)(i) and Exchange Act proposed rule 17a-3(a)(24).

- Does this approach to filing, delivery, and updating create unique challenges for firms that are providing the relationship summary electronically? Does this approach provide retail investors with ready access to the information that they need and want in connection with the decision to engage a broker-dealer or investment adviser?
- Should a relationship summary be required for all investment advisers, broker-dealers and dual registrants that provide services to retail investors, or should there be any exceptions? For example, should execution-only broker-dealers be excluded from the requirement to provide the relationship summary because they do not provide investment advice to their customers? Should clearing broker-dealers be excluded from the requirement to prepare and deliver the relationship summary to the extent their customers are introduced by an introducing broker-dealer pursuant to a clearing agreement? If so, why? Should the Commission consider any other exclusions for clearing broker-dealers or other entities? If so, why?
- Should a clearing broker-dealer and introducing broker-dealer be allowed to agree to allocate the responsibility to deliver the relationship summary pursuant to applicable self-regulatory rules?[359] Should investment advisers with sub-advisory relationships be allowed to receive the relationship summary, and any updated information in relationship summaries, from the sub-advisers, on behalf of the primary investment adviser's clients? Should such clients receive the relationship summary of the sub-adviser?
- Should the relationship summary be required in addition to firms' existing disclosure requirements, as proposed? Is the relationship summary duplicative of or does it conflict

[359] *See, e.g.*, FINRA Rule 4311(c) (Carrying Agreements) (requiring each carrying agreement in which accounts are to be carried on a fully disclosed basis to specify the responsibilities of each party to the agreement), available at http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=10028.

with any existing disclosure requirements in any way? What, if any, changes would we need to make to the relationship summary if we were to permit its delivery in lieu of other disclosures and why would those changes be appropriate? Should the Commission instead make any changes to existing rules to permit the relationship summary to serve as the venue for disclosures required by those rules?

- Should investment advisers that deliver a relationship summary have different delivery requirements for the Form ADV brochure and brochure supplement?
- Is IARD the optimal system for investment advisers to file Form CRS with the Commission? Is EDGAR the optimal system for broker-dealers to file Form CRS with the Commission? Should dual registrants be required to file on both EDGAR and IARD?[360] Should broker-dealers instead be required to file Form CRS solely through IARD? What would be the costs or benefits associated with broker-dealers becoming familiar with and filing through IARD system rather than through EDGAR? Is there another method of electronic filing the Commission should consider for Form CRS and why? If broker-dealers should file using a system other than EDGAR, what would be the costs and benefits associated with creation of, and/or becoming familiar with and filing through, that system? Should investment advisers and broker-dealers be required to file on the same system?

- How important to investors and other interested parties is the fact that IAPD serves as the single public disclosure website to access an adviser's current filings with the

[360] *See* proposed General Instruction 5.(a) to Form CRS.

Commission, and compare certain filings of other advisers? What would be the impact of retail investors having to access a separate website for the relationship summary?

- How should the relationship summary be filed? Should it be filed as a text-searchable PDF, similar to how Form ADV is currently filed? Would a structured PDF, a web-fillable form, HTML, XML, XBRL, Inline XBRL or another format be more appropriate, and why? Should the Commission require a single, specified format for all firms, require one format for EDGAR filings and another format for IARD filings, or permit filers to select from two or more possible formats? Would retail investors use the relationship summary to obtain information about one particular firm, or to compare information among firms? What type of format would make it easier for retail investors to use the relationship summary in these ways? For example, would retail investors seek to compare the information about fees across a number of firms, and if so, would a structured format, such as XML or Inline XBRL or an unstructured format, such as PDF or HTML, better facilitate such a comparison? Which filing formats would illustrate the formatting of relationship summaries that are provided electronically, for example, relationship summaries sent in the body of an email, posted on the firm's website, or formatted for a mobile device? Which formats might be most beneficial to retail investors?
- What time or expense is associated with particular formats? What time or expense would be required of the public to view disclosures in a particular format? Would open source, freely available formats be preferred by users and filers, or would commercial proprietary formats be preferred? Would a particular format require any filers or users to license commercial software they otherwise would not, and, if so, at what expense? Would a

particular format or formats provide more or fewer features with respect to comparability, reusability, validation, or analysis? What other considerations are related to specific formats? Would a particular format make it possible to confirm that a firm complied with the Form CRS requirements and validate the information provided before filing? If so, which format would filers or users find the most useful?

- We propose to require that an investment adviser deliver the relationship summary before or at the time the firm enters into an investment advisory agreement with a retail investor or, in the case of a broker-dealer, before or at the time the retail investor first engages the firm's services. Would this requirement give a retail investor ample time to process the information and ask questions before entering into an agreement? Or should we require that the relationship summary be delivered a certain amount of time before the firm enters into an agreement with a retail investor (*e.g.*, 48 hours or a 15 minute waiting period)? For broker-dealers, should we require delivery of the relationship summary at the earlier of a recommendation or engagement, as opposed to just engagement? We also propose that a broker-dealer would not need to deliver the relationship summary to a retail investor to whom a broker-dealer makes a recommendation, if that retail investor does not open or have an account with the broker-dealer, or that recommendation does not lead to a transaction with that broker-dealer. Should we instead require that broker-dealers deliver the relationship summary to prospective customers regardless of whether that leads to a transaction or account opening?
- Would the delivery requirements applicable to firms that offer only online account openings, investment advice, and transactions provide sufficient notice to retail investors of the relationship summary's availability and content? Should the Commission require

such firms to ensure that the relationship summary is delivered separately from other disclosures, with additional prominence and emphasis? For example, should firms consider employing the technology to require a retail investor to scroll through the entirety of the relationship summary before entering the next stage in the account opening process, accessing a different part of the website in order to obtain more information, or permitting the retail investor to check a box in order to accept the client agreement? Are there other requirements that should be considered for such firms in the delivery of the relationship summary when entering into the brokerage or advisory relationship, when the nature of that relationship changes, or when updates to the relationship summary are made?

- We also propose to require that a firm deliver a relationship summary before or at the time the firm implements changes that would materially change the nature and scope of the existing relationship with a retail investor, for example by the opening of an additional account or accounts and/or the migration of assets from one account type to another. Should the Commission provide more guidance for what might constitute a material change to the nature and scope of the relationship or the moving of a significant amount of assets from one type of account to another? If so, do commenters have suggestions on how the Commission should interpret "material change to the nature and scope of the relationship" and "significant amount of assets"? Should the delivery of the relationship summary under these circumstances be accompanied by additional oral disclosures or other types of supplemental information? Would this requirement give retail investors sufficient opportunity to process the information and ask questions before

the changes are made? Should we specify how far in advance a firm should deliver the relationship summary before making such changes?

- Should we require that firms deliver an updated relationship summary to retail investors periodically (*e.g.*, quarterly, semi-annually or annually) or whenever there is a material change, as proposed, such as a change in fees or commission structure?
- We propose to require that a firm deliver the relationship summary to a retail investor upon request. Would that requirement be helpful for retail investors? Would that requirement be burdensome for firms? Should we require firms to deliver the relationship summary upon request by *any* investor, not just retail investors and any trust or other similar entity that represents natural persons?
- We propose to require broker-dealers to initially deliver the relationship summary "before or at the time the retail investor first engages the firm's services." Would the proposed formulation capture instances where a retail investor engages the services of a broker-dealer to carry out a transaction outside of an account, for example, by purchasing a mutual fund or variable annuity product through the broker-dealer via "check and application"? We do not intend to capture instances in which a broker-dealer makes a recommendation to a retail investor who does not already have an account with that broker-dealer, if that recommendation does not lead to a transaction with that broker-dealer. Would such recommendations be captured by the proposed language? Would a different formulation be clearer (*e.g.*, "before or at the time the retail investor first enters a relationship," or "before or at the time the retail investor engages in a transaction or opens an account, whichever occurs first," or "before or at the time the retail investor indicates an intent to open an account or engage in a transaction, whichever occurs

first")? Why or why not? Should the delivery requirements for investment advisers and broker-dealers be identical? Why or why not?

- For investment advisers, our proposal generally tracks the initial delivery requirements for Form ADV Part 2.[361] Should we instead follow a different disclosure delivery requirement? Should we adopt a different delivery requirement, recognizing that the purpose of the relationship summary is to provide information to retail investors to help them decide whether to engage a particular firm and open an investment advisory or brokerage account?
- We propose to permit firms to deliver the relationship summary electronically consistent with prior Commission guidance on electronic delivery, as discussed above. Is the guidance clear on how firms may meet their obligations with respect to delivering the relationship summary, or should we provide more guidance? Should any additional guidance be more or less prescriptive? Would our proposed approach adequately protect investors who have no internet access or limited internet access or who prefer not to receive information about firms electronically? Is the guidance workable for a disclosure delivered at or before the retail investor enters into an agreement with an investment adviser or first engages the services of a broker-dealer?
- Should we permit firms to meet their relationship summary obligations by filing their relationship summary with the Commission or by posting it online without giving or sending it to specific retail investors?
- Should firms also be required to notify retail investors that an updated relationship summary is available online? Should we require firms to highlight the information that

[361] *See* Advisers Act rule 204-3.

has changed since the prior version in an updated relationship summary? If firms communicate the changes in the relationship summary by means other than delivery of the updated relationship summary, should they be required to inform existing retail investors that the existing version is outdated? Are there additional requirements that we should consider for amendments to relationship summaries, particularly for firms without a website?

- How can we encourage the prominence of the relationship summary for retail investors? We are proposing that, if the relationship summary is delivered on paper and not as a standalone document, firms should ensure that it is the first among any other materials or documents that are delivered at that time. Should we require that the relationship summary be given greater prominence than other materials that accompany it in some other way or that the relationship summary not be bound together with any of those materials? Should we impose additional requirements to encourage the prominence and separateness of the relationship summary? Should we include additional or different requirements for relationship summaries that are delivered electronically? Should we require that the entire text of the relationship summary be provided in the text of an email or other form of electronic messaging, instead of an attachment or a link to the summary disclosure on the firm's website? Are there more dynamic ways to present the relationship summary information online, such as with the use of tool tips, explanatory videos, or chat bots to provide answers to questions? Are there other ways of increasing the prominence of the relationship summary, whether delivered in paper format or electronically?

- Should we require a financial professional to make certain oral disclosures at time of delivery? For example, should we require that a financial professional ask the retail investor if he or she has any questions about the relationship summary? How would this be satisfied in the context of a primarily or exclusively online or electronic delivery?
- Should a firm be required to communicate any material changes made to the relationship summary within 30 days, as proposed, or sooner, for example in the case of transactions not in the normal, customary, or already agreed course of dealing? Should a firm have the option of choosing to communicate the new information by either filing an amended Form CRS or by communicating the new information to retail investors in another way? Should we provide more guidance on the types of ways in which the information may be communicated? Should we instead require a firm to deliver an amended relationship summary to its existing retail investors?
- Are there other changes in conditions that should trigger a delivery requirement?
- We are proposing that firms that do not maintain a website include in their relationship summaries a toll-free phone number for investors to call to obtain documents. Are there additional requirements or different approaches that we should consider for firms that do not maintain websites, to make it easier for the public to access their relationship summaries?

D. Transition Provisions

To provide adequate notice and opportunity to comply with the proposed relationship summary filing requirements, newly registered broker-dealers and new applicants for registration with the Commission as investment advisers would not be required to file or deliver their relationship summaries until the date six months after the effective date of the proposed new

rules and rule amendments.[362] After that date, newly registered broker-dealers would be required to file their Form CRS with the Commission by the date on which their registration with the Commission becomes effective, and the Commission would not accept any initial application for registration as an investment adviser that does not include a relationship summary that satisfies the requirements of Form ADV, Part 3: Form CRS.[363]

Similarly, we believe it would be helpful to provide sufficient time for advisers and broker-dealers already registered with us to prepare the new Form CRS and file it electronically with the Commission. Accordingly, we propose to require a broker-dealer that is registered with us as of the effective date of the proposed new rules and rule amendments to comply with the new Form CRS filing requirements by the date that is six months after the effective date of the proposed new rules and rule amendments.[364] We also propose requiring an investment adviser or a dual registrant that is registered with us as of the effective date to comply with the new filing requirements as part of the firm's next annual updating amendment to Form ADV that is required after six months after the rule's effective date.[365] Such an adviser or dual registrant would be required to include Form CRS as part of its next such annual updating amendment filing with the Commission.[366]

We are proposing to require that a firm deliver its relationship summary to all of its existing clients and customers who are retail investors on an initial one-time basis within 30 days

362 *See* Advisers Act proposed rule 203-1(a)(2) and Exchange Act proposed rule 17a-14 (f)(1).

363 *See* Advisers Act proposed rule 203-1(a)(2) and Exchange Act proposed rule 17a-14(f)(3).

364 *See* Exchange Act proposed rule 17a-14(f)(1); proposed General Instruction 5.(c)(i) to Form CRS.

365 *See* Advisers Act proposed rule 204-1(b)(3); proposed General Instruction 5.(c)(i) to Form CRS.

366 *See id*.

after the date the firm is first required to file its relationship summary with the Commission.[367] This proposed requirement would allow existing retail investor clients and customers to receive the important disclosures in the relationship summary that will be provided to new and prospective retail investor customers and clients. A firm would be required to give its relationship summary to its new and prospective clients and customers who are retail investors beginning on the date the firm is first required to electronically file its relationship summary with the Commission, and would be required to give the relationship summary to its existing clients and customers who are retail investors within 30 days, pursuant to the rule's requirements for initial delivery and updating.[368]

We request comment on our proposed implementation requirements.

- Would a six-month period from the effective date of Form CRS provide enough time for newly registered broker-dealers and investment advisers that are filing their initial applications for registration with the Commission to complete Form CRS? If not, please explain why and how much time these advisers and broker-dealers would need to complete Form CRS.
- Should implementation of Form CRS filing requirements for broker-dealers be on a separate timetable from implementation of Form CRS filing requirements for investment advisers, as we have proposed, because registered investment advisers are not all required to file their Form ADV annual updating amendments on the same timetable? If not, please explain why and whether, in order to have one

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367 *See* Advisers Act proposed rule 204-5(e)(1) and Exchange Act proposed rule 17a-14(f)(2); proposed General Instruction 5.(c)(iii) to Form CRS.

368 *See* Advisers Act proposed rule 204-5(e) and Exchange Act proposed rule 17a-14(f)(1), (2); proposed General Instruction 5.(c)(ii), (iii) to Form CRS.

uniform initial filing date for broker-dealers and investment advisers, we should require investment advisers to potentially file their initial Form CRS more than once.

- Should a firm be required to comply with the rule's requirements for initial delivery to new and prospective clients and customers and for updating beginning on the date the firm is first required to electronically file its relationship summary with the Commission, as proposed? Should a firm deliver the relationship summary to all existing clients and customers who are retail investors within 30 days after first filing the relationship summary with the Commission, as proposed? These requirements would result in a different delivery timetable for broker-dealers and investment advisers because investment advisers would file Form CRS with their Form ADV annual updating amendments. Should we instead require all firms to deliver the relationship summary to retail investors beginning on the same date (*e.g.*, within six months from the effective date of Form CRS), even if investment advisers file Form CRS after that date? Or should we require firms to deliver to existing retail investor customers and clients initial relationship summaries at a later date? For example, firms could be required to deliver the relationship summary only before or at the time a new account is opened or changes are made to the retail investor's account(s) that would materially change the nature and scope of the firm's relationship with the retail investor (including before or at the time the firm recommends that the retail investor transfers from an investment advisory account to a brokerage account or from a brokerage account to an investment advisory account, or moves assets

from one type of account to another in a transaction not in the normal, customary or already agreed course of dealing).

E. Recordkeeping Amendments

We are also proposing conforming amendments to Advisers Act rule 204-2 and Exchange Act rules 17a-3 and 17a-4, which set forth requirements for maintaining, making and preserving specified books and records, to require SEC-registered investment advisers and broker-dealers to retain copies of each relationship summary.[369] Firms would also be required to maintain each amendment to the relationship summary as well as to make and preserve a record of dates that each relationship summary and each amendment was delivered to any client or to any prospective client who subsequently becomes a client, as well as to any retail investor before such retail investor opens an account.[370] Requiring maintenance of these disclosures as part of the firm's books and records would facilitate the Commission's ability to inspect for and enforce compliance with firms' obligations with respect to Form CRS.

These proposed changes are designed to update the books and records rules in light of our proposed addition of Form ADV Part 3 for registered investment advisers and Form CRS for broker-dealers, and they mirror the current recordkeeping requirements for the Form ADV brochure and brochure supplement. The records for investment advisers would be required to be maintained in the same manner, and for the same period of time, as other books and records required to be maintained under rule 204-2(a), and the records for broker-dealers would be

369 Advisers Act proposed rule 204-2(a)(14)(i); Exchange Act proposed rules 17a-3(a)(24) and 17a-4(e)(10).

370 *Id.*

required to maintained for a period of six years.[371] The proposed required documentation, like other records, would be required to be provided to the staff "promptly" upon request.[372]

We request comment on these proposed amendments.

- Are there other records related to the relationship summary or its delivery that we should require firms to keep? Should we require them to maintain copies of the relationship summary for a longer or shorter period than we have proposed? Should broker-dealers and investment advisers be required to keep relationship summary-related records for the same amount of time? Should firms be required to document their responses to the "key questions" from investors?

III. RESTRICTIONS ON THE USE OF CERTAIN NAMES AND TITLES AND REQUIRED DISCLOSURES

As discussed above, both broker-dealers and investment advisers provide investment advice to retail investors, but the regulatory regimes and business models under which they give that advice are different. For example, the principal services, compensation structures, conflicts, disclosure obligations, and legal standards of conduct can differ.[373] We therefore believe that it is vital that retail investors understand whether the firm is a registered investment adviser or registered broker-dealer, and whether the individual providing services is associated with one or the other (or both), so that retail investors can make an informed selection of their financial professional, and then appropriately monitor their financial professional's conduct.

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371 *See* Advisers Act rule 204-2(e)(1); Exchange Act rule 17a-4(e)(10). Pursuant to Advisers Act rule 204-2(e)(1), investment advisers will be required to maintain the relationship summary for a period of five years, while Exchange Act proposed rule 17a-4(e)(10) would require broker-dealers to maintain the relationship summary for a period of six years.

372 *See* Advisers Act rule 204-2(g)(2); Exchange Act rule 17a-4(j).

373 *See, e.g.*, 913 Study, *supra* note 3.

While investors should understand who their financial professional is, and why that matters, studies indicate that retail investors do not understand these differences and are confused about whether their firm or financial professional is a broker-dealer or an investment adviser, or both.[374] Proposed Form CRS, as set out in Section II above, should help to ameliorate this confusion by helping retail investors understand the services that a particular firm offers, and how those services differ based on whether the firm is a registered broker-dealer, registered investment adviser, or both. We preliminarily believe, however, that Form CRS is not a complete remedy for investor confusion. The education and information that Form CRS provides to retail investors could potentially be overwhelmed by the way in which financial professionals present themselves to potential or current retail investors, including through advertising and other communications. This could particularly be the case where the presentation could be misleading in nature, or where advertising and communications precede the delivery of Form CRS and may have a disproportionate impact on shaping or influencing retail investor perceptions.

Specifically, we believe that certain names or titles used by broker-dealers, including "financial advisor," contribute to retail investor confusion about the distinction among different firms and investment professionals, and thus could mislead retail investors into believing that they are engaging with an investment adviser – and are receiving services commonly provided by an investment adviser and subject to an adviser's fiduciary duty, which applies to the retail

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374 *See, e.g.*, Siegel & Gale Study, *supra* note 5; RAND Study, *supra* note 5; 913 Study, *supra* note 3. Additionally, the RAND Study noted that participants "commented that the interchangeable titles and 'we do it all' advertisements [by broker-dealers] made it difficult to discern broker-dealers from investment advisers." Those participants also stated that these lines were further blurred by the marketing efforts which depicted an "ongoing relationship between the broker and the investor…." *See* RAND Study, *supra* note 5, at xix, 19.

investors' entire relationship–when they are not.[375] Additionally, broker-dealers and investment advisers, and the financial professionals that are associated with them, currently engage in communications with prospective or existing retail investors without making clear whether they are a broker-dealer or an investment adviser, which can further confuse retail investors if this distinction is not clear from context (whether intentionally or not).

As discussed below, our proposed restriction seeks to mitigate the risk that the names or titles used by a firm or financial professional result in retail investors being misled, including believing that the financial professional is a fiduciary, leading to uninformed decisions regarding which firm or financial professional to engage, which may in turn result in investors being harmed. Additionally, we believe that requiring firms and their associated natural persons or supervised persons to disclose whether the firms are broker-dealers or investment advisers and whether such financial professionals are associated with or supervised by, respectively, such firms would also help to address investor confusion and mitigate potential harm to investors resulting from that confusion. We preliminarily believe that restricting certain persons from using the term "adviser" or "advisor" coupled with the requirement that firms disclose their regulatory status in retail investor communications would deter potentially misleading sales practices. Investors who understand whether their financial professional or firm is a broker-dealer or investment adviser will be better consumers of the information presented in Form CRS, and less likely to mistakenly obtain the services of a broker-dealer when they intend to engage an investment adviser, or vice versa.[376]

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375 *See supra* notes 122 and 216 and accompanying texts.

376 Section 15(l)(2) of the Exchange Act and section 211(h)(2) of the Advisers Act.

A. Investor Confusion

Over the past decade, various studies have documented that retail investors are confused regarding the services offered by, and the standards of conduct applicable to, broker-dealers and investment advisers, including their use of certain titles.[377]

In 2005, the Siegel & Gale Study found that with respect to titles specifically, "[r]espondents in all focus groups were generally unclear about the distinctions among the titles brokers, financial advisors/financial consultants, investment advisers, and financial planners…"[378] The following year, the Commission retained RAND to conduct a study of broker-dealers and investment advisers for the purpose of examining, among other things, whether investors understood the duties and obligations owed by investment advisers and broker-dealers.[379] The RAND Study noted that "thousands of firms" are structured in a variety of ways and provide various different combinations of services and products.[380] The RAND Study concluded that "partly because of this diversity of business models and services, investors typically fail to distinguish broker-dealers and investment advisers along the lines defined by federal regulations."[381]

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377 *See*, *e.g.*, Siegel & Gale Study, *supra* note 5; RAND Study, *supra* note 5; 913 Study, *supra* note 3.

378 *See* Siegel & Gale Study, *supra* note 5, at 2. The study used focus groups in both Baltimore, MD and Memphis, TN to "explore investor opinions regarding the services, compensation and legal obligations of several types of financial services professionals." *Id.*, at 5.

379 *See* RAND Study, *supra* note 5, at xiv. In conducting the study, RAND used several methods to study current practices in the financial industry and analyze whether investors understand differences between types of financial service professionals. Among these methods, RAND sent out national household surveys through the internet which studied "household investment behavior and preferences, experience with financial service providers, and understanding of the different types of financial service providers." Additionally, RAND conducted six focus groups with investors in Alexandria, Virginia, and Fort Wayne, Indiana to gain additional evidence on investor beliefs about and experience with financial service providers. RAND also conducted two sets of [in person] interviews: one set of interviews with interested parties and one set with financial service firms. *See* RAND Study, *supra* note 5, at 3 – 4.

380 *See* RAND Study, *supra* note 5, at 118.

381 *Id.*

The RAND Study concluded that, based on interviews with industry representatives, investor surveys, and focus groups, there was generally investor confusion about the distinction between broker-dealers and investment advisers. In particular, "[interview] participants [in the RAND Study] mentioned that the line between investment adviser and broker-dealers has become further blurred, as much of the recent marketing by broker-dealers focuses on the ongoing relationship between the broker and the investor and as brokers have adopted such titles as 'financial advisor' and 'financial manager.'"[382] Additionally, participants in RAND's survey believed that financial professionals using the title "financial advisor" were "more similar to investment advisers than to brokers…"[383]

Moreover, focus group participants shed further light on this confusion when they "commented that the interchangeable titles and 'we do it all' advertisements by broker-dealers made it difficult to discern broker-dealers from investment advisers."[384] More specifically, focus group participants observed that "common job titles for investment advisers and broker-dealers are so similar that people can easily get confused over the type of professional with which they are working."[385] The focus group results also showed that when "[c]omparing beliefs on services provided by investment advisers to services provided by brokers, participants were more likely to say that investment advisers provide advice about securities, recommend specific investments, and provide planning services."[386] According to the RAND Study, focus-group participants were more likely to say that brokers rather than investment advisers execute stock transactions and

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382 *See id.*, at 19.

383 *See id.*, at xix.

384 *See id.*, at xix. Interview participants also stated that these lines were further blurred by the marketing efforts which depicted an "ongoing relationship between the broker and the investor….". *See id.*, at 19.

385 *See id.*, at 111.

386 *See id.*, at 109.

earn commissions and believed "that investment advisers and brokers are required to act in the client's best interest" and "were more likely to say that brokers rather than investment advisers are required to disclose any conflicts of interest."[387] In highlighting part of the confusion, the RAND Study noted that the responses from survey participants indicated the opposite conclusion from those of the focus-group participants, namely, that investment advisers are more likely to disclose conflicts of interest.[388]

As discussed above, in light of significant intervening market developments and advances in technology, Chairman Clayton in 2017 invited input on, among other things, investor concerns about the current regulatory framework. Commenters highlighted the risk of harm to investors who obtain services from broker-dealers under the misimpression that they are receiving services protected by the fiduciary duty that applies to investment advisers.[389] For example, one commenter examined the websites of nine different brokerage firms and "found that the firms' advertising presents the image that the firms are acting in a fiduciary capacity" with many firm advertisements continuing to present the firm "as providing all-encompassing advice, with no differentiation between the firms' investment adviser services and brokerage services."[390] This commenter also noted that "[w]ithout uniform standards, persons seeking financial advice are left to fend for themselves in deciding whether their financial advisor is serving two masters or

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387 *Id.*

388 *Id.*

389 *See, e.g.*, CFA 2017 Letter; PIABA 2017 Letter; IAA 2017 Letter; Pefin 2017 Letter; First Ascent 2018 Letter.

390 *See* PIABA 2017 Letter, at 7. *See also* IAA 2017 Letter, at 11 ("investor confusion persists where certain financial professionals are permitted to use terms such as "financial adviser" or "financial advisor" that imply a relationship of trust and confidence but, in effect, disclaim fiduciary responsibility for such a relationship"); Pefin 2017 Letter, at 3 (noting that "'Investment Advisor' or 'Financial Advisor' are not defined terms, and are currently a "catch all" for firms with wildly different practices, standards, and responsibilities to their clients. Many of these firms attempt to imply in external communication that they are a Fiduciary, while disclaiming their responsibilities in the fine print."); CFA 2017 Letter.

only one, and whether one of those masters is the advisor's financial self-interest."[391] In addition, a different commenter argued that the use of certain titles, such as "advisor," should be standardized by the Commission because they are currently "catch all" terms for firms with "wildly different practices, standards, and responsibilities to their clients."[392] Some of the commenters to Chairman Clayton's Request for Comment also noted that this confusion is the result of the misleading nature of these titles. Specifically, one commenter stated that "[t]he problem is that investors are being misled into relying on biased sales recommendations as if they were objective, best interest advice and are suffering significant financial harm as a result."[393] The commenter noted that "these titles and marketing materials are misleading" [if] … broker-dealers truly are the "mere salespeople they've claimed to be in their legal challenge to the DOL fiduciary rule."[394] A different commenter stated that "a financial professional should not be able to use a title that conveys a standard of conduct to which the professional is not in fact held under the law…."[395] Additionally, another commenter noted that customer confusion is "also driven by misleading marketing and misleading titles."[396] Finally, one commenter stated that "having SEC registered entities and their agent, claim such title gives false credence and implies a responsibility which the agent never claims to provide (numerous brokers go by the title 'Financial Advisor', implying Fiduciary standard that is not being upheld)."[397]

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391 *See* PIABA 2017 Letter, at 17.

392 *See* Pefin 2017 Letter, at 3. *See also* First Ascent 2017 Letter.

393 *See* CFA 2017 Letter, at 2.

394 *See id.*, at 11.

395 *See* Comment letter of the U.S. Chamber of Commerce (Dec. 13, 2017), at 10.

396 *See* Comment letter of the Steering Group for the Committee for the Fiduciary Standard (Nov. 8, 2017) ("Committee for the Fiduciary Standard 2017 Letter"), at 3.

397 *See* Pefin 2017 Letter, at 9.

For many years, the Commission has considered approaches for remedying investor confusion about the differing services and obligations of broker-dealers and investment advisers. In particular, in 2005 we considered addressing how investors perceive the differences between broker-dealers and investment advisers by proposing to proscribe the use of certain broker-dealer titles.[398] In adopting our final rule, which was subsequently vacated on other grounds by the Court of Appeals for the D.C. Circuit,[399] we declined to follow this approach, believing that the better approach was to require broker-dealers to clearly inform their customers receiving investment advice that they are entering into a brokerage, and not an advisory, relationship.[400] However, in light of comments in response to Chairman Clayton's Request for Comment and our experience, we believe that it is appropriate to revisit that approach.

A broker-dealer can, and does, provide investment advice to retail investors without being regulated as an investment adviser, provided that such advice is "solely incidental to" its brokerage business and the broker-dealer receives no "special compensation" for the advice.[401]

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398 Certain Broker-Dealers Deemed Not To Be Investment Advisers, Exchange Act Release No. 50980 (Jan. 6, 2005), [70 FR 2716 (Jan. 14, 2005)] ("Broker Dealer Reproposing Release").

399 *Financial Planning Association v. Securities and Exchange Commission*, 482 F.3d 481 (D.C. Cir. 2007).

400 As further discussed in the 2005 final rule release, we considered but did not adopt a rule which would have placed limitations on how a broker-dealer may hold itself out or titles it may employ without registering as an investment adviser and complying with the Advisers Act. In deciding to not prohibit the use of specific titles such as "financial advisor," "financial consultant" or other similar names, we noted that "the statutory broker-dealer exception is a recognition by Congress that a broker-dealer's regular activities include offering advice that could bring the broker-dealer within the definition of investment adviser, but which should nonetheless not be covered by the Act." As a result, we noted that the "terms 'financial advisor' and 'financial consultant,' for example, were descriptive of such services provided by broker-dealers." We also stated our view that these titles were generic terms that describe what various persons in the financial services industry do, including banks, trust companies, insurance companies, and commodity professionals. *See* 2005 Broker Dealer Release, *supra* note 7; *see also* Broker Dealer Reproposing Release, *supra* note 398.

401 The Advisers Act regulates the activities of certain "investment advisers," which are defined in section 202(a)(11) as persons who receive compensation for providing advice about securities as part of a regular business. Broker-dealers are excluded from the definition of investment adviser by section 202(a)(11)(C) provided that they meet two prongs: (i) the broker-dealer's advisory services must be "solely incidental to" its brokerage business; and (ii) the broker-dealer must receive no "special compensation" for the advice.

While we believe such advice is important for providing retail investors access to a variety of services, products, and payment options, for example, thereby increasing investor choice, we are concerned that use of the terms "adviser" and "advisor" in a name or title would continue to result in some retail investors being misled that their firm or financial professional is an investment adviser (*i.e.* a fiduciary), resulting in investor harm. We believe that these terms can obscure the fact that investment advisers and broker-dealers typically have distinct business models with varying services, fee structures, standards of conduct, and conflicts of interest.[402]

It is important for retail investors to better understand the distinction between investment advisers and broker-dealers and to have access to the information necessary to make an informed choice and avoid potential harm. Investor choices of firm type and financial professionals can, for example, affect the extent or type of services received, the amount and type of fees investors pay for such services, and the conflicts of interest associated with any such services. For example, if a retail investor prefers an advisory relationship with an active trading strategy, and he or she mistakenly retains a broker-dealer "financial adviser," this investor potentially could incur more costs if he or she is placed in a brokerage account than he or she would have paid in an advisory account with an asset-based fee. Likewise, an investor could also be misled into believing that the broker-dealer is subject to a fiduciary standard that may not apply, [403] and

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402 *See* RAND Study, *supra* note 5, at 18 ("There were also concerns as to what investors understand regarding similarities and differences of brokerage and advisory accounts, the legal obligations of each type of account, and the effect of titles and marketing used by investment professionals on the expectations of investors.").

403 *See supra* note 375. *Cf.* Comment letter of Russel Walker (Jun. 17, 207); Comment letter of Jeanne Davis (Jul. 20, 2017); Comment letter of Nancy Lowell (Jul. 20, 2017); Comment letter of John Dalton (Jul. 21, 2017); Comment letter of Nancy Tew (Jul. 21, 2017); Comment letter of Bonitta Knapp (Jul. 21, 2017); Comment letter of Alan Gazetski (Jul. 21, 2017); Comment letter of A. Arias (Jul. 21, 2017); Comment letter of Al Cohen (Jul. 21, 2017); Comment letter of James Melloh (Jul. 21, 2017); Comment letter of Mary Pellecchia (Jul. 21, 2017); Comment letter of William Muller (Jul. 21, 2017); Comment letter of Susan Lee (Jul. 22, 2017); Comment letter of Steve Daniels (Jul. 22, 2017); AARP 2017 Letter; AFL-CIO 2017 Letter; Pefin 2017 Letter; PIABA 2017 Letter; IAA 2017 Letter; CFA 2017 Letter. These

provides services it may not offer, such as regular monitoring of the account, offering advice on a regular basis, and communicating with the investor on a regular basis.

While we are proposing to require broker-dealers and investment advisers to provide retail investors with a relationship summary that would highlight certain features of an investment advisory or brokerage relationship, that information might be provided *after* the retail investor has initially decided to meet with the firm or its financial professional. The retail investor may make a selection based on such person's name or title. If firms and financial professionals that are not investment advisers are restricted from using "adviser" or "advisor" in their names or titles, retail investors would be less likely to be confused or potentially misled about the type of financial professional being engaged or nature of the services being received. Conversely, an associated natural person of a broker-dealer using the term "adviser" or "advisor" may result in an investor believing that such financial professional is an adviser with a fiduciary duty, as discussed in the relationship summary the investor would receive.[404] Similarly, requiring firms and their associated natural persons or supervised persons, as applicable, to disclose whether the firms are broker-dealers or investment advisers would help to address investor confusion and complement the information provided in the proposed relationship summary.

B. Restrictions on Certain Uses of "Adviser" and "Advisor"

We are proposing to restrict any broker or dealer, and any natural person who is an associated person of such broker or dealer, when communicating with a retail investor, from using as part of its name or title the words "adviser" or "advisor" unless such broker or dealer, is

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commenters argued that as a result of the use of certain titles and communications, retail investors are confused and are erroneously led to believe that their financial professionals are required to act "in their best interest."

404 *See* proposed Item 5.B.3. of Form CRS.

registered as an investment adviser under the Advisers Act or with a state, or any natural person who is an associated person of such broker or dealer is a supervised person of an investment adviser registered under section 203 of the Advisers Act or with a state and such person provides investment advice on behalf of such investment adviser.[405]

1. Firms Solely Registered as Broker-Dealers and Associated Natural Persons

In relevant part, the proposed rule would restrict a broker-dealer's or its associated natural persons' use of the term "adviser" or "advisor" as part of a name or title when communicating with a retail investor in particular circumstances.[406] This would include names or titles which include, in whole or in part, the term "adviser" or "advisor" such as financial advisor (or adviser), wealth advisor (or adviser), trusted advisor (or adviser), and advisory (*e.g.*, "Sample Firm Advisory") when communicating with any retail investor. In addition, we believe that the proposed rule should apply to communications with retail investors (*i.e.*, natural persons), rather than institutions, for reasons similar to those detailed above for the relationship summary.[407] Additionally, our proposed rule appropriately applies to retail investors and not to institutions, as institutions generally would be less likely to be misled by such names or titles. The proposed rule, however, would not restrict a broker-dealer's or its associated natural persons' use of the terms "adviser" or "advisor" when acting on behalf of a bank or insurance company, or when acting on behalf of a municipal advisor or a commodity trading advisor.

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405 *See* Exchange Act proposed rule 15l-2.

406 *See id*.

407 *See supra* note 29 and accompanying text. *See also* Exchange Act proposed rule 15l-2(b).

We acknowledge that there may be titles other than "adviser" or "advisor" used by financial professionals that might confuse and thus potentially mislead investors. We considered whether we should restrict broker-dealers from using additional terms, such as, for example, "financial consultant." Given this concern, we focused our proposal on the terms "adviser" or "advisor" because they are more closely related to the statutory term "investment adviser." Thus, as compared to additional terms such as "financial consultant," "adviser" and "advisor" are more likely to be associated with an investment adviser and its advisory activities rather than with a broker-dealer and its brokerage activities. Moreover, the term "investment adviser," as compared to terms like "financial consultant," is a defined term under the Advisers Act as any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities.[408] As discussed above, we believe that use of the terms "adviser" and "advisor" by broker-dealers and their associated natural persons has particularly contributed to investor confusion about the typical services, fee structures, conflicts of interest, and legal standards of conduct to which broker-dealers and investment advisers are subject.[409] Conversely, we preliminarily believe that other terms, even if investors might find them confusing, unclear, or misleading (as some commenters have suggested), do not necessarily imply that a firm or

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408 *See* section 202(a)(11)(A) of the Advisers Act, defining an "investment adviser" as "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities."

409 *See supra* note 402 and accompanying text. We are not proposing restrictions on names or titles for investment advisers. Our staff is not aware of an investment adviser using a name or title that could cause retail investors to mistakenly believe that such adviser provides brokerage services. Studies and commenters also have not identified retail investor confusion as relating to an investment adviser's use of names or titles. We request comment on our understanding below.

its financial professional is an "investment adviser" who would have the principal services, compensation structures, conflicts of interest, disclosure obligations, and legal standards of conduct that are typically associated with being an investment adviser.[410]

Accordingly, we preliminarily do not believe these terms would cause retail investors to believe that their financial professional is an investment adviser when he or she is, in fact, a broker-dealer. We therefore preliminarily believe that restricting use of terms that are similar to "investment adviser" appropriately tailors the rule to terms that are likely to result in confusion or mislead retail investors about whether such broker-dealer is an investment adviser and thus a fiduciary.

As we discuss in more detail above, the proposed relationship summary is designed to provide clarity to retail investors regarding information about broker-dealers and investment advisers under a prescribed set of topics (*e.g.*, services, fees, standards of conduct, conflicts). While the proposed relationship summary is designed to help retail investors to distinguish between investment advisers and broker-dealers, we are concerned that the effectiveness of the relationship summary could be undermined if we do not restrict a broker-dealer from using in a name or title the terms "adviser" and "advisor."

For instance, we preliminarily believe that restricting a broker-dealer or its associated natural persons from using "adviser" or "advisor" in a name or title would

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410 Firms and financial professionals should keep in mind the applicability of the antifraud provisions of the federal securities laws, including section 17(a) of the Securities Act, and section 10(b) of the Exchange Act and rule 10b-5 thereunder, to the use of names or titles. *See also generally* FINRA Rule 2210 (stating in part "[a]ll retail communications and correspondence must: (A) prominently disclose the name of the member, or the name under which the member's broker-dealer business primarily is conducted as disclosed on the member's Form BD, and may also include a fictional name by which the member is commonly recognized or which is required by any state or jurisdiction; (B) reflect any relationship between the member and any non-member or individual who is also named; and (C) if it includes other names, reflect which products or services are being offered by the member.")

mitigate the risk that a retail investor would be misled into believing and expecting that his or her "financial advisor," – who may solely provide brokerage services at a broker-dealer – is an *investment adviser* because of the name or title. For example, if a retail investor were to engage a financial professional with the title "wealth advisor" who solely provides brokerage services but who is associated with a dually registered firm,[411] such investor would likely receive the dually registered firm's relationship summary. The relationship summary would include a description of both business models; however, the retail investor could incorrectly match the services he or she would receive from such "wealth advisor" to the description in the relationship summary of *investment advisory* services. As a result, the retail investor may be misled to believe that the brokerage services provided by the "wealth advisor" are in fact the investment advisory services as described in the relationship summary.

Similarly, a retail investor who engages a financial professional with the title "wealth advisor" who is associated solely with a broker-dealer entity would likely receive the broker-dealer's relationship summary, which focuses on the characteristics of the *broker-dealer* business model. As a result, there would be an inconsistency between the description of the broker-dealer business model and the investors' likely perceptions that their professional is an investment adviser. Therefore, the proposed restriction on the use of names or titles would increase the effectiveness of the relationship summary by reducing the risk of a mismatch between investor preferences and type of services received.

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411 For the purposes of Section III, we are defining a "dually registered firm" in the same manner as it is defined in the baseline of the Economic Analysis. *See infra* Section IV, note 453.

We acknowledge that studies have demonstrated that many retail investors select financial professionals and firms based on personal referrals by family, friends, or colleagues.[412] Even if the name or title of the firm or professional may not impact choices made by such investors, we preliminarily believe that the protections offered to other investors by the proposed restriction and disclosure requirements justify the rules.

2. Dually Registered Firms and Dual Hatted Financial Professionals

The proposed rule would permit firms that are registered both as investment advisers (including state-registered investment advisers) and broker-dealers to use the term "adviser" or "advisor" in their name or title.[413] The proposed rule would, however, only permit an associated natural person of a dually registered firm to use these terms where such person is a supervised person of a registered investment adviser *and* such person provides investment advice on behalf of such investment adviser.[414] This would limit the ability of natural persons associated with a broker-dealer who do not provide investment advice as an investment adviser from continuing to use the term "adviser" or "advisor" simply by virtue of the fact that they are associated with a dually registered firm.[415] We discuss these aspects of the rule in further detail below.

a. Dually Registered Firms

We are not proposing to apply the restriction to dually registered firms. We believe that it is inappropriate to restrict a dually registered firm from using a name or title that accurately describes its registration status. We recognize that under our proposed rule there might be

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412 *See infra* note 546 and accompanying text. *See also* Section IV.A.3.g.

413 *See* Exchange Act proposed rule 15l-2(a)(1).

414 *See* Exchange Act proposed rule 15l-2(a)(2).

415 *See* section 202(a)(25) of the Advisers Act [15 U.S.C. 80b-2(a)(25)] defining "supervised person" as "any partner, officer, director (or other person occupying a similar status or performing similar functions), or employee of an investment adviser, or other person who provides investment advice on behalf of the investment adviser and is subject to the supervision and control of the investment adviser".

occasions where a dually registered firm provides a particular retail investor only brokerage services, which could lead to some investor confusion.

At the firm level, we do not believe that the determination of when the restriction applies should be based on what capacity a dually registered firm is acting in a particular circumstance, *i.e.*, whether a dually registered firm is acting solely as a broker-dealer and not offering investment advisory services. If we were to apply the restriction in this manner, it could result in firms using multiple names and titles, which may lead to further confusion and create operational and compliance complexities. Accordingly, this could lead to dually registered firms avoiding the use of the title "adviser" or "advisor" unless they believe they would *always* offer investment advisory services, which we believe is not necessary to avoid the potential investor harm. Additionally, we also seek to avoid the potential misimpression that may result should a firm use a name or title to reflect only its brokerage services and not its investment advisory services. In such a circumstance, a retail investor may not know that such firm offers both business models and could be led to believe that only brokerage services are available.

b. Dual Hatted Financial Professionals

Dual hatted financial professionals of dually registered firms (including state-registered investment advisers) can provide brokerage services, advisory services, or both. We believe it is appropriate for financial professionals that provide services as an investment adviser to retail investors to be permitted to use names or titles which include "adviser" and "advisor," even if, as a part of their business, they also provide brokerage services. As such, our proposed rule would not restrict, for example, a financial professional that is both a supervised person of an investment adviser and an associated person of a broker-dealer from using the term "adviser" or "advisor" in his or her name or title if such person provides investment advice to retail investors

on behalf of the investment adviser.[416] We believe that the relationship summary can sufficiently reduce the risk of investors being misled and avoid investor harm because it contains parallel information with respect to each of the services the dual hatted financial professional offers.

By contrast, we recognize that some financial professionals of dually registered firms only provide brokerage services. We are concerned that if these financial professionals use "adviser" or "advisor" in their names or titles, retail investors may be misled about the nature of services they are receiving, and may incorrectly believe that such person would provide them investment advisory services rather than brokerage services. Therefore, we believe that a financial professional who does not provide investment advice to retail investors on behalf of the investment adviser, *i.e.*, a financial professional that only offers brokerage services to retail investors, should be restricted from using the title "adviser" or "advisor" despite such person's association with a dually registered firm.

We recognize that, as with dually registered firms, some dual hatted financial professionals may under some circumstances only offer brokerage services to a particular retail investor, which has the potential to cause confusion. For the same reasons discussed above regarding dually registered firms, however, we do not believe that the determination of when the restriction applies should be based on what capacity a dual hatted financial professional is acting in a particular circumstance, *i.e.*, whether a dual hatted professional is offering only brokerage services to that particular investor and not offering investment advisory services.[417] Moreover, we are proposing in Regulation Best Interest to require a broker-dealer to make certain

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416 *See* Exchange Act proposed rule 15l-2(a)(2).

417 *See supra* note 410. Firms and financial professionals should keep in mind the applicability of the antifraud provisions of the federal securities laws, including section 17(a) of the Securities Act, and section 10(b) of the Exchange Act and rule 10b-5 thereunder, to the use of names or titles.

disclosures, including the capacity of the financial professional and firm.[418] We request comment below on whether and if so how the proposed rule should address this particular circumstance.

C. Alternative Approaches

Over the past decade, we and commenters have expressed concern about broker-dealer marketing efforts, including through the use of titles, and whether these efforts are consistent with a broker-dealer's reliance on the exclusion from the definition of investment adviser under section 202(a)(11)(C) of the Advisers Act.[419] Under section 202(a)(11)(C), a broker-dealer is excluded from the definition of investment adviser if its "performance of [advisory] services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor."[420] In this regard, and as an alternative to our proposed rule today, we considered proposing a rule which would have stated that a broker-dealer that uses the term "adviser" or "advisor" as part of a name or title cannot be considered to provide investment advice solely incidental to the conduct of its business as a broker-dealer and therefore is not excluded from the definition of investment adviser under section 202(a)(11)(C). We also considered proposing a rule that would preclude a broker-dealer from relying on the exclusion when such a broker-dealer held itself out as an investment adviser. We are not proposing these alternatives for the reasons discussed below. However, we request comment on these alternatives below.

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418 See Regulation Best Interest Proposal, *supra* note 24.

419 *See, e.g.*, Comment letter of Investment Counsel Association of America (Feb. 7, 2005) ("ICAA 2005 Letter); Comment letter of T. Rowe Price (Feb. 22, 2005) ("T. Rowe Price 2005 Letter") on Broker Dealer Reproposing Release, *supra* note 398. *See also* Certain Broker-Dealers Deemed Not to Be Investment Advisers, Exchange Act Release No. 42099 (Nov. 4, 1999) ("Release 42099").

420 Section 202(a)(11)(C) of the Advisers Act.

Our concerns regarding broker-dealer marketing efforts are not new. For example, we have previously requested comment on whether we should preclude broker-dealers from relying on the solely incidental prong of the exclusion if they market their services in a manner that suggests that they are offering advisory accounts, including through the use of names or titles.[421] While we have never viewed the broker-dealer exclusion as precluding a broker-dealer from marketing itself as providing some amount of advisory services, we have noted that these marketing efforts raised "troubling questions as to whether the advisory services are not (or would be perceived by investors not to be) incidental to the brokerage services."[422] Certain commenters have voiced similar concerns, arguing that the use of certain titles, such as "financial advisor," is inconsistent with the broker-dealer exclusion, with some noting that the marketing of advisory services by a broker-dealer is inconsistent with those services being solely incidental to the brokerage business.[423] Others, however, contended that the titles are consistent with the services provided by broker-dealers, whether in fee-based or commission-based accounts.[424]

Taking into account our concerns and the views of commenters, we considered proposing a rule which would have stated that a broker-dealer that uses the term "adviser" or "advisor" as part of a name or title would not be considered to provide investment advice solely incidental to the conduct of its brokerage business and therefore would not be excluded from the definition of investment adviser under section 202(a)(11)(C) of the Advisers Act.[425] In considering this

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421 *See, e.g.*, Release 42099, *supra* note 419.

422 *See id.*

423 *See, e.g.*, ICAA 2005 Letter; T. Rowe Price 2005 Letter. *See also e.g.* AFL-CIO 2017 Letter; CFA 2017 Letter; Comment letter of CFA Institute (Jan. 10, 2018); Comment letter of The Committee for the Fiduciary Standard (Jan. 12, 2018).

424 *See* Broker Dealer Reproposing Release.

425 As with the proposal, our alternative approach would likewise preclude an associated natural person of a dually registered firm from using the term "adviser" or "advisor" in a name or title unless he or she is a

alternative, we questioned whether a broker-dealer that uses these terms to market or promote its services to retail investors is doing so because its advice is significant or even instrumental to its brokerage business. Consequently, we questioned whether that broker-dealer's provision of advice is therefore no longer solely incidental to its brokerage business. Similarly, we believe that if a broker-dealer invests its capital into marketing, branding, and creating intellectual property in using the terms "adviser" or "advisor" in its name or its financial professionals' titles, the broker-dealer is indicating that advice is an important part of its retail investor broker-dealer business. As compared to the more principles-based "holding out" approach below, this alternative may offer more certainty and clarity to broker-dealers. It also specifically addresses our concerns about the use of "adviser" and "advisor," as discussed in this release.

We also considered a broader approach that would have precluded a broker-dealer from relying on the solely incidental exclusion of section 202(a)(11)(C) if a broker-dealer "held itself out" as an investment adviser to retail investors.[426] For example, "holding out" could encompass a broker-dealer that represented or implied through any communication or other sales practice (including through the use of names or titles) that it was offering investment advice to retail investors subject to a fiduciary relationship with an investment adviser. As with our alternative approach above, we questioned whether these activities could suggest, or could reasonably be understood as suggesting, that such broker-dealer or its associated natural persons were performing investment advisory services in a manner that was not solely incidental to their business as a broker-dealer. In particular, this approach could reduce the risk that if we restricted

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supervised person of an investment adviser and provides investment advice on behalf of such investment adviser.

426 *See* AFL-CIO 2017 Letter, at 3 (stating that "[o]ne way for the SEC to proceed is to clarify that those firms that offer advisory services, or hold themselves out as offering such services, cannot take advantage of the existing broker-dealer 'solely incidental to' exemption from the Investment Advisers Act."); IAA 2017 Letter; AICPA 2017 Letter.

certain titles (or limited the use of certain titles used to market services) other potentially misleading titles could proliferate. Certain commenters to Chairman Clayton's Request for Comment also supported this approach, so that retail investors receiving advice from firms "holding out" as investment advisers would receive appropriate protections, either under the Advisers Act or through a heightened standard of conduct for broker-dealers.[427] However, we preliminarily believe that a "holding out" approach would create uncertainty regarding which activities (and the extent of such activities) would be permissible. Such an approach could also reduce investor choice, as broker-dealers may decide to provide fewer services out of an abundance of caution.

We are not proposing any of these approaches however, because we preliminarily believe that a restriction on the use of "adviser" and "advisor" in names and titles in combination with the requirement to deliver a relationship summary would be a simpler, more administrable approach to address the confusion about the difference between investment advisers and broker-dealers, and to prevent investors from being potentially misled, compared to the alternatives presented above. While we acknowledge that there are other titles or marketing communications that may contribute to investor confusion or mislead investors, our proposal is tailored toward creating greater clarity with respect to the names and titles that are most closely related to the statutory term investment adviser. In particular, our proposed rule, in combination with the

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427 *See* IAA 2017 Letter, at 11 ("We urge the Commission to address this source of investor confusion by prohibiting firms or individuals from holding themselves out as trusted advisers without being subject to either the Advisers Act fiduciary principles or a new equally stringent best interest standard under the Exchange Act, discussed above."). *See also, e.g.* AFL-CIO 2017 Letter, at 3 ("clarify that those firms that offer advisory services, or hold themselves out as offering such services, cannot take advantage of the existing broker-dealer "solely incidental to" exemption from the Investment Advisers Act. Permitting brokers to rely on this exemption when engaged in advisory activities has had the effect of exempting them from the fiduciary duty appropriate to that advisory role. Adopting this approach would require the SEC to determine what constitutes "holding out" as an adviser, addressing marketing practices, as well as job titles, that create the reasonable expectation among investors that they will receive advice and not just sales recommendations.").

relationship summary, would help distinguish between who is and who is not an investment adviser and allow retail investors to select the business model that best suits their financial goals. The restriction of the use of the terms "adviser" and "advisor" that we are proposing is intended to augment protections provided to investors by applicable provisions of the federal securities laws. Broker-dealers and their natural associated persons can face liability for intentionally, recklessly, or negligently misleading investors about the nature of the services they are providing through, among other things, materially misleading advertisements or other communications that include statements or omissions, or deceptive practices or courses of business.[428]

We request comment generally on our proposed restriction on the use of certain titles and in particular on the following issues:

- Given the required relationship summary, is it necessary to impose any restrictions on the use of names or titles?
- Do you agree with our proposed restriction on the use of "adviser" and "advisor"? Why or why not? To what extent does the disclosure provided in Form CRS complement our proposed restriction? To what extent could it be a substitute?
- Is our approach too broad or too narrow? Are there additional terms that we should explicitly include in the rule? For example, do any of the following names or titles have the potential to confuse investors about the differences between investment advisers and broker-dealers: wealth manager; financial consultant; financial manager; money manager; investment manager; and investment consultant? Why or why not? What are the names or titles most commonly used that have the potential for investor confusion? Should we consider restricting the

[428] *See, e.g.*, rule 10b-5 under the Securities Exchange Act and section 17(a) of the Securities Act.

use of names, titles, or terms that are synonymous with "adviser" or "advisor" and if so, what would those names, titles, or terms be?

- Do commenters believe that names or titles are a main factor contributing to investor confusion and the potential for investors to be misled, or are there other more significant factors? For example, do particular services offered by broker-dealers contribute to, or primarily cause, investor confusion and the potential for the broker-dealer's customers to be misled into believing that the broker-dealer is an investment adviser? If so, which services specifically? For example, do commenters believe that retirement and financial planning is more often associated with investment advisers rather than broker-dealers or vice versa? Additionally, do commenters believe that monitoring is more often associated with investment advisers than broker-dealers or vice versa?
- Our proposed rule does not apply to financial professionals of a broker-dealer when acting in the capacity, for example, as an insurance broker on behalf of an insurance company or a banker on behalf of a bank. Do you believe our proposed rule is clear that such persons are excluded from the restriction? If not, how should we provide such clarification?
- As discussed above, our proposed rule would not prohibit dually registered firms from using the term "adviser" or "advisor" in their name or title. However, it would restrict the use of such names or titles by some associated natural persons and supervised persons of those firms, depending on whether they provide investment advice to retail investors on behalf of the investment adviser. Do you agree with our proposed approach? Is there investor confusion concerning what

capacity a dually registered firm, a dual hatted financial professional, or an associated or supervised person of a dually registered firm is acting in when communicating with a retail investor? If such confusion exists, how should we address it, in addition to the proposed relationship summary? For example, are retail investors confused about which type of account their financial professional is referring to when he or she makes a particular recommendation? If this is a source of confusion, how should we address it (*e.g.*, should we address it through affirmative disclosures of account types in account statements or another form of disclosure)?

- Given the prevalence of dually registered firms and their associated dual hatted financial professionals, do retail investors typically believe they are engaging a financial professional who is solely a broker-dealer or investment adviser, or do investors understand that such person is a dual hatted professional and therefore may be able to engage with them as a broker-dealer and an investment adviser? Or do retail investors currently not understand enough to distinguish among these options in any meaningful manner?
- Do commenters believe that retail investors will understand that there is, and will continue to be under proposed Regulation Best Interest, differences in the standards of conduct, compensation structures, and services offered (among other items) depending on the capacity in which such professional engages a retail investor?
- We are proposing to permit or restrict financial professionals associated with dually registered firms from using the term "adviser" or "advisor" in their name

or title based on whether they provide investment advice on behalf of such investment advisers. Are there alternatives we should consider in implementing this portion of the rule? For example, should we only allow a supervised person to use such names or titles where "a substantial part of his or her business consists of rendering investment supervisory services" to retail investors, based upon a facts and circumstances determination?[429]

- Our proposed rule would not prohibit dually registered firms or dually hatted financial professionals from using "adviser" or "advisor" in their names or titles, even in circumstances where the firm or financial professional provides only brokerage services to a particular retail investor. Do you agree with our approach? Why or why not? For example, should the proposed rule's application depend on the capacity in which a financial professional engages a particular retail investor? If so, should financial professionals use multiple titles that would vary based on the capacity in which they are acting, and what titles would they use? Are there compliance challenges associated with this approach? Conversely, would this discourage dually registered firms or dually hatted financial professionals from using any title with "adviser" or "advisor," even when they are providing advisory services? Would this discourage dually hatted financial professionals from providing brokerage services? Would a firm use different names or titles for different subsets of their financial professionals?

[429] *See* section 208(c) of the Advisers Act: "[i]t shall be unlawful for any person registered under section 203 of this title to represent that he is an investment counsel or to use the name 'investment counsel' as descriptive of his business unless (1) his or its principal business consists of acting as investment adviser, and (2) a substantial part of his or its business consists of rendering investment supervisory services."

- Do you agree that the use of the terms "adviser" or "advisor" by broker-dealers are the main sources of investor confusion? If so, what do these terms confuse investors about (*e.g.*, the differences as to the standard of conduct their financial professional owes, the duration of the relationship, fees charged, compensation)? Are investors harmed by this confusion? If so, how? Do you agree that "adviser" and "advisor" are often associated with the statutory term "investment adviser"? Do you believe that retail investors understand what the terms "adviser" and "broker-dealer" mean and can correctly identify what type of financial professional they have engaged?
- We understand that the terms "adviser" or "advisor" are included in some professional designations earned by financial professionals.[430] We also understand that particular professional designations have been an area of concern for FINRA and NASAA.[431] Should we include an exception to permit the use of professional designations that use the terms "adviser" or "advisor"? What factors should the Commission consider if it were to include such an exception? For example, should such an exception be conditioned on prominent disclosure that the individual is not an investment adviser or supervised by one?
- Do you agree with the proposed approach in Exchange Act proposed rules 15l-2 and 15l-3 and Advisers Act proposed rule 211h-1 of limiting our proposed rules

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430 *See* FINRA, Professional Designations, *available at* https://www.finra.org/investors/professional-designations.

431 *See* Senior Designations, FINRA Notice 11-52 (Nov. 2011), *available at* http://www.finra.org/sites/default/files/NoticeDocument/p125092.pdf; NASAA, *NASAA Model Rule on the Use of Senior –Specific Certifications and Professional Designations* (Mar. 20, 2008), *available at* http://www.nasaa.org/wp-content/uploads/2011/07/3-Senior_Model_Rule_Adopted.pdf.

to "retail investors" where such persons are defined to include all natural persons as discussed above?[432] Should we instead exclude certain categories of natural persons based on their net worth or income level, such as accredited investors,[433] qualified clients[434] or qualified purchasers?[435] If we did exclude certain categories of natural persons based on their net worth, what threshold should we use for measuring net worth? Should we exclude certain categories of natural persons for other reasons?

- Should we conform the definition of retail investor to the definition of retail customer as proposed in Regulation Best Interest, which would include non-natural persons, provided the recommendation is primarily for personal, family, or household purposes? What kind of compliance burdens would it create to base Form CRS delivery off of a definition of retail investor that only included recommendations primarily for personal, family, or household purposes?_ Should the definition of retail investor include trusts or similar entities that represent natural persons, as proposed? Are there other persons or entities that should be covered? Should we expand the definition to cover plan participants in workplace retirement plans who receive services from a broker-dealer or investment adviser for their individual accounts within a plan?
- What costs would broker-dealers impacted by our proposed rule incur as a result of having to rebrand themselves and their financial professionals along with

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432 *See supra* notes 28-32 and accompanying text.

433 *See supra* note 66.

434 *See supra* note 67.

435 *See supra* note 68.

revising their communications? Are there means to mitigate such costs? Would the costs differ if we made the broker-dealer exclusion in the Advisers Act unavailable to broker-dealers that use the terms "adviser" or "advisor"?

- How would broker-dealers and associated natural persons of broker-dealers who would be impacted by our proposed rule change the way they market themselves or communicate with retail investors as a result of our proposed rule? Would this cause any other changes to their business? For example, would more broker-dealer firms also register with the Commission or the states as investment advisers as a result of our proposed rule? Will firms exit the brokerage business as a result of our proposed rule? Would more associated natural persons of broker-dealers become dual hatted?
- Would our proposed rule impact the marketing and communications of dually registered firms and their professionals in any manner? If so, how?
- Do investment advisers and their supervised persons also use names, titles, or professional designations that can lead or contribute to retail investor confusion? If so, please provide examples of these names or titles and how they can lead or contribute to confusion. Should we restrict investment advisers and their supervised persons from using these names or titles?
- What costs would our proposed restriction on certain names and titles impose? Are there greater or lower costs associated with our proposed rules as compared to alternative approaches that consider whether certain titles or marketing practices are consistent with advice being "solely incidental" to the firm's brokerage activities and thus permissible for a firm relying on the broker-dealer

exclusion from the Advisers Act? If so, what are the specific cost estimates of each approach and the components of those estimates? Are there ways to mitigate their impact and if so, what methods could be taken? Are there operational and compliance challenges associated with our proposed approach as compared to the alternatives approaches, and if so, what are they?

- We request comment on the alternative approach in which a broker-dealer would not be considered to provide investment advice solely incidental to the conduct of its brokerage business if it uses the term "adviser" or "advisor" to market or promote its services and would instead treat such practices as indicating that the broker-dealer's advisory services are not "solely incidental" to its conduct of business as a broker-dealer. What would be the advantages or disadvantages of using this approach instead of the approach we have proposed? Would the alternative approach address and mitigate investor confusion about the differences between broker-dealers and investment advisers? Would the alternative approach reduce the likelihood that investors may be misled as to the type of firm they are engaging with and therefore make an uninformed decision? Would the alternative approach have other effects on the analysis of when advisory activities are or are not solely incidental to brokerage activities? How would this alternative approach impact dually registered firms and dual hatted financial professionals? Are there operational and compliance challenges associated with this approach, and if so, what are they? How would broker-dealers and associated natural persons of broker-dealers impacted by the alternative approach change the way they market

themselves or communicate with retail investors as a result of our proposed rule? Would this cause any other changes to their business?

- Would the alternative approach discussed above that would preclude a broker-dealer or an associated natural person of a broker-dealer from relying on the broker-dealer exclusion of section 202(a)(11)(C) of the Advisers Act if it "held itself out" as an investment adviser address investor confusion? What would be the advantages or disadvantages of using this approach instead of the approach we have proposed? Which communications or level of advice do you think imply that a broker-dealer or its associated natural person is "holding out" as an investment adviser? How would an approach that focuses on "holding out" as an investment adviser impact access to advice from different kinds of firms, and how retail investors pay for this advice? How would this approach affect competition? Would this "holding out" approach address any confusion that may arise from broker-dealer marketing efforts focusing on the ongoing relationship between the broker and the investor? Are there operational and compliance challenges associated with this approach, and if so, what are they?
- Instead of a prohibition or restriction on the use of certain terms, should we permit such terms but require broker-dealers and their associated natural persons other than dual registrants and dual hatted financial professionals to include a disclaimer in their communications that they are *not* an investment adviser or investment adviser representative, respectively, each time they use or refer to the term "adviser" or "advisor"? Would this approach address investor confusion or mitigate the likelihood that investors may be misled when broker-dealers and their

associated natural persons use the term "adviser" or "advisor"? Should this approach be coupled with an affirmative obligation that a dually registered broker-dealer or its dual hatted associated natural persons disclose that it is an investment adviser or an investment adviser representative, respectively, when using terms *other than* "adviser" or "advisor"? Would this requirement discourage broker-dealers from using these terms even if they were not prohibited? How would this approach impact our proposed rule requiring disclosure of the firm's regulatory status and the financial professional's association with the firm? How would this approach impact dually registered firms and dually hatted financial professionals? Are there operational and compliance challenges associated with this approach, and if so, what are they?

- We recognize that the term "adviser" is used differently in connection with the regulation of investment advisory services provided to workplace retirement plans and IRAs under ERISA and the prohibited transaction provisions of the Internal Revenue Code. For example, a statutory exemption for the provision of investment advice to participants of ERISA-covered workplace retirement plans and IRAs, and related DOL regulations, define the term "fiduciary adviser" broadly to include a variety of persons acting in a fiduciary capacity in providing investment advice, including investment advisers registered under the Advisers Act or under state laws, registered broker-dealers, banks or similar financial institutions providing advice through a trust department, and insurance

companies, and their affiliates, employees and other agents.[436] Given that there are definitions of "adviser" under other federal regulations that capture entities and individuals who are not regulated under the Advisers Act, would a restriction on the use of the term "adviser" that applies only to registered broker-dealers and their registered representatives contribute to investor confusion or result in conflicting regulations, and possibly increased compliance burdens, or affect competition?

- What would be the effect on competition by prohibiting broker-dealers from using these terms? What would be the effect on competition by the alternative approaches described?

D. Disclosures about a Firm's Regulatory Status and a Financial Professional's Association

We are also proposing rules under the Exchange Act and the Advisers Act to require a broker-dealer and an investment adviser registered under section 203 to prominently disclose that it is registered as a broker-dealer or investment adviser, as applicable, with the Commission in print or electronic retail investor communications.[437] We are also proposing as part of our proposed Exchange Act rule to require an associated natural person of a broker or dealer to prominently disclose that he or she is an associated person of a broker-dealer registered with the

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436 *See* ERISA § 408 (g)(11)(A); Code § 4975(f)(8)(J)(i) and 29 CFR 2550.408g-1. In addition, under the DOL's BIC Exemption, the term "Adviser" would mean an *individual* who is an employee or other agent (including a registered representative) of a state or federally registered investment adviser, registered broker-dealer, bank or similar financial institution, or an insurance company. *See* Corrected BIC Exemption, *infra* note 504, section VIII(a).

437 *See* Exchange Act proposed rule 15l-3(a) and Advisers Act proposed rule 211h-1(a). We note that in Form ADV investment advisers are required to state that registration with the Commission does not imply a certain level of skill or training. *See* Item 1.C. of Form ADV Part 2A. We are requesting comment on whether we should require broker-dealers and investment advisers to include this statement in addition to disclosing their applicable regulatory status.

Commission in print or electronic retail investor communications.[438] In addition, we are proposing as part of our Advisers Act rule to require a supervised person of an investment adviser registered under section 203 to prominently disclose that he or she is a supervised person of an investment adviser registered with the Commission in print or electronic retail investor communications.[439] For example, an investment adviser registered with the Commission would prominently disclose the following on its print or electronic communications: "[Name of Firm], an investment adviser registered with the Securities and Exchange Commission" or "[Name of Firm], an SEC-registered investment adviser." Dually registered firms would similarly be required to prominently disclose both registration statuses in their print or electronic communications, for example: "[Name of Firm], an SEC-registered broker-dealer and SEC-registered investment adviser." Similarly, an associated natural person of a broker-dealer would prominently disclose the following, for example, on his or her business card or signature block: "[Name of professional], a [title] of [Name of Firm], an associated person of an SEC-registered broker-dealer." Alternatively, a supervised person of an investment adviser would prominently disclose the following on, for example, his or her business card or signature block: "[Name of professional], a [title] of [Name of Firm], a supervised person of an SEC-registered investment adviser." Finally, a financial professional who is both an associated person of a broker-dealer and a supervised person of an investment adviser would prominently disclose the following, for example: "[Name of professional], a [title] of [Name of Firm], an associated person of an SEC-registered broker-dealer and a supervised person of an SEC- registered investment adviser."

438 *See* Exchange Act proposed rule 15l-3(b).

439 *See* Advisers Act proposed rule 211h-1(b).

Our proposed registration disclosure rules, like the proposed restriction on names and titles, or our proposed alternative approaches, complement our proposed requirement that broker-dealers and investment advisers deliver a relationship summary to retail investors. Even if a firm uses various titles, such as "wealth consultant" or "wealth manager," the legal term for these firms is "investment adviser" and/or "broker-dealer." These statutory terms have meaning because they relate to a particular regulatory framework that is designed to address the nature and scope of the firm's activities, which the firm would describe for a retail investor in the relationship summary.[440] Accordingly, we preliminarily believe that requiring a firm to disclose whether it is a broker-dealer or an investment adviser in print or electronic communications to retail investors would assist retail investors to determine which type of firm is more appropriate for their specific investment needs.

For similar reasons, we preliminarily believe that because retail investors interact with a firm primarily through financial professionals, it is important that financial professionals disclose the firm type with which they are associated. We acknowledge that in the studies and the comments received, retail investors generally believe broker-dealers and investment advisers are similar, and that they did not understand differences between them.[441] As discussed above, while we acknowledge that broker-dealers and investment advisers are similar in that they provide investment advice, they commonly are dissimilar in a variety of key areas such as disclosure of

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440 For similar reasons, we are requiring the use of the terms "supervised person" and "associated person" as they are defined legal terms generally describing the financial professional's association with the investment adviser or broker-dealer, respectively.

441 *See supra* Section III.A. *See also, e.g.*, RAND Study, *supra* note 5, at 19, 20 ("Many [industry interview] participants reported that they thought that offering such [fee-based account] products and services meant that broker-dealers and investment advisers became less distinguishable from one another. They claimed that bundling of advice and sales by broker-dealers also added to investor confusion….[Industry Representative] interviews suggest that individual investors do not distinguish between investment advisers and broker-dealers. Marketplace changes that have resulted in investment advisers and broker-dealers offering similar services have added to investor confusion.").

conflicts of interest, types of fees charged, and standard of conduct. In particular, the proposed relationship summary would inform retail investors about many of these differences, and in so doing, would be addressing investor confusion. As a result, even if investors are currently confused, over time they should better understand that investment advisers and broker-dealers may be different, and how they are different.

Similarly, our proposed rules to require a firm to disclose whether it is a broker-dealer or an investment adviser in print or electronic communications to retail investors would help to facilitate investor understanding, even if investors currently may not understand the differences between investment advisers and broker-dealers.

We believe that disclosures that are as important as whether a firm is a broker-dealer or an investment adviser or whether a financial professional is associated with a broker-dealer or is a supervised person of an investment adviser, should not be inconspicuous or placed in fine print. Accordingly, we are proposing to require a firm and its financial professionals to disclose their registration statuses in print communications in a type size at least as large as and of a font style different from, but at least as prominent as, that used in the majority of the communication.[442] To be "prominent," for example, we believe the disclosures should be included, at a minimum, on the front of a business card or in another communication, in a manner clearly intended to draw attention to it. In addition, we are proposing to require the disclosure to be presented in the body of the communication and not in a footnote.[443] If a communication is delivered through an electronic communication or in any publication by radio or television, the disclosure must be

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442 *See* Exchange Act proposed rule 15l-3(c)(1) and Advisers Act proposed rule 211h-1(c)(1).

443 *See supra* note 442.

presented in a manner reasonably calculated to draw retail investors' attention to it.[444] For example, in a televised or video presentation, a voice overlay and on-screen text could clearly convey the required information. Finally, we propose to stage the compliance date to ensure that firms and financial professionals can phase out certain older communications from circulation through the regular business lifecycle rather than having to retroactively change them.[445]

We request comment generally on our proposed requirement to disclose a firm's regulatory status and, for financial professionals, their association with such firm, and in particular on the following issues:

- Does our proposed rule requiring disclosure of a firm's registration status, either alone or in combination with the proposed relationship summary, sufficiently address the concerns addressed by our proposed restriction on certain names or titles? If not, why not?
- Would the proposed rules requiring disclosure of registration status and the financial professional's association with the firm give retail investors greater clarity about various aspects of their relationship with a financial professional (*e.g.*, his or her services, compensation structures, conflicts of interest, and legal obligations)?
- To what extent do firms already clearly and conspicuously disclose their federal and/or state registration as investment advisers or broker-dealers? To what extent

444 *See* Exchange Act proposed rule 15l-3(c)(2) and Advisers Act proposed rule 211h-1(c)(2). *See also* Proposed Amendments to Investment Company Advertising Rules, Investment Company Act Release No. 25575 (May 17, 2002); Amendments to Investment Company Advertising Rules, Investment Company Act Release No. 26195 (Sept. 29, 2003) (stating that "radio and television advertisements [must] give the required narrative disclosures emphasis equal to that used in the major portion of the advertisement"). *See also* 17 CFR 230.420.

445 Similarly, we are not requiring firms to send new communications to replace all older print communications as this would be overly burdensome and costly for firms.

do financial professionals already disclose their association with the broker-dealer or investment adviser? If such status is disclosed, is it typically in fine print or presented in a manner that it is not easily recognizable to investors?

- Do retail investors understand what it means for a firm to be "registered" with the Commission or a state? Additionally, do retail investors understand what it means for a financial professional to be an "associated person" of a broker-dealer or a "supervised person" of an investment adviser?
- Would our proposed rules improve clarity and consistency for investors in identifying a firm's regulatory status and a financial professional's association with a firm or will it lead to unnecessary, wordy, and possibly redundant disclosure? If the latter, how can we address this?
- Are we correct that investors would find it helpful to know whether a firm is registered as an investment adviser or a broker-dealer or a financial professional is associated with a broker-dealer or supervised by an investment adviser so that they can refer to the relationship summary to better understand the practical implications of the firm's registration and such financial professional's association with that firm?
- Should dually registered firms be required to disclose both registration statuses? Would this requirement cause more confusion or help to address it? If so, how? By requiring a financial professional to disclose whether he or she is an associated person of a broker-dealer or a supervised person of an investment adviser, would we be assisting retail investors in understanding the capacity in which their financial professional services them? For example, would retail investors

serviced by dual hatted financial professionals understand that their financial professional may act in dual capacities (*i.e.*, brokerage and advisory)?

- Are our proposed requirements prescribing the presentation of the disclosure appropriate? Should we consider removing any of these requirements? Alternatively, are there requirements we should add? If so, which requirements and why? Are there requirements that we should modify? For example, could the Commission's objective of ensuring prominence of disclosure be served through a more principles-based approach, or through different requirements (e.g., that the disclosure be not 20% smaller than the principal text)?
- Should the account statement or other disclosure clarify whether a retail investor has an advisory or a brokerage account? If so, how?
- Should our proposed rules define "communication"? For example, should we include in the rule a definition that tracks FINRA's definition of "communication" in Rule 2210? In particular, FINRA Rule 2210 defines a "communication" as correspondence, retail communications and institutional communications. "Correspondence" means any written (including electronic) communication that is distributed or made available to 25 or fewer retail investors within any 30 calendar day period and "Retail communication" means any written (including electronic) communication that is distributed or made available to more than 25 retail investors within any 30 calendar day period. Finally, "Institutional communication" means any written (including electronic) communication that is distributed or made available only to institutional investors, but does not include a member's internal communications. Are there other definitions of

"communication" we should consider? As an alternative to the word "communication" in our proposed rules, should we use "advertisements" as defined in rule 206(4)-1 under the Advisers Act, or a different term?[446]

- Should the proposed rules apply to all communications to retail investors, including oral communications? On the other hand, are there certain types of written communications that could be exempted, *e.g.* communications that do not make any financial or investment recommendation or otherwise promote a product or service of the member?[447]

- Should we permit the use of hyperlinks to the registration status disclosure statement for electronic communications rather than requiring the disclosure statement on the communication itself? Would permitting hyperlinks limit or promote the effectiveness of this disclosure requirement, and if so, how?

- Should we require broker-dealers, investment advisers and financial professionals to state that registration with the Commission does not imply a certain level of skill or training? Are there potential benefits or drawbacks to requiring this type of statement?

IV. ECONOMIC ANALYSIS

We are sensitive to the economic effects, including the costs and benefits that stem from the proposed rules. Whenever the Commission engages in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, section 3(f) of the Exchange Act requires the Commission to consider whether the action would promote

446 *See* FINRA Rule 2210(a); rule 206(4)-1 under the Advisers Act.

447 *See* FINRA Rule 2210(b)(1)(D)(iii) (exempting certain communications from principal pre-approval).

efficiency, competition, and capital formation, in addition to the protection of investors.[448] Further, when making rules under the Exchange Act, section 23(a)(2) of the Exchange Act requires the Commission to consider the impact such rules would have on competition.[449] Section 23(a)(2) of the Exchange Act also prohibits the Commission from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.[450]

Section 202(c) of the Advisers Act requires the Commission, when engaging in rulemaking and required to consider or determine whether an action is necessary or appropriate in the public interest, also to consider whether the action will promote efficiency, competition, and capital formation, in addition to the protection of investors.[451] The Commission provides both a qualitative assessment of the potential effects and, where feasible, quantitative estimates of the potential aggregate initial and aggregate ongoing costs. In some cases, however, quantification is particularly challenging due to the difficulty of predicting how market participants would act under the conditions of the proposed rules. For example, although we expect that the proposal would increase retail investors' understanding of the services provided to them, investors could respond differently to the increased understanding – by transferring to a different financial firm or professional, hiring a financial professional for the first time, or entirely abandoning the financial services market while moving their assets to other products or

448 *See* 15 U.S.C. 77b(b) and 15 U.S.C. 78c(f).

449 *See* 15 U.S.C. 78w(a)(2).

450 *Id.*

451 15 U.S.C. 80b-2(c).

markets (e.g., bank deposits or insurance products). The Commission encourages commenters to provide any data and information that could help us quantify these long-term effects.

In the economic analysis that follows, we first examine the current regulatory and economic landscape to form a baseline for our analysis. We then analyze the likely economic effects – including benefits and costs and impact on efficiency, competition, and capital formation – arising from the proposed rules relative to the baseline discussed below.

A. Baseline

This section discusses, as it relates to this proposal, the current state of the broker-dealer and investment adviser markets, the current regulatory environment, and the current state of retail investor perceptions in the market.

1. Providers of Financial Services

a. Broker-Dealers

As noted above, one market that would be affected by these proposed rules[452] is the market for broker-dealer services, including firms that are dually registered as broker-dealers and investment advisers.[453] The market for broker-dealer services encompasses a small set of large broker-dealers and thousands of small broker-dealers competing for niche or regional segments of the market.[454]

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452 "Proposed rules" used in this economic analysis is inclusive of Form CRS and related proposed forms as well as the proposed rules themselves.

453 Not all firms that are dually registered as an investment adviser and a broker-dealer offer both brokerage and advisory accounts to retail investors – for example, some dual registrants offer advisory accounts to retail investors but offer only brokerage services, such as underwriting services, to institutional clients. For purposes of the discussion of the baseline in this economic analysis, a dual registrant is any firm that is dually registered with the Commission as an investment adviser and a broker-dealer. For the purposes of the relationship summary, however, we propose to define dual registrant as a firm that is dually registered as a broker-dealer and an investment adviser and offers services to retail investors as both a broker-dealer and investment adviser. *See supra* note 25.

454 *See* Risk Management Controls for Brokers or Dealers with Market Access, Securities Exchange Act Release No. 63241 (Nov. 3, 2010) [75 FR 69791, 69822 (Nov. 15, 2010)].

As of December 2017, there were approximately 3,841 registered broker-dealers with over 130 million customer accounts. In total, these broker-dealers have close to $4 trillion in total assets.[455] More than two-thirds of all brokerage assets and close to one-third of all customer accounts are held by the 16 largest broker-dealers, as shown in Table 1, Panel A.[456] Of the broker-dealers registered with the Commission as of December 2017, 366 broker-dealers were dually registered as investment advisers;[457] however, these firms hold nearly 90 million (68%) customer accounts.[458] Approximately 546 broker-dealers (14%) reported at least one type of non-securities business, including insurance, retirement planning, mergers & acquisitions, and real estate, among others.[459] Approximately 74% of registered broker-dealers report retail customer activity.[460]

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455 Assets are estimated by Total Assets (allowable and non-allowable) from Part II of the FOCUS filings (Form X-17A-5 Part II, *available at* https://www.sec.gov/files/formx-17a-5_2.pdf) and correspond to balance sheet total assets for the broker-dealer. The Commission does not have an estimate of the total amount of customer assets for broker-dealers. We estimate broker-dealer size from the total balance sheet assets as described above.

456 Approximately $3.91 trillion of total assets of broker-dealers (98%) are at firms with total assets in excess of $1 billion. Of the 30 dual registrants in the group of broker-dealers with total assets in excess of $1 billion, total assets for these dual registrants are $2.46 trillion (62%) of aggregate broker-dealer assets. Of the remaining 88 firms, 81 have affiliated investment advisers.

457 Because this number does not include the number of broker-dealers who are also registered as state investment advisers, the number undercounts the full number of broker-dealers that operate in both capacities. Further, not all firms that are dually registered as an investment adviser and a broker-dealer offer both brokerage and advisory accounts to retail investors – for example, some dual registrants offer advisory accounts to retail investors but offer only brokerage services, such as underwriting services, to institutional customers. For purposes of the discussion of the baseline in this economic analysis, a dual registrant is any firm that is dually registered with the Commission as an investment adviser and a broker-dealer.

458 Some broker-dealers may be affiliated with investment advisers without being dually registered. From Question 10 on Form BD, 2,145 broker-dealers report that directly or indirectly, they either control, are controlled by, or under common control with an entity that is engaged in the securities or investment advisory business. Comparatively, 2,478 (19.57%) SEC-registered investment advisers report an affiliate that is a broker-dealer in Section 7A of Schedule D of Form ADV, including 1,916 SEC-registered investment advisers that report an affiliate that is a registered broker-dealer. Approximately 75% of total assets under management of investment advisers are managed by these 2,478 investment advisers.

459 We examined Form BD filings to identify broker-dealers reporting non-securities business. For the 546 broker-dealers reporting such business, staff analyzed the narrative descriptions of these businesses on Form BD, and identified the most common types of businesses: insurance (208),

Panel B of Table 1 limits the broker-dealers to those that report some retail investor activity. As of December 2017, there were approximately 2,857 broker-dealers that served retail investors, with over $3.6 trillion in assets (90% of total broker-dealer assets) and 128 million (96%) customer accounts.[461] Of those broker-dealers serving retail investors, 360 are dually registered as investment advisers.[462]

Table 1: Panel A: Registered Broker-Dealers as of December 2017[463]
Cumulative Broker-Dealer Total Assets and Customer Accounts[464]

Size of Broker-Dealer (Total Assets)	Total Num. of BDs	Num. of Dual-Registered BDs	Cumulative Total Assets	Cumulative Number of Customer

management/financial/other consulting (101), advisory/retirement planning (80), mergers & acquisitions (71), foreign exchange/swaps/other derivatives (31), real estate/property management (31), tax services (15), and other (141). Note that a broker-dealer may have more than one line of non-securities business.

460 The value of customer accounts is not available from FOCUS data for broker-dealers. Therefore, to obtain estimates of firm size for broker-dealers, we rely on the value of broker-dealers total assets as obtained from FOCUS reports. Retail sales activity is identified from Form BR, which categorizes retail activity broadly (by marking the "sales" box) or narrowly (by marking the "retail" or "institutional" boxes as types of sales activity). We use the broad definition of sales as we preliminarily believe that many firms will just mark "sales" if they have both retail and institutional activity. However, we note that this may capture some broker-dealers that do not have retail activity, although we are unable to estimate that frequency. We request comment on whether firms that intermediate both retail and institutional customer activity generally market only "sales" on Form BR.

461 Total assets and customer accounts for broker-dealers that serve retail customers also include institutional accounts. Data available from Form BD and FOCUS data is not sufficiently granular to identify the percentage of retail and institutional accounts at firms.

462 Of the 36 dual registrants in the group of retail broker-dealers with total assets in excess of $500 million, total assets for these dual registrants are $2.19 trillion (60%) of aggregate retail broker-dealer assets. Of the remaining 72 retail broker-dealers, 67 have affiliated investment advisers.

463 The data is obtained from FOCUS filings as of December 2017. Note that there may be a double-counting of customer accounts among in particular the larger broker-dealers as they may report introducing broker-dealer accounts as well in their role as clearing broker-dealers.

464 In addition to the approximately 130 million individual accounts at broker-dealers, there are approximately 293,000 omnibus accounts (0.2% of total accounts at broker-dealers), across all 3,841 broker-dealers, of which approximately 99% are held at broker-dealers with greater than $1 billion in total assets. *See also supra* note 455. Omnibus accounts reported in FOCUS data are the accounts of non-carrying broker-dealers with carrying broker-dealers. These accounts may have securities of multiple customers (of the non-carrying firm), or securities that are proprietary assets of the non-carrying broker-dealer. We are unaware from the data available to determine how many customer accounts non-carrying broker-dealers may have. The data does not allow the Commission to parse the total assets in those accounts to determine to whom such assets belong. Therefore, our estimate may be underinclusive of all customer accounts held at broker-dealers.

				Accounts[465]
> $50 billion	16	10	$2,717 bil.	40,969,187
$1 billion to $50 billion	102	20	$1,196 bil.	81,611,933
$500 million to $1 billion	38	7	$26 bil.	4,599,330
$100 million to $500 million	118	26	$26 bil.	1,957,981
$10 million to $100 million	482	94	$17 bil.	2,970,133
$1 million to $10 million	1,035	141	$4 bil.	233,946
< $1 million	2,055	68	$1 bil.	5,588
Total	3,841	366	$3,987 bil.	132,348,098

Table 1, Panel B: Registered Retail Broker-Dealers as of December 2017
Cumulative Broker-Dealer Total Assets and Customer Accounts

Size of Broker-Dealer (Total Assets)	Total Num. of BDs	Num. of Dual-Registered BDs	Cumulative Total Assets	Cumulative Number of Customer Accounts
> $50 billion	15	10	$2,647 bil.	40,964,945
$1 billion to $50 billion	70	19	$923 bil.	77,667,615
$500 million to $1 billion	23	7	$16 bil.	4,547,574
$100 million to $500 million	93	25	$20 bil.	1,957,981
$10 million to $100 million	372	94	$14 bil.	2,566,203
$1 million to $10 million	815	139	$3 bil.	216,158
< $1 million	1,469	66	$.4 bil.	5,588
Total	2,857	360	$3,624 bil.	127,926,064

Table 2 reports information on brokerage commissions,[466] fees, and selling concessions from the fourth quarter of 2017 for all broker-dealers, including dual registrants.[467] On average, broker-dealers, including those that are dually registered as investment advisers, earn about $2.1

[465] Customer Accounts includes both broker-dealer and investment adviser accounts for dual registrants.

[466] FOCUS data does not provide mark-ups or mark-downs as a separate revenue category and they are not included as part of the brokerage commission revenue.

[467] Source: FOCUS data.

million per quarter in revenue from commissions and more than double that amount in fees,[468] although the Commission notes that fees encompass a variety of fees, not just those related to advisory services.[469] The level of revenues earned from broker-dealers for commissions and fees increases with broker-dealer size, but also tends to be more heavily weighted towards commissions for broker-dealers with less than $10 million in assets and is weighted more heavily towards fees for broker-dealers with assets in excess of $10 million. For example, for the 102 broker-dealers with assets between $1 billion and $50 billion, average revenues from commissions are $25 million, while average revenues from fees are approximately $91 million.[470]

In addition to revenue generated from commissions and fees, broker-dealers may also receive revenues from other sources, including margin interest, underwriting, research services, and third-party selling concessions, such as from sales of investment company ("IC") shares. As shown in Table 2, Panel A, these selling concessions are generally a smaller fraction of broker-dealer revenues than either commissions or fees, except for broker-dealers with total assets between $10 million and $100 million. For these broker-dealers, revenue from third-party

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468 Fees, as detailed in the FOCUS data, include fees for account supervision, investment advisory and administrative services. Beyond the broad classifications of fee types included in fee revenue, we are unable to determine whether fees such as 12b-1 fees, sub-accounting, or other such service fees are included. The data covers both broker-dealers and dually-registered firms. FINRA's Supplemental Statement of Income, Line 13975 (Account Supervision and Investment Advisory Services) denotes that fees earned for account supervision are those fees charged by the firm for providing investment advisory services where there is no fee charged for trade execution. Investment Advisory Services generally encompass investment advisory work and execution of client transactions, such as wrap arrangements. These fees also include fees charged by broker-dealers that are also registered with the Commodity Futures Trading Commission ("CFTC"), but do not include fees earned from affiliated entities (Item A of question 9 under Revenue in the Supplemental Statement of Income).

469 With respect to the FOCUS data, additional granularity of what services comprise "advisory services" is not available.

470 A rough estimate of total fees in this size category would be 102 broker-dealers with assets between $1 billion and $50 billion multiplied by the average fee revenue of $91 million, or $9.381 billion in total fees. Divided by the number of customer accounts in this size category (81,611,933), the average account would be charged approximately $115 in fees per quarter, or $460 per year.

selling concessions is the largest category of revenues and constitutes approximately 44% of total revenues earned by these firms.

Table 2, Panel B, below provides aggregate revenues by revenue type (commissions, fees, or selling concessions) for broker-dealers delineated by whether the broker-dealer is also a dual registrant. Broker-dealers dually registered as investment advisers have a significantly larger fraction of their revenues from fees compared to commissions or selling concessions, whereas broker-dealers that are not dually registered generated approximately 43% of their advice-related revenues as commissions and only 32% of their advice-related revenues from fees, although we lack granularity to determine whether advisory services, in addition to supervision and administrative services, contribute to fees at standalone broker-dealers.

Table 2, Panel A: Average Broker-Dealer Revenues from Revenue Generating Activities[471]

Size of Broker-Dealer in Total Assets	N	Commissions	Fees[472]	Sales of IC Shares
> $50 billion	16	$176,193,599	$365,014,954	$20,493,769
$1 billion - $50 billion	102	$25,109,619	$91,966,559	$18,808,687
$500 million - $1 billion	38	$6,322,803	$11,312,112	$6,724,401
$100 million - $500 million	118	$7,698,889	$11,338,175	$4,536,407
$10 million - $100 million	483	$1,801,079	$2,811,290	$3,653,475
$1 million - $10 million	1,035	$633,720	$372,757	$217,444
< $1 million	2,049	$66,503	$38,618	$26,270
Average of All Broker-Dealers	3,841	$2,132,544	$4,897,521	$1,322,759

471 The data obtained from December 2017 FOCUS reports and averaged across size groups.

472 Fees, as detailed in the FOCUS data, include fees for account supervision, investment advisory and administrative services. The data covers both broker-dealers and dually-registered firms.

Table 2, Panel B: Aggregate Total Revenues from Revenue Generating Activities for Broker-Dealers based on Dual Registrant Status

Broker-Dealer Type	N	Commissions	Fees[473]	Sales of IC Shares
Dual Registered as IAs	366	$4.27 bil.	$15.88 bil.	$2.8 bil.
Standalone Registered BDs	3,475	$3.92 bil.	$2.93 bil.	$2.28 bil.
All	3,841	$8.19 bil.	$18.81 bil.	$5.08 bil.

i. Disclosures for Broker-Dealers

Broker-dealers register with and report information to the Commission, the SROs, and other jurisdictions through Form BD. Form BD requires information about the background of the applicant, its principals, controlling persons, and employees, as well as information about the type of business the broker-dealer proposes to engage in and all control affiliates engaged in the securities or investment advisory business.[474] Broker-dealers report whether a broker-dealer or any of its control affiliates have been subject to criminal prosecutions, regulatory actions, or civil actions in connection with any investment-related activity, as well as certain financial matters.[475] Once a broker-dealer is registered, it must keep its Form BD current by amending it promptly when the information is or becomes inaccurate for any reason.[476] In addition, firms report similar information and additional information to FINRA pursuant to FINRA Rule 4530.[477] The current Paperwork Reduction Act estimate for the total industry-wide annual filing burden to comply with rule 15b1-1 and file Form BD is approximately 4,999 hours, with an estimated internal cost of compliance associated with those burden hours for all broker-dealers of $1,394,721.

473 *See id*.

474 *See generally* Form BD.

475 *See* Item 11 and Disclosure Reporting Pages, Form BD.

476 *See* Exchange Act rule 15b3-1(a).

477 *See supra* Section 0.

A significant amount of information concerning broker-dealers and their associated natural persons, including information from Form BD, Form BDW, and Forms U4, U5, and U6, is publicly available through FINRA's BrokerCheck system. This information includes violations of and claims of violations of the securities and other financial laws by broker-dealers and their financial professionals; criminal or civil litigation, regulatory actions, arbitration, or customer complaints against broker-dealers and their financial professionals; and the employment history and licensing information of financial professionals associated with broker-dealers, among other things.[478]

Broker-dealers are subject to other disclosure requirements under the federal securities laws and SRO rules. For instance, under existing antifraud provisions of the Exchange Act, a broker-dealer has a duty to disclose material information to its customers conditional on the scope of the relationship with the customer.[479] Disclosure has also been a feature of other regulatory efforts related to financial services, including those of DOL and certain FINRA rules.[480]

b. Investment Advisers

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478 FINRA Rule 8312 governs the information FINRA releases to the public via BrokerCheck. *See supra* note 280 and accompanying text.

479 A broker-dealer also may be liable if it does not disclose "material adverse facts of which it is aware". *See, e.g., Chasins v. Smith, Barney & Co.*, 438 F.2d at 1172; *SEC v. Hasho*, 784 F. Supp. at 1110; Release 48758, *supra* note 243 ("When a securities dealer recommends stock to a customer, it is not only obligated to avoid affirmative misstatements, but also must disclose material adverse facts of which it is aware. That includes disclosure of "adverse interests" such as "economic self-interest" that could have influenced its recommendation.") (citations omitted).

480 *See*, *infra* Section 0.c; FINRA Notice 10-54, *supra* note 12. Generally, all registered broker-dealers that deal with the public must become members of FINRA, a registered national securities association, and may choose to become exchange members. *See* Exchange Act section 15(b)(8) and Exchange Act rule 15b9-1. FINRA is the sole national securities association registered with the SEC under section 15A of the Exchange Act. Accordingly, for purposes of discussing a broker-dealer's regulatory requirements when providing advice, we focus on FINRA's regulation, examination and enforcement with respect to member broker-dealers. FINRA disclosure rules include but are not limited FINRA rules 2210(d)(2) (communications with the public), 2260 (disclosures), 2230 (customer account statements and confirmations), and 2270 (day-trading risk disclosure statement).

Other parties that would be affected by the proposed rules and proposed Form CRS are SEC-registered investment advisers.[481] This section first discusses SEC-registered investment advisers, followed by a discussion of state-registered investment advisers.

As of December 2017, there are approximately 12,700 investment advisers registered with the Commission. The majority of SEC-registered investment advisers report that they provide portfolio management services for individuals and small businesses.[482]

Of all SEC-registered investment advisers, 366 identified themselves as dually registered broker-dealers.[483] Further, 2,478 investment advisers (20%) reported an affiliate that is a broker-dealer, including 1,916 investment advisers (15%) that reported an SEC-registered broker-dealer affiliate.[484] As shown in Panel A of Table 3 below, in aggregate, investment advisers have over $72 trillion in assets under management ("AUM"). A substantial percentage of AUM at investment advisers is held by institutional clients, such as investment companies, pooled investment vehicles, and pension or profit sharing plans; therefore, although the dollar value of AUM for investment advisers and of customer assets in broker-dealer accounts is comparable, the total number of accounts for investment advisers is only 27% of the number of customer accounts for broker-dealers.

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481 In addition to SEC-registered investment advisers, which are the focus of this section, the proposed rules and proposed Form CRS could also affect banks, trusts, insurance companies, and other providers of financial advice.

482 Of the approximately 12,700 SEC-registered investment advisers, 7,979 (64%) report in Item 5.G.(2) of Form ADV that they provide portfolio management services for individuals and/or small businesses. In addition, there are approximately 17,800 state-registered investment advisers, of which 145 are also registered with the Commission. Approximately 13,800 state-registered investment advisers are retail facing (*see* Item 5.D of Form ADV).

483 See *supra* note 457.

484 Item 7.A.1 of Form ADV.

Based on staff analysis of Form ADV data, approximately 60% of investment advisers (7,600) have some portion of their business dedicated to retail investors, including both high net worth and non-high net worth individual clients, as shown in Panel B of Table 3.[485] In total, these firms have approximately $32 trillion of assets under management.[486] Approximately 6,600 registered investment advisers (52%) serve 29 million non-high net worth individual clients and have approximately $5.33 trillion in assets under management, while nearly 7,400 registered investment advisers (58%) serve approximately 4.8 million high net worth individual clients with $6.56 trillion in assets under management.[487]

Table 3, Panel A: Registered Investment Advisers (RIAs) as of December 2017 Cumulative RIA Assets under Management (AUM) and Accounts

Size of Investment Adviser (AUM)	Num. of RIAs	Num. of Dual-registered RIAs	Cumulative AUM	Cumulative Number of Accounts
> $50 billion	246	15	$48,221 bil.	17,392,968
$1 billion to $50 billion	3,238	115	$21,766 bil.	11,560,805
$500 million to $1 billion	1,554	53	$1,090 bil.	2,678,084
$100 million to $500 million	5,568	129	$1,303 bil.	3,942,639
$10 million to $100 million	1,103	24	$59 bil.	198,659
$1 million to $10 million	172	2	$1 bil.	5,852
< $1 million	778	28	$.02 bil.	31,291
Total	12,659	366	$72,439 bil.	35,810,298

485 We use the responses to Items 5.D.(a)(1), 5.D.(a)(3), 5.D.(b)(1), and 5.D.(b)(3) of Part 1A. If at least one of these responses was filled out as greater than 0, the firm is considered as providing business to retail investors. Form ADV Part 1A.

486 The aggregate AUM reported for these investment advisers that have retail investors includes both retail AUM as well as any institutional AUM also held at these advisers.

487 Estimates are based on IARD system data as of December 31, 2017. The AUM reported here is specifically that of those non-high net worth clients. Of the 7,600 investment advisers serving retail investors, 360 may also be dually registered as broker-dealers.

Table 3, Panel B: Retail Registered Investment Advisers (RIAs) as of December 2017 Cumulative RIA Assets under Management (AUM) and Accounts

Size of Investment Adviser (AUM)	Num. of RIAs	Num. of Dual-registered RIAs	Cumulative AUM	Cumulative Number of Accounts
> $50 billion	106	15	$22,788 bil.	16,638,548
$1 billion to $50 billion	1,427	114	$8,472 bil.	10,822,275
$500 million to $1 billion	934	52	$652 bil.	2,602,220
$100 million to $500 million	4,114	126	$917 bil.	3,814,900
$10 million to $100 million	711	24	$40 bil.	231,663
$1 million to $10 million	98	1	$.4 bil.	5,804
< $1 million	198	29	$.02 bil.	31,271
Total	7,588	361	$32,870 bil.	34,146,681

As an alternative to registering with the Commission, smaller investment advisers could register with state regulators.[488] As of December 2017, there are 17,635 state registered investment advisers,[489] of which 145 are also registered with the Commission. Of the state-registered investment advisers, 236 are dually registered as broker-dealers, while 5% (920) report a broker-dealer affiliate. In aggregate, state-registered investment advisers have approximately $341 billion in AUM. Eighty-two percent of state-registered investment advisers report that they

488 Pursuant to the Dodd-Frank Act, Item 2.A. of Part 1A of Form ADV requires an investment adviser to register with the SEC if it (i) is a large adviser that has $100 million or more of regulatory assets under management (or $90 million or more if an adviser is filing its most recent annual updating amendment and is already registered with the SEC); (ii) is a mid-sized adviser that does not meet the criteria for state registration or is not subject to examination; (iii) meets the requirements for one or more of the revised exemptive rules under section 203A discussed below; (iv) is an adviser (or subadviser) to a registered investment company; (v) is an adviser to a business development company and has at least $25 million of regulatory assets under management; or (vi) received an order permitting the adviser to register with the Commission. Although the statutory threshold is $100 million, the SEC raised the threshold to $110 million for those investment advisers that do not already file with the SEC.

489 There are 79 investment advisers with latest reported Regulatory Assets Under Management in excess of $110 million but are not listed as registered with the SEC. For the purposes of this rulemaking, these are considered erroneous submissions.

provide portfolio management services for individuals and small businesses, compared to just 64% for SEC-registered investment advisers.

Approximately 77% of state-registered investment advisers (13,470) have some portion of their business dedicated to retail investors,[490] and in aggregate, these firms have approximately $308 billion in AUM.[491] Approximately 12,700 (72%) state-registered advisers serve 616,000 non-high net worth retail clients and have approximately $125 billion in AUM, while over 11,000 (63%) state-registered advisers serve approximately 194,000 high net worth retail clients with $138 billion in AUM.[492]

Table 4 details the compensation structures employed by approximately 12,700 investment advisers. Approximately 95% are compensated through a fee-based arrangement, where a percentage of assets under management are remitted to the investment adviser from the investor for advisory services. As shown in the table below, most investment advisers rely on a combination of different compensation types, beyond fee-based compensation, including fixed fees, hourly charges, and performance based fees. Less than 4% of investment advisers charge commissions[493] to their investors.

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490 We use the responses to Items 5.D.(a)(1), 5.D.(a)(3), 5.D.(b)(1), and 5.D.(b)(3) of Part 1A. If at least one of these responses was filled out as greater than 0, the firm is considered as providing business to retail investors. Form ADV Part 1A.

491 The aggregate AUM reported for these investment advisers that have retail investors includes both retail AUM as well as any institutional AUM also held at these advisers.

492 Estimates are based on IARD system data as of December 31, 2017. The AUM reported here is specifically that of those non-high net worth investors. Of the 13,471 investment advisers serving retail investors, 144 may also be dually registered as broker-dealers.

493 Some investment advisers report on Item 5.E. of Form ADV that they receive "commissions." As a form of deferred sales load, all payments of ongoing sales charges to intermediaries would constitute transaction-related compensation. Intermediaries receiving those payments should consider whether they need to register as broker-dealers under section 15 of the Exchange Act.

Table 4: Registered Investment Advisers Compensation by Type

Compensation Type	Yes	No
A percentage of assets under management	12,041	617
Hourly charges	3,670	8,988
Subscription fees (for a newsletter or periodical)	119	12,539
Fixed fees (other than subscription fees)	5,406	7,252
Commissions	490	12,168
Performance-based fees	4,780	7,878
Other	1,846	10,812

As discussed above, many investment advisers participate in wrap fee programs. As of December 31, 2017, more than 5% of the SEC-registered investment advisers sponsor a wrap fee program and more than 9% act as a portfolio manager for one or more wrap fee programs.[494] From the data available, we are unable to determine how many advisers provide advice about investing in wrap fee programs, because advisers providing such advice may be neither sponsors nor portfolio managers.

ii. Disclosures for Investment Advisers

As fiduciaries, investment advisers have a duty to provide full and fair disclosure of material facts and are subject to express disclosure requirements in Form ADV.[495] Consistent

494 A wrap fee program sponsor is as a firm that sponsors, organizes, or administers the program or selects, or provides advice to clients regarding the selection of, other investment advisers in the program. *See* General Instructions to Form ADV.

495 *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. at 194; *see also* Brochure Adopting Release, *supra* note 157. *See also* 913 Study, *supra* note 3, at n.92. For example, if an adviser selects or recommends other advisers to investors, it must disclose any compensation arrangements or other business relationships between the advisory firms, along with the conflicts created, and explain how it addresses these conflicts. *See* Item 10 of Form ADV Part 2A. *See also* 913 Study, *supra* note 3, at n.93. Other potential conflicts of interest include acting as a principal in transactions with investors and compensation received thereof; incentives provided by third parties to sell their services and products; and agency cross-trades, where the advisers is also a broker-dealer and executes a client's order by crossing the orders with those of non-advisory clients. *See* Interpretation of Section 206(3) of the Investment Advisers Act of 1940, Investment Advisers Act Release No. 1732 (Jul. 20, 1998), at n.3.

with this duty and those requirements, investment advisers file Form ADV to register with the Commission or state securities authorities, as applicable, and provide an annual update to the form.[496] Part 1 of Form ADV provides information to regulators, and made available to clients, prospective clients, and the public, about the registrants' ownership, investors, and business practices. Advisers also prepare a Form ADV Part 2A narrative brochure that contains information about the investment adviser's business practices, fees, conflicts of interest, and disciplinary information,[497] in addition to a Part 2B brochure supplement that includes information about the specific individuals, acting on behalf of the investment adviser, who actually provide investment advice and interact with the client.[498] Currently, the Part 2A brochure is the primary client-facing disclosure document,[499] however, Parts 1 and 2A are both made publicly available by the Commission through IAPD,[500] and advisers are generally required to deliver Part 2A and Part 2B to their clients. The current Paperwork Reduction Act estimate of

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496 *See* Advisers Act rules 203-1 and 204-1. Part 1A (1B) of Form ADV is the registration application for the Commission (and state securities authorities). Part 2 of Form ADV consists of a narrative "brochure" about the adviser and "brochure supplements" about certain advisory personnel on whom clients may rely for investment advice. *See* Brochure Adopting Release, *supra* note 157.

497 Part 2A of Form ADV contains 18 mandatory disclosure items about the advisory firm, including information about an adviser's: (1) range of fees; (2) methods of analysis; (3) investment strategies and risk of loss; (4) brokerage, including trade aggregation polices and directed brokerage practices, as well as the use of soft dollars; (5) review of accounts; (6) client referrals and other compensation; (7) disciplinary history; and (8) financial information, among other things. Much of the disclosure in Part 2A addresses an investment adviser's conflicts of interest with its investors, and is disclosure that the adviser, as a fiduciary, must make to investors in some manner regardless of the form requirements. *See* Brochure Adopting Release, *supra* note 157.

498 Part 2B, or the "brochure supplement," includes information about certain advisory personnel that provide retail client investment advice, and contains educational background, disciplinary history, and the adviser's supervision of the advisory activities of its personnel. *See* Instruction 5 of General Instructions for Form ADV. Registrants are not required to file Part 2B (brochure supplement) electronically, but must preserve a copy of the supplement(s) and make them available upon request.

499 *See* Brochure Adopting Release, *supra* note 157.

500 *See* Investment Adviser Public Disclosure, *available at* https://adviserinfo.sec.gov/.

the average annual cost and hour burden for investment advisers to complete, amend, and file all parts of Form ADV are $6,051 and 23.77 hours.[501]

c. Disclosure Obligations for Broker-Dealers and Investment Advisers Under DOL Rules and Exemptions

As noted, firms and financial professionals providing services to customers in retirement accounts, including workplace retirement plans and IRAs, are subject to certain disclosure obligations under rules and exemptions issued by the DOL under ERISA and the prohibited transaction provisions of the Code.[502] For example, DOL regulations under a statutory exemption for investment advice services provided to plan participants and IRAs requires firms and financial professionals to disclose information about the services that they will provide and their fees and other compensation, and to acknowledge that the adviser is acting as a fiduciary.[503]

More recently, the DOL's BIC Exemption would require that firms seeking to rely on the exemption to receive commissions and other fees in connection with making investment recommendations to IRAs and participants of ERISA-covered plans (including advice relating to rollovers from plans or between account types)[504] generally must (among other conditions)

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501 *See infra* Section V.A.2.

502 See *supra* note 11.

503 See 29 CFR 2550.408g-1(b)(7). In general, firms and financial professionals who receive commissions or other transaction-related compensation in connection with providing certain fiduciary investment recommendations relating to the assets of ERISA-covered workplace retirement plans and IRAs could violate provisions under the Code prohibiting fiduciaries from engaging in self-dealing and receiving compensation from third parties in connection with investments by these plans and IRA (and, with respect to such plans, substantially similar prohibited transaction rules that apply under ERISA to transactions involving ERISA plans but not IRAs). To receive such compensation, firms have historically complied with one or more prohibited transaction exemptions ("PTEs") issued by the DOL over time, which generally required (among other conditions) disclosures about, e.g., direct and indirect compensation received in connection with a recommended transactions. *See* Definition of the Term "Fiduciary;" Conflict of Interest Rule – Retirement Investment Advice, 81 FR 20945, 20991-92 (Apr. 8, 2016) (to be codified at 20 C.F.R. pts. 2509, 2510 and 2550) ("DOL Fiduciary Rule Adopting Release") (describing action to adopt new and amended PTEs and revoke certain PTEs applicable to investment advice services).

504 *See* Best Interest Contract Exemption, 81 FR 21002, 21006-7 (Apr. 8, 2016) ("BIC Exemption Release") Best Interest Contract Exemption; Correction (Prohibited Transaction Exemption 2016-01), 81 FR 44773

provide disclosure about the services to be performed (including monitoring of recommendations, offering proprietary products and limiting recommendations) and how the investor will pay for services, material conflicts of interest (including third party compensation to the firm, affiliates and financial professionals), and must also make certain ongoing disclosures on a public website.[505] The DOL adopted the BIC Exemption in connection with the amendment of its regulation defining "investment advice," which had the effect of expanding the circumstances under which broker-dealers and investment advisers may be fiduciaries for purposes of the prohibited transaction provisions under ERISA and the Code (the "DOL Fiduciary Rule").[506] Although a decision of the Court of Appeals for the Fifth Circuit recently vacated the DOL Fiduciary Rule,[507] we understand that many firms already have taken steps to implement conditions under the BIC Exemption.[508]

The Commission does not currently have data on the number of firms that are subject to

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(July 11, 2016) ("Corrected BIC Exemption"), *as amended* 18-Month Extension of Transition Period and Delay of Applicability Dates; Best Interest Contract Exemption (PTE 2016-01); Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs (PTE 2016-02); Prohibited Transaction Exemption 84-24 for Certain Transactions Involving Insurance Agents and Brokers, Pension Consultants, Insurance Companies, and Investment Company Principal Underwriters (PTE 84-24), 82 FR 56545 (Nov. 29, 2017). Depending on how they are compensated, investment advisers receiving a level fee may not be subject to the full set of contract, disclosure and other conditions of the BIC Exemption.

505 *See* Corrected BIC Exemption, *supra* note, 504, at sections II and III. Ongoing website disclosure would include information about certain material conflicts of interest and third party payments, a schedule of typical fees and service charges, a description of the compensation and incentive arrangements for individual financial professionals, and a written description of the financial institution's policies and procedures. *Id.*, at section III. In the case of recommendations provided to an IRA, the firm also would be required to enter into a written contract with the IRA owner that includes an acknowledgement of fiduciary status and an enforceable promise to adhere to certain "impartial conduct standards" (including a best interest standard of conduct). *Id.*, at section II(a).

506 *See* DOL Fiduciary Rule Adopting Release, *supra* note 503.

507 *See Chamber of Commerce of the U.S.A., e. al. v. U.S. Dep't of Labor, et. al.*, No. 17-10238 (5th Cir. Mar 15, 2018).

508 *See* SIFMA and Deloitte, *The DOL Fiduciary Rule: A study on how financial institutions have responded and the resulting impacts on retirement investors* (Aug. 9, 2017), *available at* https://www.sifma.org/wp-content/uploads/2017/08/Deloitte-White-Paper-on-the-DOL-Fiduciary-Rule-August-2017.pdf.

disclosure obligations under applicable DOL rules and exemptions.[509] However, because we understand that most broker-dealers expected that they would be required to comply with the BIC Exemption to continue to provide services to retail investors in IRAs and participant-directed workplace retirement plans,[510] the Commission can broadly estimate the maximum number of broker-dealers that could be subject to disclosure obligations under DOL rules and exemption including the BIC Exemption from the number of broker-dealers that have retail investor accounts. Approximately 74.4% (2,857) of registered broker-dealers report sales to retail customers.[511] Similarly, approximately 60% (7,600) of investment advisers serve high net worth and non-high net worth individual clients. The Commission believes that this number likely overestimates those broker-dealers and investment advisers that provide retirement account services. Therefore, these 2,850 broker-dealers and 7,600 investment advisers that provide retail services represent an upper bound of the number of broker-dealers and investment advisers that would likely be subject to compliance with disclosure obligations under DOL rules and exemptions and may have taken steps to comply with the contract, disclosure and other conditions under the DOL's BIC Exemption.[512]

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509 In order to obtain this information, the Commission would need to know which financial firms have retirement-based accounts as part of their business model. Under the current reporting regime for both broker-dealers and investment advisers, they are not required to disclose whether (or what fraction) of their accounts are held by retail investors in retirement-based accounts.

510 *See* BIC Exemption Release, *supra* note 504, at 21006-07 (DOL states that it "anticipates that the [DOL Fiduciary Rule] will cover many investment professionals who did not previously consider themselves to be fiduciaries under ERISA or the Code.").

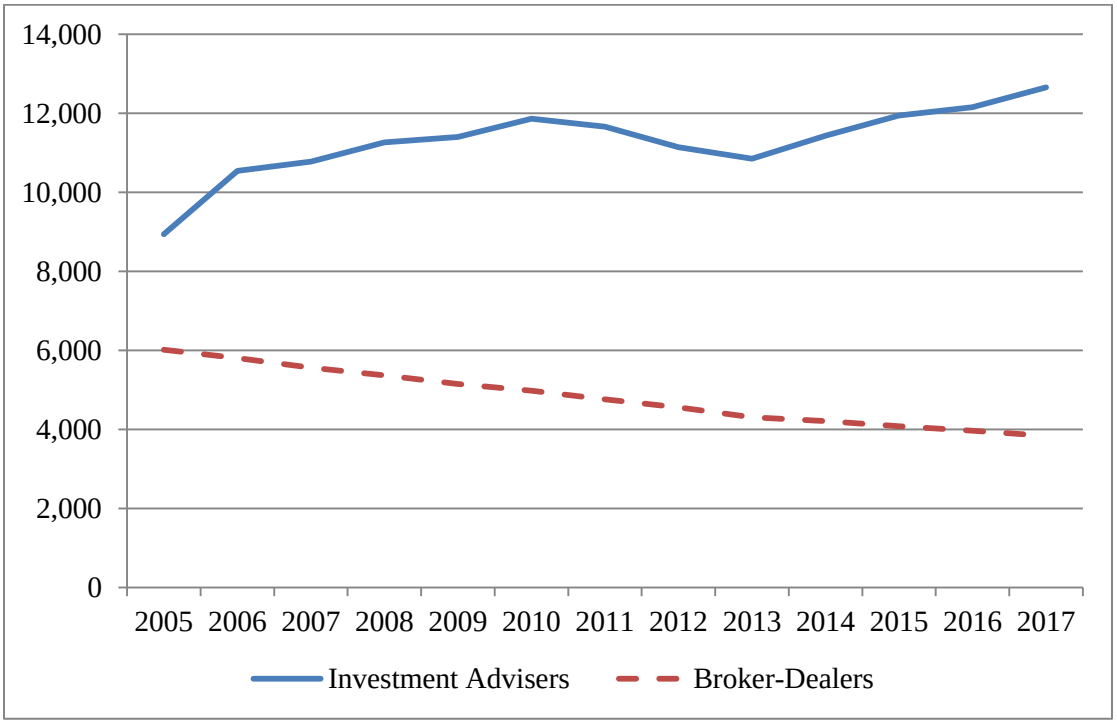
511 As of December 2017, 3,841 broker-dealers filed Form BD. Retail sales by broker-dealers were obtained from Form BD.

512 The DOL's Regulatory Impact Analysis estimated that the numbers of broker-dealers and investment advisers (including state-registered investment advisers) that could be affected by their rule are approximately 2,500 and 17,500, respectively. *See* Regulatory Impact Analysis for Final Rule and Exemptions, *Definition Of The Term "Fiduciary" Conflicts Of Interest - Retirement Investment Advice* (Apr. 2016), at 215 – 229, *available at* https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/conflict-of-interest-ria.pdf.

d. Trends in the Relative Numbers of Providers of Financial Services

Over time, the relative number of broker-dealers and investment advisers has changed. Figure 1 presented below shows the time series trend of growth in broker-dealers and investment advisers between 2005 and 2017. Over the last 13 years, the number of broker-dealers has declined from over 6,000 in 2005 to less than 4,000 in 2017, while the number of investment advisers has increased from approximately 9,000 in 2005 to over 12,000 in 2017. This change in the relative numbers of broker-dealers and investment advisers over time likely affects the competition for advice, and potentially alters the choices available to investors on how to receive or pay for such advice, the nature of the advice, and the attendant conflicts of interest.

Figure 1: Time Series of the Number of Investment Advisers and Broker-Dealers (2005 – 2017)



Increases in the number of investment advisers and decreases in the number of broker-dealers could have occurred for a number of reasons, including anticipation of possible regulatory changes to the industry, other regulatory restrictions, technological innovation (i.e.,

robo-advisers and online trading platforms), product proliferation (e.g., index mutual funds and exchange-traded products), and industry consolidation driven by economic and market conditions, particularly among broker-dealers.[513] Commission staff has observed the transition by broker-dealers from traditional brokerage services to also providing investment advisory services (often under an investment adviser registration, whether federal or state), and many firms have been more focused on offering fee-based accounts than accounts that charge commissions.[514] Broker-dealers have indicated that the following factors have contributed to this migration: provision of stability or increase in profitability,[515] perceived lower regulatory burden, and provisions of more services to retail customers.

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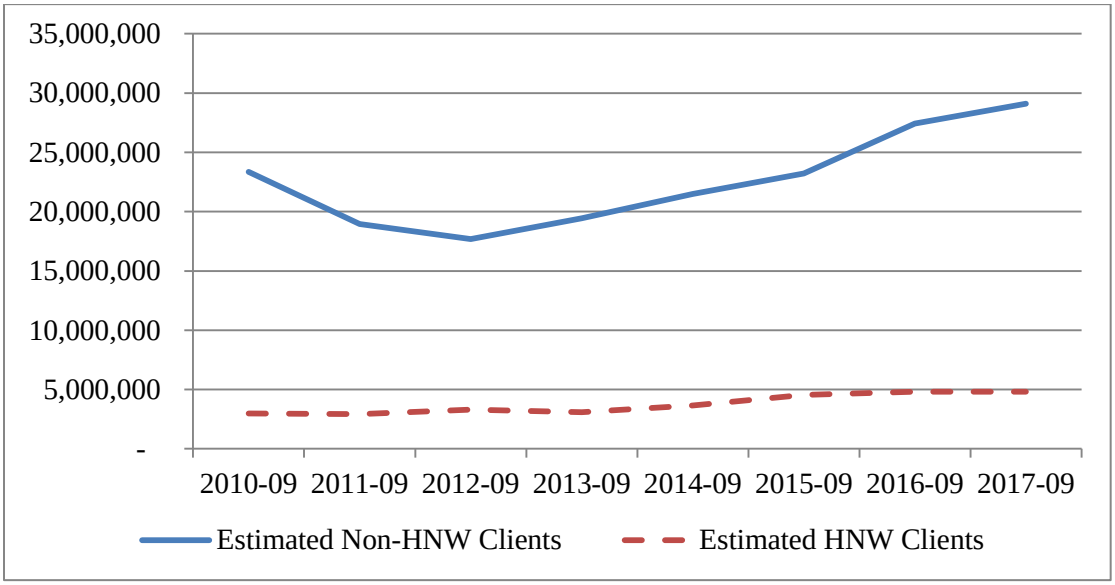
513 *See*, Hester Peirce, *Dwindling numbers in the financial industry*, Brookings Center on Markets and Regulation (May 15, 2017), *available at* https://www.brookings.edu/research/dwindling-numbers-in-the-financial-industry/ ("Brookings Report") which notes that "SEC restrictions have increased by almost thirty percent [since 2000]," and that regulations post-2010 were driven in large part by the Dodd-Frank Act, page 5. Further, the Brookings Report observation of increased regulatory restrictions on broker-dealers only reflects CFTC or SEC regulatory actions, but does not include regulation by FINRA, SROs, NFA, or the MSRB.

514 The Brookings Report, *supra* note 513, also discusses the shift from broker-dealer to investment advisory business models for retail investors, in part due to the DOL Fiduciary Rule (page 7). *See also* the RAND Study, *supra* note 5, which documents a shift from transaction-based to fee-based accounts prior to recent regulatory changes. Declining transaction-based revenue due to declining commission rates and competition from discount brokerage firms has made fee-based products and services more attractive. Although discount brokerage firms generally provide execution-only services and do not compete directly in the advice market with full service broker-dealers and investment advisers, entry by discount brokers has contributed to lower commission rates throughout the broker-dealer industry. Further, fee-based activity generates a steady stream of revenue regardless of the customer trading activity, unlike commission-based accounts.

515 Commission staff examined a sample of recent Form 10-K or Form 10-Q filings of large broker-dealers, many of which are dually registered as investment advisers, that have a large fraction of retail customer accounts to identify relevant broker-dealers. *See, e.g.*, Edward Jones 9/30/2017 Form 10-Q *available at* https://www.sec.gov/Archives/edgar/data/815917/000156459017023050/ck0000815917-10q_20170929.htm; Raymond James 9/30/2017 Form 10-K *available at* https://www.sec.gov/Archives/edgar/data/720005/000072000517000089/rjf-20170930x10k.htm; Stifle 12/31/2016 Form 10-K *available at* https://www.sec.gov/Archives/edgar/data/720672/000156459017022758/sf-10q_20170930.htm; Wells Fargo 9/30/2017 10-Q *available at* https://www.sec.gov/Archives/edgar/data/72971/000007297117000466/wfc-09302017x10q.htm; and Ameriprise 12/31/2016 Form 10-K *available at* https://www.sec.gov/Archives/edgar/data/820027/000082002717000007/ameriprisefinancial12312016.htm. We note that discussions in Form 10-K and 10-Q filings of this sample of broker-dealers here may not be representative of other large broker-dealers or of small to mid-size broker-dealers. Some firms have

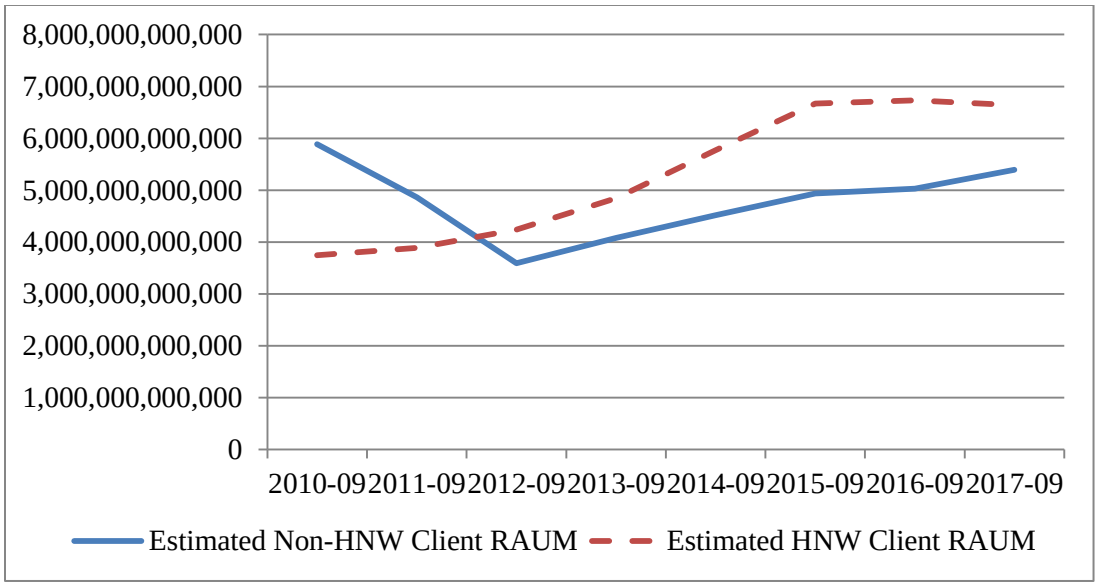
Further, there has been a substantial increase in the number of retail clients at investment advisers, both high net worth clients and non-high net worth clients as shown in Figure 2. Although the number of non-high net worth retail customers of investment advisers dipped between 2010 and 2012, since 2012, more than 12 million new non-high net worth retail clients have been added. With respect to assets under management, we observe a similar, albeit more pronounced pattern for non-high net worth retail clients as shown in Figure 3. For high net worth retail clients, there has been a pronounced increase in AUM since 2012, although AUM has leveled off since 2015.

Figure 2: Time Series of the Number of Retail Clients of Investment Advisers (2010 – 2017)



reported record profits as a result of moving clients into fee-based accounts, and cite that it provides "stability and high returns." *See* "Morgan Stanley Wealth Management fees climb to all-time high," Bloomberg, Jan. 18, 2018, *available at* https://www.bloomberg.com/news/articles/2018-01-18/morgan-stanley-wealth-management-fees-hit-record-on-stock-rally. Morgan Stanley increased the percentage of client assets in fee-based accounts from 37% in 2013 to 44% in 2017, while decreasing the dependence on transaction-based revenues from 30% to 19% over the same time period (Morgan Stanley Strategic Update, (Jan. 18, 2018), *available at* https://www.morganstanley.com/about-us-ir/shareholder/4q2017-strategic-update.pdf). *See also* Beilfuss, Lisa & Brian Hershberg, *WSJ Wealth Adviser Briefing: The Reinvention of Morgan and Merrill, Adviser Profile*, The Wall Street Journal (Jan. 25, 2018), *available at* https://blogs.wsj.com/moneybeat/2018/01/25/wsj-wealth-adviser-briefing-the-reinvention-of-morgan-and-merrill-adviser-profile/.

Figure 3: Time Series of the Retail Clients of Investment Advisers Assets under Management (2010 – 2017)



e. Registered Representatives of Broker-Dealers, Investment Advisers and Dually Registered Firms

We estimate the number of associated natural persons of broker-dealers through data obtained from Form U4, which generally is filed for individuals who are engaged in the securities or investment banking business of a broker-dealer that is a member of a self-regulatory organization ("registered representatives" or "RR"s). [516] Similarly, we approximate the number of supervised persons of registered investment advisers through the number of registered investment adviser representatives (or "registered IAR"s), who are supervised persons of

[516] The number of associated natural persons of broker-dealers may be different from the number of registered representatives of broker-dealers, because clerical/ministerial employees of broker-dealers are associated persons, but are not required to register with the firm. Therefore, using the registered representative number does not include such persons. However, we do not have data on the number of associated natural persons and therefore are not able to provide an estimate of the number of associated natural persons. We believe that the number of registered representatives is an appropriate approximation because they are the individuals at broker-dealers that provide advice and services to customers.

investment advisers who meet the definition of investment adviser representatives in Advisers Act rule 203A-3 and are registered with one or more state securities authorities to solicit or communicate with clients.[517]

We estimate the number of registered representatives and registered IARs (together "registered financial professionals") at broker-dealers, investment advisers, and dual registrants by considering only the employees of those firms that have Series 6 or Series 7 licenses or are registered with a state as a broker-dealer agent or investment adviser representative.[518] We only consider employees at firms who have retail-facing business, as defined previously.[519] We observe in Table 5, that approximately 61% of registered financial professionals are employed by dually registered entities. The percentage varies by the size of the firm. For example, for firms with total assets between $1 billion and $50 billion, 72% of all registered financial professionals in that size category are employed by dually registered firms. Focusing on dually registered firms only, approximately 59.7% of total licensed representatives at these firms are dual-hatted,

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517 *See* Advisers Act rule 203A-3. However, we note that the data on numbers of registered IARs may undercount the number of supervised persons of investment advisers who provide investment advice to retail investors because not all supervised persons who provide investment advice to retail investors are required to register as IARs. For example, Commission rules exempt from IAR registration supervised persons who provide advice only to non-individual clients or to individuals that meet the definition of "qualified client." As discussed above, the definition of retail investor for purposes of this proposed rulemaking would include qualified clients who are natural persons and trusts that represent natural persons. Proposed General Instruction 9.(e) to Form CRS. In addition, state securities authorities may impose different criteria for requiring registration as an investment adviser representative.

518 We calculate these numbers based on Form U4 filings. Representatives of broker-dealers, investment advisers, and issuers of securities must file this form when applying to become registered in appropriate jurisdictions and with self-regulatory organizations. Firms and representatives have an obligation to amend and update information as changes occur. Using the examination information contained in the form, we consider an employee a financial professional if he has an approved, pending, or temporary registration status for either Series 6 or 7 (RR) or is registered as an investment adviser representative in any state or US territory (IAR). We limit the firms to only those that do business with retail investors, and only to licenses specifically required to be licensed as an RR or IAR.

519 *See supra* notes 460 and 485.

approximately 39.9% are only registered representatives; and less than one percent are only registered investment adviser representatives.

Table 5: Total Licensed Representatives at Broker-Dealers, Investment Advisers, and Dually Registered Firms with Retail Investors[520]

Size of Firm (Total Assets for Standalone BDs and Dually Registered Firms; AUM for Standalone IAs)	Total Number of Representatives	% of Representatives in Dually Registered Firms	% of Representatives in Standalone BD	% Representatives in Standalone IA
>$50 billion	82,668	75%	8%	18%
$1 billion to $50 billion	150,662	72%	10%	18%
$500 million to $1 billion	31,673	67%	16%	16%
$100 million to $500 million	62,539	58%	24%	18%
$10 million to $100 million	116,047	52%	47%	1%
$1 million to $10 million	37,247	34%	63%	2%
< $1 million	13,563	7%	87%	6%
Total Licensed Representatives	494,399	61%	27%	12%

In Table 6 below, we estimate the number of employees who are registered representatives, registered investment adviser representatives, or both ("dual-hatted representatives").[521] Similar to Table 5, we calculate these numbers using Form U4 filings. Here, we also limit the sample to employees at firms that have retail-facing businesses as discussed previously.[522]

In Table 6, approximately 24% of registered employees at registered broker-dealers or investment advisers are dual-hatted representatives. However, this proportion varies

520 The classification of firms as dually registered, standalone broker-dealers, and standalone investment advisers comes from Forms BD, FOCUS, and ADV as described earlier. The number of representatives at each firm is obtained from Form U4 filings. Note that all percentages in the table have been rounded to the nearest whole percentage point.

521 We calculate these numbers based on Form U4 filings.

522 *See supra* notes 460 and 485.

significantly across size categories. For example, for firms with total assets between $1 billion and $50 billion,[523] approximately 36% of all registered employees are both registered representatives and investment adviser representatives. In contrast, for firms with total assets below $1 million, 15% of all employees are dual-hatted representatives.

Table 6: Number of Employees at Retail Facing Firms who are Registered Representatives, Investment Adviser Representatives, or Both[524]

Size of Firm (Total Assets for Standalone BDs and Dually Registered Firms; AUM for Standalone IAs)	Total Number of Employees	Percentage of Dual-Hatted Representatives	Percentage of RRs Only	Percentages of IARs Only
>$50 billion	216,655	18%	17%	1%
$1 billion to $50 billion	292,663	36%	11%	3%
$500 million to $1 billion	50,531	15%	40%	6%
$100 million to $500 million	112,119	23%	24%	8%
$10 million to $100 million	189,318	19%	41%	1%
$1 million to $10 million	61,310	19%	39%	1%
< $1 million	19,619	15%	46%	3%
Total Employees at Retail Facing Firms	942,215	24%	24%	3%

Approximately 88% of investment adviser representatives are dual-hatted as registered representatives. This percentage is relatively unchanged from 2010. According to information provided in a FINRA comment letter in connection with the 913 Study, 87.6% of registered investment adviser representatives were dually registered as registered representatives as of mid-

523 Firm size is defined as total assets from the balance sheet (source: FOCUS reports) for broker-dealers and dual registrants and is assets under management for investment advisers (source: Form ADV).

524 *See supra* notes 520 – 521. Note that all percentages in the table have been rounded to the nearest whole percentage point.

October 2010.[525] In contrast, approximately 50% of registered representatives were dually registered as investment adviser representatives at the end of 2017.[526]

With respect to disclosure made about licensed individuals, broker-dealers and investment advisers must report certain criminal, regulatory, and civil actions and complaint information and information about certain financial matters in Forms U4[527] and U5[528] for their representatives. Self-regulatory organizations, regulators and jurisdictions report disclosure events on Form U6.[529] FINRA's BrokerCheck system discloses to the public certain information on registered representatives and investment adviser representatives such as principal place of business, business activities, owners, and criminal prosecutions, regulatory actions, and civil actions in connection with any investment-related activity.

f. Current Use of Names and Titles

Although many financial services firms are registered as broker-dealers, investment advisers, or are dually registered, both firms and financial professionals use a variety of terms to label both the firm and the professional. Approximately 103 broker-dealers that are not dually registered as investment advisers use the term "adviser," "advisor," or "advisory" as part of their

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525 Comment letter of FINRA to File Number 4-606; Obligations of Brokers, Dealers and Investment Advisers (Nov. 3, 2010), at 1, *available at* https://www.sec.gov/comments/4-606/4606-2836.pdf.

526 In order to obtain the percentage of IARs that are dually registered as registered representatives of broker-dealers, we sum the representatives at dually-registered entities and those at investment advisers, across size categories to obtain the aggregate number of representatives in each of the two categories. We then divide the aggregate dually-registered representatives by the sum of the dually-registered representatives and the IARs at investment adviser-only firms. We perform a similar calculation to obtain the percentage of registered representatives of broker-dealers that are dually registered as IARs.

527 Form U4 requires disclosure of registered representatives' and investment adviser representatives' criminal, regulatory, and civil actions similar to those reported on Form BD or Form ADV as well as certain customer-initiated complaints, arbitration, and civil litigation cases. *See generally* Form U4.

528 Form U5 requires information about representatives' termination from their employers.

529 *See* FINRA, Current Uniform Registration Forms for Electronic Filing in Web CRD, *available at* http://www.finra.org/industry/web-crd/current-uniform-registration-forms-electronic-filing-web-crd.

current company name.[530] Of these broker-dealers, 16 reported at least one type of non-securities business. Approximately 39 percent of the 103 broker-dealers described above used a proper name coupled with the term "advisor" alone,[531] and an additional 31 percent used a proper name coupled with the term "capital advisor." In addition to those terms, less than 10% of these broker-dealers use the terms "financial advisor," "investment advisor," or "wealth advisor" in their corporate name. The remainder of the broker-dealers (approximately 25 firms) use unique combinations of other words along with "adviser," "advisor" or "advisory."

In addition to company names or professional titles, firms are likely to use labels or terms other than their formal company names to describe themselves in corporate descriptions, marketing material, or other communications with the public. To gauge the extent that registered broker-dealers and investment advisers use terms other than their registration status as descriptors, Commission staff conducted an analysis to evaluate the different terms that broker-dealer, investment adviser, and dually-registered firms use to describe themselves.[532]

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530 Source: Form BD.

531 *E.g.* "ABC Advisor."

532 From the full sample of broker-dealers with retail investors (2,857) and investment advisers with retail investors (7,600), the Commission staff used a random number generator to select 20 firms in each of the size categories listed in Table 7, from which to construct a sample of firms for which staff hand-collected data on firm descriptions from firm website homepages and "About" pages, as available. When a size category contained less than 20 firms we sampled all firms in that category. Relative to the overall proportion of firms, we oversampled firms from the larger size categories because they employ a majority of all licensed representatives and are therefore the firms the average retail investor is most likely to come in contact with. Overall, 83 randomly selected standalone broker-dealers, 100 randomly selected investment advisers, and 91 randomly selected dual registrants based on the previously identified size categories (either total assets for broker-dealers and dual registrants or assets under management for investment advisers) provided the sample reviewed in the staff study. Further, the 917 Financial Literacy Study (*see supra* note 20) showed that a substantial percentage of retail investors use information obtained from firm websites in making the selection of their financial professional.

Commission staff reviewed firm websites to collect the terms that were used on the website to describe the firm.[533] Many firms provided multiple descriptions of their businesses.[534]

As shown below in Panel A of Table 7, over 50% of broker-dealers sampled use the term "broker," "dealer," "broker-dealer," or "brokerage" to describe their business, while less than 10% use "financial advisor," "wealth advisor," or "investment advisor." Registered investment advisers (Panel B) are more likely to use the term "investment advisor," "wealth advisor," or "financial advisor" as a description of their business compared to broker-dealers (approximately 40%). Nearly 50% of the sampled standalone investment advisers use the term "investment manager" or "wealth manager" to describe their business model compared to less than 10% of broker-dealers that use these terms. Dually registered firms (Panel C) are much more diverse in their use of firm descriptions; approximately 40% use the term "brokerage," "broker-dealer," "broker," or "dealer," while nearly 30% use a firm description that contains the term "adviser" or "advisor."

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533 *See* Table 7, Panel A for firm level identifiers for broker-dealers, Panel B for identifiers for investment advisers, and Panel C for dual registrants. Not all firms provided a description of their firm on their website, which we coded as "N/A" for not available.

534 For purposes of our classification analysis, if "ABC & Co." were to be a SEC-registered standalone broker-dealer and, on ABC's webpage in describing its business and operations, ABC refers to itself as a brokerage firm and a wealth manager, we would classify, ABC & Co. as using both "brokerage" and "wealth manager" as descriptors in our analysis.

Table 7, Panel A:
Description of Standalone Broker-Dealer Firms on Firm Websites[535]

	Broker-Dealer	Investment Bank	Wealth/Investment Management	Advisory	Other	N/A
>$50 billion	2	2	0	2	0	0
$1 billion to $50 billion	15	6	0	0	0	1
$500 million to $1 billion	14	2	0	0	1	0
$100 million to $500 million	12	7	4	2	4	0
$10 million to $100 million	11	2	5	3	4	0
Total	54	19	9	7	9	1

Table 7, Panel B:
Description of Standalone Investment Adviser Firms on Firm Website[536]

	Broker-Dealer	Investment Bank	Wealth/Investment Management	Advisory	Other	N/A
>$50 billion	0	1	16	3	4	0
$1 billion to $50 billion	0	0	13	5	8	0
$500 million to $1 billion	0	0	10	13	9	0
$100 million to $500	0	0	6	7	9	3

[535] Broker-dealers are randomly drawn from Form BD data (as of Dec. 2017). The data on firm descriptions is hand collected from individual broker-dealer websites.

[536] Investment advisers are randomly drawn from Form ADV data (as of Dec. 2017). The data on firm descriptions is hand collected from individual investment adviser websites.

million						
$10 million to $100 million	2	0	2	10	7	1
Total	2	1	47	38	37	4

Table 7, Panel C:
Description of Dually-Registered Firms on Firm Website[537]

	Broker-Dealer	Investment Bank	Wealth/Investment Management	Advisory	Other	N/A
>$50 billion	5	8	2	4	1	0
$1 billion to $50 billion	7	8	5	6	9	0
$500 million to $1 billion	3	1	2	1	2	0
$100 million to $500 million	13	3	1	7	6	0
$10 million to $100 million	10	1	3	10	7	0
Total	38	21	13	28	25	0

Regarding the use of titles by individual financial professionals, a 2008 RAND Study,[538] found that households responding to the survey[539] reported a wide variety of titles were used by financial professionals with whom they worked. The RAND Study Table 6.3 (replicated below

[537] Dual registrants are randomly drawn from Form BD data (as of Dec. 2017). The data on firm descriptions is hand collected from individual dually-registered firms' websites.

[538] RAND Study, *supra* note 5.

[539] Internet survey administered to members of the American Life Panel; 654 (out of 1000) households completed the survey.

in Table 8) provides an overview of the most commonly used titles by services provided. As shown in the table, financial professionals providing brokerage services use a large variety of titles to describe their business and the services that they offer, including "financial advisor," "financial consultant," "banker," and "broker." Around 31% of professionals providing only brokerage services used titles containing the terms "adviser" or "advisor." Professionals providing advisory services or both brokerage and advisory services similarly also use a wide variety of titles, but the proportion of professionals who use titles containing the terms "adviser" or "advisor" are somewhat larger at 35%. Note that the RAND Study did not distinguish financial professionals' use of tiles based on whether they were RRs or IARs, but rather by type of services provided.

Table 8: Replication of Table 6.3 of the RAND Study –
Professional Titles Most Commonly Reported by Respondents

Title	All Individual Professionals	Provide Advisory Services Only	Provide Brokerage Services Only	Provide Both Types of Services
Advisor	11	1	1	9
Banker	21	2	8	11
Broker, stockbroker, or registered representative	38	0	8	30
CFP (Certified Financial Planner)	21	3	3	15
Financial adviser or financial advisor	78	7	11	60
Financial consultant	25	2	0	23
Financial planner	44	6	1	37
Investment adviser or investment advisor	22	3	3	16
President or vice president	20	0	2	18

2. Investor Account Statistics

Investors seek financial advice and services to achieve a number of different goals, such as saving for retirement or children's college education. As shown above in Figures 2 and 3, the number of retail investors and their assets under management associated with investment advisers has increased significantly, particularly since 2012. As of December 2016, nearly $24.2 trillion is invested in retirement accounts, of which $7.5 trillion is in IRAs.[540] In 2016, a total of 43.3 million U.S. households have either an IRA or a brokerage account, of which an estimated 20.2 million U.S. households have a brokerage account and 37.7 million households have an IRA (including 72% of households that also hold a brokerage account).[541] Table 9 below provides an overview of account ownership segmented by account type (e.g., IRA, brokerage, or both) and investor income category based on the Survey of Consumer Finances (SCF).[542]

Table 9: Ownership by Account Type in the U.S. by Income Group (as reported by the 2016 SCF)

Income Category	% Brokerage Only	% IRA Only	% Both Brokerage and IRA
Bottom 25%	1.2%	7.6%	2.4%
25% - 50%	3.2%	14.5%	5.4%
50% - 75%	4.1%	21.4%	11.4%
75% - 90%	7.5%	33.4%	16.5%

540 *See* ICI Research Perspective, *The Role of IRAs in U.S. Households' Saving for Retirement, 2016* (Jan. 2017), *available at* https://www.ici.org/pdf/per23-01.pdf.

541 The data is obtained from the Federal Reserve System's 2016 Survey of Consumer Finances ("SCF"), a triennial survey of approximately 6,200 U.S. households and imputes weights to extrapolate the results to the entire U.S. population. As noted, some survey respondent households have both a brokerage and an IRA. Federal Reserve, *Survey of Consumer Finances* (2016), *available at* https://www.federalreserve.gov/econres/scfindex.htm. The SCF data does not directly examine the incidence of households that could use advisory accounts instead of brokerage accounts; however, some fraction of IRA accounts reported in the survey could be those held at investment advisers.

542 *Id.* To the extent that investors have IRA accounts at banks that are not also registered as broker-dealers, our data may overestimate the numbers of IRA accounts held by retail investors that could be subject to this proposed rulemaking.

Top 10%	12.0%	24.7%	43.9%
Average	4.4%	18.3%	11.6%

One question in the SCF asks what sources of information households' financial decision-makers use when making decisions about savings and investments. Respondents can list up to fifteen possible sources from a preset list that includes "Broker" or "Financial Planner" as well as "Banker," "Lawyer," "Accountant," and a list of non-professional sources.[543] Panel A of Table 10 below presents the breakdown of where households who have brokerage accounts seek advice about savings and investments. The table shows that of those respondents with brokerage accounts, 23% (4.7 million households) used advice services of broker-dealers for savings and investment decisions, while 49% (7.8 million households) took advice from a "financial planner." Approximately 36% (7.2 million households) sought advice from other sources such as bankers, accountants, and lawyers. Almost 25% (5.0 million households) did not use advice from the above sources.

Panel B of Table 10 below presents the breakdown of advice received for households who have an IRA. 15% (5.7 million households) relied on advice services of their broker-dealers, 48% (18.3 million households) obtained advice from financial planners. Approximately 41% (15.5 million households) sought advice from bankers, accountants, or lawyers, while the 25% (9.5 million households) used no advice or sought advice from other sources.

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543 The SCF specifically asks participants "Do you get advice from a friend, relative, lawyer, accountant, banker, broker, or financial planner? Or do you do something else?" (*see* Federal Reserve, *Codebook for 2016 Survey of Consumer Finances* (2016), *available at* https://www.federalreserve.gov/econres/files/codebk2016.txt). Other response choices presented by the survey included "Calling Around," "Magazines," "Self," "Past Experience," "Telemarketer," and "Insurance Agent," as well as other choices. Respondents could also choose "Do Not Save/Invest." The SCF allows for multiple responses, so these categories are not mutually exclusive. However, we would note that the list of terms in the question did not specifically include "investment adviser."

Table 10, Panel A: Sources of Advice for Households who have a Brokerage Account in the U.S. by Income Group[544]

Income Category	% Taking Advice from Brokers	% Taking Advice from Financial Planners	% Taking Advice from Lawyers, Bankers, or Accountants	% Taking no Advice or from Other Sources
Bottom 25%	20.55%	53.89%	35.64%	24.30%
25% - 50%	22.98%	38.03%	43.92%	32.36%
50% - 75%	20.75%	52.00%	31.42%	23.61%
75% - 90%	22.56%	48.94%	32.25%	28.10%
Top 10%	25.29%	50.53%	38.47%	21.06%
Average	23.02%	49.02%	35.99%	24.94%

Table 10, Panel B: Sources of Advice for Households who have an IRA in the U.S. by Income Group[545]

Income Category	% Taking Advice from Brokers	% Taking Advice from Financial Planners	% Taking Advice from Bankers, Accountants, or Lawyers	% Taking no Advice or from Other Sources
Bottom 25%	12.14%	38.30%	43.69%	31.85%
25% - 50%	9.79%	43.82%	40.67%	32.74%
50% - 75%	14.93%	45.20%	41.23%	25.23%
75% - 90%	14.68%	52.14%	41.65%	24.26%
Top 10%	21.40%	55.40%	40.03%	18.56%
Average	15.25%	48.45%	41.17%	25.28%

3. Investor Perceptions about Broker-Dealers and Investment Advisers

Although many retail investors rely on broker-dealers and investment advisers to help them achieve financial goals, evidence indicates that many retail investors do not understand, or are confused by, among other items, the different standards of conduct applicable to broker-dealers and investment advisers, and are also confused and potentially misled by the titles used

544 *Id.*

545 *Id.*

by firms and financial professionals. In the subsections below, we review in greater detail five aspects of investor perceptions with respect to: 1) how investors search for financial professionals and firms and; 2) the nature of the relationship with their financial professional (investment adviser or broker-dealer) and the meaning of company names and professional titles; 3) the structure and level of fees in the industry; 4) the existing conflicts of interest; 5) and the disciplinary history of the financial professional or firm.

g. How investors select financial firms or professionals

A number of surveys show that retail investors predominantly find their current financial firm or financial professional from personal referrals by family, friends, or colleagues.[546] For instance, the RAND Study reported that 46% of survey respondents indicated that they located a financial professional from personal referral, although this percentage varied depending on the type of service provided (*e.g.*, only 35% of survey participants used personal referrals for brokerage services). After personal referrals, RAND survey participants ranked professional referrals (31%), print advertisements (4%), direct mailings (3%), online advertisements (2%), and television advertisements (1%), as their source of locating individual professionals. The RAND Study separately inquired about locating a financial firm, which yielded substantially different results from the selection of the financial professional.[547] Respondents reported selecting financial firm (of any type) based on: referral from family or friends (29%), professional referral (18%), print advertisement (11%), online advertisements (8%), television advertisements (6%), direct mailings (2%), with a general "other" category (36%).

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546 S*ee* RAND Study, *supra* at 5; 917 Financial Literacy Study, *supra* note 20.

547 The Commission notes that only one-third of the survey respondents that responded to "method to locate individual professionals" also provided information regarding locating the financial firm.

The 917 Financial Literacy Study provides similar responses, although it allowed survey respondents to identify multiple sources from which they obtained information that facilitated the selection of the current financial firm or financial professional.[548] In the 917 Financial Literacy Study,[549] 51% of survey participants received a referral from family, friends, or colleagues. Other sources of information or referrals came from: referral from another financial professional (23%), online search (14%), attendance at a financial professional-hosted investment seminar (13%), advertisement (e.g., television or newspaper) (11.5%), other (8%), while approximately 4% did not know or could not remember how they selected their financial firm or financial professional. Twenty-five percent of survey respondents indicated that the "name or reputation of the financial firm or financial professional" affected the selection decision.

h. Nature of the relationship

Comment letters as well as several studies provide us with information about retail investor confusion about the distinctions among different types firms and financial professionals. Several commenters in response to Chairman Clayton's recent Request for Comment highlighted investor confusion about whether financial services providers are subject to the fiduciary duty.[550] Particularly, some commenters tied investor confusion about the standard of care applicable to financial service providers to the names or titles of such firms and financial professionals.[551] Similarly, during the public comment process as part of the 913 Study, commenters indicated that retail investors did not understand or found confusing the distinctions between broker-

548 *See* 917 Financial Literacy Study, *supra* note 20.

549 The data used in the 917 Financial Literacy Study comes from the Siegel & Gale *Investor Research Report* (Jul. 26, 2012), *available at* https://www.sec.gov/news/studies/2012/917-financial-literacy-study-part3.pdf, at 249 – 250.

550 *See, e.g.*, CFA 2017 Letter; PIABA 2017 Letter; IAA 2017 Letter; Pefin 2017 Letter.

551 *See* Chamber 2017 Letter, at 10; Committee for the Fiduciary Standard 2017 Letter, at 3; Pefin 2017 Letter, at 9.

dealers and investment advisers, for example, in terms of services provided and applicable standards of care.[552] Investor advocate groups submitted comments that reiterated the view that many market participants also believe that financial professionals should act in investors' best interests.[553] 913 Study commenters also expressed beliefs that certain titles used by firms and financial professionals are confusing to investors.[554]

Further findings of investor confusion about the roles and titles of financial professionals comes from studies conducted by Siegel & Gale[555] in 2004, RAND [556] in 2008 and CFA in 2010.[557] The Siegel & Gale Study found that focus group participants did not understand that the roles and legal obligations of broker-dealers differed from investment advisers, and were further confused by different labels or titles used by advice providers (e.g., financial planner, financial advisor, financial consultant, broker-dealer, or investment adviser). More specifically, participants in the Siegel & Gale Study focus groups believed that brokers executed trades and

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552 *See* 913 Study, *supra* note 3, at section III.A.

553 *Id. See also* AFL-CIO 2017 Letter; AARP 2017 Letter.

554 *See, e.g.*, Comment letters on 913 Study, *available at* https://www.sec.gov/comments/4-606/4-606.shtml. Comment letter of Bert Oshiro (Aug. 29, 2010) ("Years ago, I was pretty sure who I was dealing with based on their titles… Today it's a totally different story. All kinds of products such as securities, insurance, fee based products, bank accounts, loans, health insurance, auto/homeowners insurance, etc. are sold by people calling themselves: financial advisors; financial consultants; investment advisors; investment consultants; financial planners; asset managers; financial services advisors; [and] registered representatives… It has come to the point that I really don't know who I'm dealing with."); Comment letter of Larry J. Massung (Aug. 29, 2010) ("I believe there is considerable confusion within the general public with the fiduciary duty, responsibilities, and titles of brokers, dealers and investment advisors"); and Comment letter of Cecylia Escarcega (Aug. 30, 2010) ("Personally, I find the titles confusing because the broker, dealer or investment advisor typically does not tell me what their role is and the scope of their fiduciary duty to me as an investor").

555 The Commission retained Siegel and Gale in 2004 to conduct the focus group testing in order to determine how investors distinguish the roles, legal obligations, and compensation structures between broker-dealers and investment advisers. *See* Siegel & Gale Study, *supra* note 549.

556 The RAND Study contained two components: (1) an analysis of business practices at broker-dealers and investment advisers based on regulatory filings and interviews with stakeholders (including members of the broker-dealer and investment adviser industries); and (2) a survey of 654 households or focus group testing on household investment behavior and preferences, experience with financial service providers, and understanding of the different types of providers. *See* RAND Study, *supra* note 5.

557 *See* CFA Survey, *supra* note 5.

were focused on "near-term" advice, while financial advisors and consultants provided many of the same services as brokers, but also provided a greater scope of long-term planning advice (e.g., portfolio allocation). "Investment adviser," on the other hand, was a term unfamiliar to many participants, but financial professionals using this label were perceived to provide similar services to financial advisors and financial consultants. Financial planners were viewed to provide services related to insurance and estate planning in addition to investment advice, and encompassed long-term financial planning including college, retirement, and other long-term savings and investment goals. The Siegel & Gale Study focus group participants assumed that financial advisors/consultants, investment advisers, and financial planners provided planning services, while brokers, financial advisors/consultants, and investment advisers provided trade execution services.[558] Further, the focus group participants generally did not understand certain legal terms, such as "fiduciary."

Similarly, the RAND Study generally concluded that investors did not understand the differences between broker-dealers and investment advisers and that common job titles contributed to investor confusion.[559] Further, participants responded similarly that investment advisers and brokers are required to act in the client's best interest. Similar to the Siegel and Gale Study, focus group participants did not understand the term fiduciary, or how the fiduciary

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558 The Commission notes that the results of the Siegel & Gale Study relied on a small sample of focus group testing conducted over a decade ago. While relevant to our understanding of investor perception about broker-dealers and investment advisers, the results of the study may not reliably reflect the current views of the general population of U.S. retail investors.

559 RAND study participants "commented that the interchangeable titles and 'we do it all' advertisements [by broker-dealers] made it difficult to discern broker-dealers from investment advisers." Although the RAND Study indicates that investors are confused the services provided and the titles used by financial professionals, more than 70% of participants also answered that they were "very satisfied with the service received from the firm," that "they trust the firm acts in their best interest," and that "the firm provides a valuable service." These numbers increased to 80% when the length of time spent at a firm was at least 10 years. The Commission notes that the results of the RAND Study relied on testing conducted nearly 10 years ago; therefore, the results of the study may not reliably reflect the current views of the general population of U.S. retail investors

standard differed from suitability. In addition, the RAND Study noted that the confusion about titles, services, legal obligations, and compensation persisted even after a fact sheet on broker-dealers and investment advisers was provided to participants.[560]

Similar to the Siegel and Gale Study and the RAND Study, the CFA Survey concluded that investors do not understand differences between broker-dealers and investment advisers, or the standards of conduct that apply to advice or recommendations made by these firms. For example, approximately 34% of investors surveyed believed that "offering advice" was a primary service of broker-dealers.[561] With respect to conduct-related questions, 91% of those surveyed believed that broker-dealers and investment advisers should follow the same investor protection rules if providing the same sort of advisory services, while 85% believed that the person providing advice should put the retail customer's interest ahead of theirs and should disclose fees and commissions earned or any conflicts of interest that could affect the advice provided. More than two-thirds believed that a fiduciary duty is owed to customers by broker-dealers, suggesting a degree of investor confusion.[562]

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560 *See* RAND Study, *supra* note 5, at 111. The fact sheet provided to RAND Study participants included information on the definition of broker and investment adviser, including a description of common job titles, legal duties and typical compensation. Participants in the RAND Study focus groups indicated that they were confused over common job titles of broker-dealers and investment advisers, thought that because brokers are required to be licensed, investment advisers were not as qualified as brokers, deemed the term "suitable" too vague, and concluded that it would be difficult to prove whether or not an investment adviser was not acting in the client's best interest.

561 *See* CFA Study, *supra* note 5.

562 In some circumstances, broker-dealers may owe a fiduciary duty to their customers. For example, there is a body of case law holding that broker-dealers that exercise discretion or control over customer assets, or have a relationship of trust and confidence with their customers, owe customers a fiduciary duty, or the scope of obligations that attach by virtue of that duty. *See, e.g., U.S. v. Skelly*, 442 F.3d 94, 98 (2d Cir. 2006) (fiduciary duty found "most commonly" where "a broker has discretionary authority over the customer's account"); *United States v. Szur*, 289 F.3d 200, 211 (2d Cir. 2002) ("Although it is true that there 'is no general fiduciary duty inherent in an ordinary broker/customer relationship,' a relationship of trust and confidence does exist between a broker and a customer with respect to those matters that have been entrusted to the broker.") (citations omitted); *Leib v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 461 F. Supp. 951, 953-954 (E.D. Mich. 1978), *aff'd,* 647 F.2d 165 (6th Cir. 1981) (recognizing that a broker who has de facto control over non-discretionary account generally owes customer duties of a fiduciary

i. Fees

The 917 Financial Literacy Study showed that, prior to engaging an investment adviser,[563] approximately 76.4% of survey participants indicated that disclosure of the fees and compensation of investment advisers was an absolutely essential element to any disclosure.[564] With respect to how investors prefer information about fees and compensation to advisers, 23% of respondents preferred a table format with examples, 21% preferred a bulleted format with examples, 20% preferred a bulleted format, and 12% preferred a table format.[565]

In 2015, FINRA conducted an "Investor Survey" which included questions about investors' understanding of fees charged for investment services.[566] Approximately 70% of survey participants reported that they thought investment firm (generically referred to as "adviser" in the study) compensation and account fees to be very clear, with less than 4% stating that they thought compensation to be unclear. Between 54.7% and 57.6% of respondents indicated that they considered account fees to be "reasonable," while between 0% and 2.3% of respondents indicated that account fees were not reasonable. Of investors that have commission-based accounts, approximately 28% believed that commissions did not affect advice given.

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nature; looking to customer's sophistication, and the degree of trust and confidence in the relationship, among other things, to determine duties owed); Arleen W. Hughes, Exchange Act Release No. 4048 (Feb. 18, 1948) (Commission Opinion), *aff'd sub nom. Hughes v. SEC*, 174 F.2d 969 (D.C. Cir. 1949) (noting that fiduciary requirements generally are not imposed upon broker-dealers who render investment advice as an incident to their brokerage unless they have placed themselves in a position of trust and confidence, and finding that Hughes was in a relationship of trust and confidence with her clients).

563 The 917 Financial Literacy Study, *supra* note 20, uses the term financial intermediary when discussing the importance of certain disclosures of firms or financial professionals.

564 *See* 917 Financial Literacy Study, *supra* note 20, at 67.

565 23% of respondents also preferred the "status quo" – "the way it was presented" in the example .

566 *See* FINRA Report on Conflicts of Interest, (Oct. 2013), at 6, *available at* http://www.finra.org/sites/default/files/Industry/p359971.pdf ("Investor Survey").

Those percentages decline to 15% or less when asked to consider whether selling incentives and third party compensation had not affected the advice provided by investment firms.

Table 11: Investor Perception of Compensation to Financial Professionals (as obtained from the 2015 FINRA Investor Survey)

	Unadvised (%)	Advised: Asset Fee (%)	Advised: Commission-based Fee (%)
Advisor Compensation Clear?			
Very	NA	70.9	68.5
Somewhat	NA	27.6	28.0
Not	NA	1.5	3.5
Account Fees Clear?			
Very	68.0	70.3	74.7
Somewhat	29.0	29.7	23.5
Not	2.9	0	1.8
Account Fees Reasonable?			
Agree	55.6	54.7	57.6
Somewhat Agree	42.1	45.3	40.2
Disagree	2.3	0	2.2
Commissions Affect Advice?			
Great Deal	58.3	21.8	29.7
Somewhat	32.8	57.8	42.5
Not At All	8.9	20.4	27.7
Selling Incentives Affect Advice?			
Great Deal	66.1	41.9	44.3
Somewhat	28.4	43.7	40.6
Not At All	5.5	14.4	15.1
Third Party Compensation Affects Advice?			
Great Deal	68.6	32.8	41.4
Somewhat	26.3	56.4	45.3
Not At All	5.1	10.8	13.4

Academic evidence also indicates that retail investors exhibit limited understanding of the fees and commissions of financial products. Several academic studies show that even when

disclosures are provided to investors, investors experience difficulty in accounting for and understanding how fees affect their financial choices.[567]

j. Conflicts of interest

Studies have found that investors consider conflicts of interest to be an important factor in the market for financial advice. For example, in the 917 Financial Literacy Study,[568] approximately 52.1% of survey participants indicated that an essential component of any disclosure would be their financial intermediary's conflicts of interest, while 30.7% considered information about conflicts of interest to be important, but not essential. Investors also were asked to rate their level of concern about potential conflicts of interest that their adviser might have. Approximately 36% of the investors expressed concerns that their adviser might recommend investments in products for which its affiliate receives a fee or other compensation, while 57% were concerned that their adviser would recommend investments in products for which it gets paid by other sources. In addition to conflicts directly related to compensation practices of financial professionals, some investors were concerned about conflicts related to the trading activity of these firms. For example, more than 26% of participants were concerned that an adviser might buy and sell from its account at the same time it is recommending securities to

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567 Experimental evidence from the U.S. mutual fund market is provided by, James J. Choi, David Laibson, & Brigitte C. Madrian, *Why Does the Law of One Price Fail? An Experiment on Index Mutual Funds* Review of Financial Studies 23(4): 1405-1432 (Nov. 14, 2009) ("Choi Laibson Article") (finding that experimental subjects fail to minimize fees among four different actual S&P 500 index funds and 80-90% of the subjects in the study presented with simplified fee disclosures still failed to select the lowest-priced options among products with similar characteristics). Field-based evidence from the payday loans market is provided by, Marianne Bertrand & Adair Morse, *Information Disclosure, Cognitive Biases, and Payday Borrowing*, The Journal of Finance 46(6): 1865-1893 (Nov. 14, 2011). For a comprehensive survey of the literature see George Loewenstein, Cass R. Sunstein, & Russell Golman, *Disclosure: Psychology Changes Everything*, Annual Review of Economics 6: 391-419 (Aug. 2014) ("Loewenstein Sunstein Article").

568 Section 917 of the Dodd-Frank Act further required the Commission to conduct a study to identify the level of financial literacy among retail investors as well as methods and efforts to increase the financial literacy of investors. *See* 917 Financial Literacy Study, *supra* note 20.

investors; and more than 55% of investors were also concerned about their adviser's engaging in principal trading.

Approximately 70% of the participants in the 917 Financial Literacy Study indicated that they would read disclosures on conflicts of interest if made available, with 48% requesting additional information from their adviser, 41% increasing the monitoring of their adviser, and 33% proposing to limit their exposure of specific conflicts. The majority of investors (70%) also wanted to see specific examples of conflicts and how those related to the investment advice provided. Academic research also suggests that information about conflicts of interest could improve individual decisions.[569]

k. Disciplinary history

Survey evidence indicates that knowledge of a firm's and financial professional's disciplinary history is among the most important items for retail investors deciding whether to receive financial services from a particular firm, according to one study.[570] Despite this, most investors do not actively seek disciplinary information for their advisers and broker-dealers.[571] A recent FINRA survey, however, found that only 15% of survey respondents checked their financial professional's background, although the Commission notes that the study encompasses

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569 *See* S. Sah & G. Loewenstein, *Nothing to declare: mandatory and voluntary disclosure leads advisors to avoid conflicts of interest*, Psychological Science 25, 575–584 (2014).

570 *See* 917 Financial Literacy Study, *supra* note 20, at nn. 311 and 498 and accompanying text (Approximately 67.5% of the online survey respondents considered information about an adviser's disciplinary history to be absolutely essential, and about 20.0% deemed it important, but not essential, and "When asked how important certain factors would be to them if they were to search for comparative information on investment advisers, the majority of online survey respondents identified the fees charged and the adviser's disciplinary history as the most important factors.").

571 For example, the FINRA 2015 Investor Survey finds that only 24% of investors are aware of Investor.gov; only 16% are aware of BrokerCheck; only 14% are aware of the IAPD website, and only 7% have used BrokerCheck. Investor Survey, *supra* note 566.

a wide group of advisers, such as debt counselors and tax professionals.[572] Another FINRA survey found that only 7% of survey respondents use FINRA's BrokerCheck and approximately 14% of survey respondents are aware of the Investment Adviser Public Disclosure (IAPD) website.[573]

B. Form CRS Relationship Summary

1. Broad Economic Considerations

We are proposing to require broker-dealers, investment advisers, and firms that are dually registered to deliver a relationship summary to retail investors.[574] The economic tradeoffs involved in disclosures made by financial firms and financial professionals are complex and affected by a wide range of factors, which we consider in more detail below. In this section, we discuss the characteristics of disclosures that may effectively convey information that is useful to retail investors when they are searching for a financial firm and to facilitate matching between retail investors' expectations and the choice of financial firm or financial professional.

Disclosure requirements provide benefits to participants in financial markets because disclosing parties may lack private incentives to voluntarily disclose or standardize relevant information.[575] Disclosure can benefit not only investors but also the disclosing parties,[576] as well as provide indirect benefits to financial markets.[577]

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572 2009 National Survey Initial Report, *supra* note 275.

573 *See* Investor Survey, *supra* note 566.

574 *See supra* Section 0.

575 *See, e.g.,* Confirmation Requirements and Point of Sale Disclosure Requirements for Transactions in Certain Mutual Funds and Other Securities, and Other Confirmation Requirement Amendments, and Amendments to the Registration Form for Mutual Funds, Exchange Act Release No. 8358 (Jan. 29, 2004) [69 FR 6437 (Feb. 10, 2004)] ("The Commission believes that permitting investors to more readily obtain information about distribution-related costs that have the potential to reduce their investment returns and to give investors a better understanding of some of the distribution-related arrangements that create conflicts of interest for brokers, dealers, municipal securities dealers, and their associated natural persons. The disclosure of information about these costs and arrangements can help investors make better informed

Although the majority of the information proposed for Form CRS may be publicly available in a number of existing regulatory forms and platforms, including, for example, Form ADV (and IAPD) or BrokerCheck, or may be included in disclosures developed to meet disclosure requirements under DOL regulations or exemptions, such as the BIC Exemption, the Commission preliminary believes that all retail investors would benefit from short summary disclosure that focuses on certain aspects of a firm and its services to retail investors which could be supplemented by additional disclosure. Like other public-facing disclosures, the objective of Form CRS would be to provide relevant and reliable information to investors. The relationship summary would apply to a broad array of relationships, spanning different firms as well as both retirement and non-retirement accounts.[578] By requiring both investment advisers and broker-dealers to deliver to existing and prospective retail investors and file a publicly available concise relationship summary that discusses, in one place, both types of services and their differences, the proposed rules for Form CRS would also help retail investors to compare certain different types of accounts and firms.

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investment decisions."). *See also* P. Healy & K. Palepu, *Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical corporate disclosure literature*, Journal of Accounting and Economics 31, 405-440 (2001).

576 *See*, Michael Jensen & William Meckling, *Theory of the firm: Managerial behavior, agency costs, and ownership structure*, Journal of Financial Economics 3, 305-360 (1976); Patel, S. and G. Dallas, *Transparency and disclosure: Overview of methodology and study results*, United States, Standard & Poor's, New York (2002); A. Ferrell, *Mandatory disclosure and stock returns: Evidence from the over-the-counter market*, The Journal of Legal Studies 36, 213-253 (2007). Regarding the effect of corporate disclosures on improved corporate governance, *see, e.g.* B. Hermalin & M. Weisbach, *Transparency and corporate governance*, NBER Working paper No. W12875 (2007); R. Lambert, C. Leuz, & R. Verrecchia, *Accounting information, disclosure, and the cost of capital*, Journal of Accounting Research 45, 385-420 (2007).

577 *See* L. Holder-Webb, J. Cohen, L. Nath, & D. Wood, *A survey of governance disclosures among U.S. firms*, Journal of Business Ethics 83, 543-563 (2008); Z. Rezaee, *Causes, consequences, and deterrence of financial statement fraud*, Critical Perspectives on Accounting 16, 277-298 (2005).

578 For comparison, the disclosure conditions under applicable DOL regulations and exemptions apply only to financial firms and financial professionals servicing IRAs and ERISA-covered retirement plans and participants in such plans.

Given that most of the information provided by Form CRS would already have been made available by investment advisers through other regulatory disclosures, and by some broker-dealers through contracts or other voluntary disclosures, the focus of this economic analysis is on the effects of the format and structure of the proposed Form CRS disclosures. Studies have found that the format and structure of disclosure may improve (or decrease) investor understanding of the disclosures being made.[579]

Before elaborating on the characteristics of an effective disclosure regime, we note that some studies undertaken outside the market for financial services find that sometimes certain disclosures may result in unintended consequences. In general, the structure of the disclosure may affect the choices that investors make. Every disclosed item not only presents a piece of new information to retail investors but also provides a frame within which all other items are evaluated.[580] This framing effect could lead investors to draw different conclusions depending on how information is presented. For example, if the disciplinary history information is presented first, it could affect the way investors perceive all subsequent disclosures in the relationship summary and, possibly, discount more heavily the information provided by firms with disciplinary events than by firms with clean record. The effect of the disciplinary history information would be moderated if this information is provided at the end of the relationship summary.

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579 *See*, Justine S. Hastings & Lydia Tejeda-Ashton, *Financial Literacy, Information, and Demand Elasticity: Survey and Experimental Evidence from Mexico*, NBER Working Paper 14538 (Dec. 2008) (finding that providing fee disclosures to Mexican investors in peso rather than percentage terms caused financially inexperienced investors to focus on fees); *See*, Richard G. Newell & Juha Siikamaki, *Nudging Energy Efficiency Behavior*, Resources for the Future Discussion Paper 13-17 (Jul. 10, 2013) (finds that providing dollar operating costs in simplified energy efficiency labeling significantly encouraged consumers to choose higher energy efficiency appliances, while another related study presents similar evidence from payday loans).

580 *See* Tversky, A., Kahneman, D., 1981. The framing of decisions and the psychology of choice. Science 211, 453–458 ("Tversky Kahneman Article").

Existing research has also found that conflict of interest disclosures can increase the likelihood that the disclosing party would act on the conflict of interest.[581] This bias can be caused by "moral licensing," a belief that the disclosing party has already fulfilled its moral obligations in the relationship and therefore can act in any way, or it can be caused by "strategic biasing," aimed at compensating the disclosing party for the anticipated loss of profit due to the disclosure.[582] Experimental evidence also suggests that disclosure could turn some clients or customers into "reluctant altruists."[583] For example, if financial professionals disclose that they earn a referral fee if a customer enrolls in a program, the customer may implicitly feel that they are being asked to help their financial professional receive the fee. One study also found evidence that disclosure of a professional's financial interests (particularly in face-to-face interactions) can induce a panhandler effect, whereby customers may face an implicit social pressure to meet the professional's financial interests.[584] The above literature indicates that conflicts of interest disclosures could undermine the intended benefits of the disclosures for investors if investors become reluctant altruists or feel an obligation to succumb to the panhandler effect. However, these studies also suggest certain factors that may mitigate the

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581 *See*, Daylian Cain, George Loewenstein & Don Moore, *The Dirt on Coming Clean: Perverse Effects of Disclosing Conflicts of Interest*, Journal of Legal Studies 34: 1-25 (Jan. 2005) ("Cain 2005 Article"); Daylian Cain, George Loewenstein & Don Moore, *When Sunlight Fails to Disinfect: Understanding the Perverse Effects of Disclosing Conflicts of Interest*, Journal of Consumer Research 37: 1-45 (Aug. 27, 2010); Bryan Church & Xi Kuang, *Conflicts of Disclosure and (Costly) Sanctions: Experimental Evidence*, Journal of Legal Studies 38 2: 505-532 (Jun. 2009); Christopher Tarver Robertson, *Biased Advice*, Emory Law Journal 60: 653-703 (Feb. 17, 2011). These papers study conflicts of interest in general, experimental settings, not specialized to the provision of financial advice.

582 Although disclosures in general may cause negative unintended consequences, existing rules and regulations for broker-dealers and investment advisers, as well as proposed Regulation Best Interest, are likely to moderate the effects of moral licensing or strategic bias for financial professionals.

583 *See* J. Dana, D. Cain & R. Dawes, *What you don't know won't hurt me: Costly (but quiet) exit in dictator games*, Organizational Behavior and Human Decision Processes 100:193–201 (2006).

584 Daylian Cain, George Loewenstein & Don Moore, *The burden of disclosure: Increased compliance with distrusted advice*, Journal of Personality and Social Psychology, 104(2): 289-304 (2013) ("Burden of Disclosure Article").

unintended consequences. For example, in the case of the "panhandler effect," researchers have found that distancing the client or customer from the financial professional either in the decision or disclosure phase can dampen this effect.[585]

Academic research has identified a set of characteristics, including targeted and simple disclosures, salience, and standardization, that may increase the effectiveness of a disclosure regime. Adhering to these characteristics is expected to increase the benefits of a disclosure document to consumers. These characteristics, discussed below, frame our analysis of the economic impacts of the proposed rule.[586]

First, existing research demonstrates that individuals exhibit limited ability to absorb and process information.[587] These cognitive limitations suggest that more targeted and simpler disclosures may be more effective in communicating information to investors than more complex disclosures. As discussed more thoroughly below, costs, such as increased investor confusion or reduced understanding of the key elements of the disclosure, are likely to increase as disclosure documents become longer, more convoluted, or more reliant on narratives.[588] Moreover, empirical evidence suggests that simplification benefits consumers of disclosed information.[589]

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585 *See id.*

586 *See* Loewenstein Sunstein Article, *supra* note 567. The paper provides a comprehensive survey of the literature relevant to disclosure regulation.

587 *See* Nisbett RE & Ross L. *Human Inference: Strategies and Shortcomings of Social Judgment* (1980). Englewood Cliffs, NJ: Prentice Hall. David Hirshleifer & Siew Hong Teoh, *Limited attention, information disclosure, and financial reporting*, Journal of Accounting and Economics 36, 337-386 (Dec. 2003).

588 *See, e.g.*, S.B. Bonsall IV & B.P. Miller, *The Impact of Narrative Disclosure Readability on Bond Ratings and the Cost of Capital*, The Review of Accounting Studies 2 (2017) and A. Lawrence, *Individual Investors and Financial Disclosure*, Journal of Accounting & Economics 56, 130–47 (2013).

589 *See supra* notes 35, 46 – 48 and accompanying text. *See also* S. Agarwal, S. Chomsisengphet, N. Mahoney & J. Stroebel, *Regulating consumer financial products: evidence from credit cards*, NBER Working Paper 19484 (Jun. 2014) (finding that a series of requirements in the Credit Card Accountability Responsibility and Disclosure Act (CARD Act), including several provisions designed to promote simplified disclosure, has produced substantial decreases in both over-limit fees and late fees, thus saving U.S. credit card users $12.6 billion annually).

These results appear to support requirements of simple disclosures, which provide benefits to consumers of that information.

A second characteristic of an effective disclosure is salience, or the tendency to 'stand out' or contrast with other information on a page. Salience detection is a key feature of the human cognition allowing individuals to focus their limited mental resources on a subset of the available information and causing them to over-weight this information in their decision making processes.[590] Within the context of disclosures, more salient information, such as information presented in bold text, would be more effective in attracting attention than less salient information, such as information presented in a footnote. There is also empirical evidence that visualization improves individual perception of information.[591] For example, one experimental study shows that tabular reports lead to better decision making and graphical reports lead to faster decision making (when people are subject to time constraints).[592]

A third characteristic of effective disclosure is standardization. People are generally able to make more coherent and rational decisions when they have comparative information that allows them to assess relevant trade-offs.[593] Standardization could be particularly important for

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590 Daniel Kahneman, *Thinking, Fast and Slow*, New York: Farrar, Strauss, Giroux (2013). Susan Fiske & Shelley E. Taylor, *Social cognition: From Brains to Culture*, SAGE Publications Ltd; 3rd ed. (2017).

591 J. Hattie, *Visible learning. A synthesis of over 800 meta-analyses relating to achievement*, Oxon: Routledge (2008) ("Hattie").

592 I. Benbasat & A.S. Dexter, *An Investigation of the Effectiveness of Color and Graphical Presentation under Varying Time Constraints*, MIS Quarterly 10, 59-83 (Mar. 1986) ("Benbasat & Dexter").

593 *See, e.g.*, JR Kling, S. Mullainathan, E. Shafir, LC Vermeulen & MV Wrobel, *Comparison friction: experimental evidence from Medicare drug plans*, Quarterly Journal of Economics 127, 199–235 (2012) (finding that in a randomized field experiment, in which some senior citizens choosing between Medicare drug plans that were randomly selected to receive a letter with personalized, standardized, comparative cost information ("the intervention group") while another group ("the comparison group") received a general letter referring them to the Medicare website, plan switching was 28% in the intervention group, but only 17% in the comparison group, and the intervention caused an average decline in predicted consumer cost of about $100 a year among letter recipients); CK Hsee, GF Loewenstein, S. Blount & MH Bazerman, *Preference reversals between joint and separate evaluations of options: a review and theoretical analysis*, Psychological Bulletin 125, 576–590 (Oct. 2006).

the disclosure of certain quantitative aspects of financial services, such as the level and structure of fees.

Finally, personalization may further enhance the effectiveness of disclosure.[594] This approach might involve, for example, adjusting the presentation to take account of the receiver's interests, expectations, or format preferences or to tailor the information based on what the receiver already knows in order not to repeat existing knowledge. Personalization is usually achieved at the expense of standardization, however, and can be costly to create.

Current reporting and disclosure requirements for broker-dealers and registered investment advisers including Form BD and Form ADV may provide detailed information to investors. However, because these existing reports and disclosures (which serve the purposes for which they were created) are made in multiple, sometimes lengthy forms, and made available at different websites or delivery methods, it can be difficult for investors to grasp the most important features of the financial services and products they receive. In addition, the information available to retail investors about broker-dealers on BrokerCheck does not include the same information that investment advisers provide in the Form ADV brochure and brochure supplement. The relatively low financial literacy of many investors also makes it less likely that they would be able to effectively compile this information on their own and use it in their decision making. Furthermore, most financial firms and professionals could lack the incentives and resources to disclose the main aspects of their business practices to their customers in the absence of the proposed requirements.

In evaluating the broad economic issues related to disclosure, the Commission preliminarily believes that all retail investors would benefit from a short summary that focuses

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[594] *See* Loewenstein Sunstein Article, *supra* note 567.

on certain aspects of the firm and its financial professionals and its services. By requiring both investment advisers and broker-dealers to provide a concise relationship summary that discusses both types of services and their differences, the relationship summary would help all retail investors to understand these aspects of a particular firm, to compare different types of accounts, and to compare one firm with other firms. The relationship summary would also highlight, in one place, the services, some categories of fees, specified conflicts of interest, and whether the firm or its financial professionals currently have reportable disciplinary events.

2. Economic Effects of the Relationship Summary

This section analyzes the anticipated economic effects from the proposed relationship summary to the directly affected parties: retail investors, and broker-dealers and investment advisers that offer brokerage or advisory services to retail investors.[595]

a. Retail Investors

As noted above, substantial evidence suggests that retail investors lack financial literacy and do not understand many basic financial concepts, such as the implications of investment costs for investment performance.[596] This, in turn, supports the notion that a well-functioning market for financial services may provide benefits to investors by helping them obtain information and guidance from firms and financial professionals and thereby make better investment decisions. At the same time, however, evidence also suggests that investors do not fully comprehend the nature of the business relationships and responsibilities in the market which makes them vulnerable to confusion and being misled by firms and financial

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595 Economic effects of the proposal on the market for financial services, including on indirectly-affected parties such as banks or insurers that are not regulated by the SEC, are considered in the following section.

596 *See* 917 Financial Literacy Study, *supra* note 20.

professionals;[597] it also implies that any improvement of retail investor understanding of their relationship with financial professionals could improve investor's investment decisions.

The content of the proposed relationship summary is intended to alert retail investors to information that would help them to choose a firm or a financial professional and prompt retail investors to ask informed questions. It is also intended to facilitate comparisons across firms that offer the same or substantially similar services. Specifically, the relationship summary would provide information on the relationships and services offered by investment advisers and broker-dealers, the standards of conduct applicable to those services, certain categories of fees and costs of the services offered, comparisons of brokerage and investment advisory services (for standalone broker-dealers and investment advisers),[598] conflicts of interest, and some additional information, including the existence of currently reportable legal or disciplinary events. The Commission believes that the information in the relationship summary could help alleviate investor confusion and would promote effective communication between the firm and its retail investors and assist investors in making an informed choice when choosing an investment firm and professional and type of account to help to ensure they receive services that meet their preferences and expectations. Although the relationship summary applies only to broker-dealers and registered investment advisers, its impact could extend beyond the current and prospective clients of these institutions and impact a larger set of investors through various channels such as

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597 *See* 913 Study, *supra* note 3, at section III.A.; Siegel & Gale Study, *supra* note 550; RAND Study, *supra* note 5.

598 For purposes of the relationship summary, we propose to define a standalone investment adviser as a registered investment adviser that offers services to retail investors and (i) is not dually registered as a broker-dealer or (ii) is dually registered as a broker-dealer but does not offer services to retail investors as a broker-dealer. We propose to define a standalone broker-dealer as a registered broker-dealer that offers services to retail investors and (i) is not dually registered as an investment adviser or (ii) is dually registered as an investment adviser but does not offer services to retail investors as an investment adviser. Proposed General Instruction 9.(f) to Form CRS.

public filings and website posting. Both the content and the form of the relationship summary are designed to increase the likelihood that the disclosed information is consumed easily and effectively by retail investors. We discuss the potential benefits and costs of the relationship summary and its components in detail below.

i. Structure of the Relationship Summary

The structure of the relationship summary is designed to facilitate retail investors' absorption of the provided information. The proposed design intentionally restricts the length of the relationship summary, whether in electronic or paper format, to four pages on 8 ½ x 11 inch paper if converted to PDF format, with a specified font size and margin requirements. Existing research suggests that shorter disclosures help investors absorb and process information.[599] Shorter disclosure would also facilitate a layered approach to disclosure. The Commission acknowledges that a limit on overall document length (or equivalent length for electronic disclosure) may entail limiting the information provided through the relationship summary. However, based on the studies described above, we preliminarily believe that limiting the length of the relationship summary appropriately trades off the benefits of additional detail against the costs of increased complexity associated with longer disclosures. Similarly, while the required standardization across the relationship summary limits the ability of firms to provide customized information to potential retail investors, we preliminarily believe these constraints are appropriate to facilitate comparability.

In addition, firms would be required to use short sentences, active voice, and plain language throughout the relationship summary. Firms would not be permitted to use legal jargon, highly technical business terms, or multiple negatives. Existing research also shows that

[599] *See supra* Section 0.

visualization helps individuals absorb information more efficiently.[600] Consistent with this research, firms would be permitted to use graphical presentations, and dual registrants would be required in certain aspects, to use tables to simplify and highlight the information. For example, dual registrants will be required to provide a side-by-side tabular presentation of all relevant information provided in the relationship summary.

Moreover, the disclosure would involve a certain degree of standardization across firms. In particular, firms would be required to use the same headings, prescribed wording, and present the information under the headings in the same order.[601] Additionally, firms would be prohibited from adding any items to those prescribed by the Commission and any information other than what the Instructions require or permit. As discussed above, standardization facilitates comparisons of content across disclosures.[602] We believe that allowing only the required and permitted information would promote standardization of the information presented to retail investors, and would allow retail investors to focus on information that we believe is particularly helpful in deciding among firms. At the same time, we acknowledge that standardization of disclosures not only limits personalization that may be valuable to retail investors but also could result in disclosures that are less precise. Further, all information in the relationship summary must be true and not misleading. In particular, the Instructions permit firms to omit or modify any prescribed statement that is inapplicable to their business or would be misleading to a reasonable retail investor. In addition, for certain items, firms will have some flexibility in how they include the required information.

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600 *See* commenters' feedback in the Financial Literacy Study, *supra* note 20, at iv, xx, 21-22.

601 *See supra* note 593.

602 *See supra* Section IV.B.1.

ii. Introduction

The proposed Introduction of the relationship summary would highlight to retail investors the type of accounts and services the firm offers to retail investors, and the firm's SEC registration status. In addition, the introduction would require prescribed wording stating there are different ways for investors to get help with their investments, and that they should carefully consider what type of account and services would be right for them and that there are suggested questions at the end of the disclosure. An introduction designed in this manner may benefit retail investors by clarifying that there are choices available in terms of accounts and services and that the some services, firms, or financial professionals may be a better fit than others for the investor. This in turn may trigger a closer read of the relationship summary and perhaps also additional information gathering by the investor that could lead to a more informed choice of financial professional and better fit between the investor's need and the type of accounts and services they use.

iii. Relationships and Services

In the second section of the relationship summary, firms would discuss specific information about the nature, scope, and duration of its relationships and services, including the types of accounts and services the firm offers, how often it offers investment advice, and whether the firm monitors the account. As noted above, the relationships and services of firms can differ in nature, scope, and duration. The Commission believes that a better understanding of the relationships and services could lower search costs and the risk of mismatch for retail investors, by facilitating cross-firm comparisons, and make it easier for them to find a firm and a financial professional that most closely meet their expectations, depending on how important different types of fee structures, services, standards of conduct or other information points are to them.

iv. Obligations to the Retail Investor – Standard of Conduct

The third section of the relationship summary briefly describes in plain language the firm's legal standard of conduct. As noted above, studies show that many retail investors are confused about the standard of conduct that applies to firms and financial professionals,[603] and the Commission believes that providing retail investors with a brief description of legal obligations of firms and professionals could help alleviate this confusion. Furthermore, to the extent this section makes the issue of standard of conduct more salient to the investors, it may encourage additional information gathering by the investors about the standard of conduct, which could further increase investors' understanding.

Investor understanding of the obligations of their firms and financial professionals with respect to each type of account could help investors align their expectations with the expected conduct of their firm or financial professional. For example, depending on their preferences, some investors might find an advisory account more appropriate. Other investors could prefer the services and standards of conduct associated with a brokerage account. Thus, to the extent the proposed disclosure of obligations in the relationship summary increase investors understanding in this area, it may improve the match between investors' preferences and expectations and the type of accounts and services they select while preserving investor choice.

v. Summary of Fees and Costs

The Commission is also proposing that firms include an overview of specified types of fees and expenses that retail investors will pay in connection with their brokerage and investment advisory accounts.[604] This section would include a description of the principal type of fees that

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603 *See, e.g.*, Siegel & Gale Study, *supra* note 5 and RAND Study, *supra* note 5. *See also* CFA Survey, *supra* note 5.

604 *See supra* Section 0.

the firm will charge retail investors as compensation for the firm's advisory or brokerage services, including whether the firm's fees vary and are negotiable, and factors that would help a reasonable retail investor understand the fees that he or she is likely to pay. As such, the improved disclosure of the categories of fees, including wrap fees, could help improve retail investor's decision to engage a firm and a financial professional.

vi. Comparisons

The Commission is also proposing to require standalone investment advisers and standalone broker-dealers to provide comparisons to the other type of firm. Standalone broker-dealers would include information about the following: (i) the primary types of fees that investment advisers charge; (ii) services generally provided by investment advisers, (iii) advisers' standard of conduct; and (iv) certain incentives advisers have based on the investment adviser's asset-based fee structure. For investment advisers, this section would include parallel categories of information regarding broker-dealers.

The choice between a brokerage account and an advisory account in part may determine the types of fees and costs and standard of conduct associated with the account. Retail investors who are provided with more information would be more likely to match their choice of the type of account with their expectations; if retail investors do not understand the differences between of broker-dealers and investment advisers, they are less likely to be able to match their expectations for financial services providers with their choices. Thus, the Commission preliminary believes that having a clear explanation of differences in the fees, scope of services, standard of conduct, and incentives that are generally relevant to advisory and brokerage accounts may help retail investors who are considering one such type of relationship to compare how their preferences and expectations might be better met with the other type of relationship.

vii. Conflicts of interest

The Commission is also proposing that firms summarize their conflicts of interest related to certain financial incentives. Specifically, firms would be required to disclose conflicts relating to: (i) financial incentives to offer to, or recommend that the retail investor invest in, certain investments because (a) such products are issued, sponsored, or managed by the firm or its affiliates, (b) third parties compensate the firm when it recommends or sells the investments, or (c) both; (ii) financial incentives to offer to, or to recommend that the retail investor invest in, certain investments because the manager or sponsor of those investments or another third party (such as an intermediary) shares revenue it earns on those products with the firm; and (iii) the firm buying investments from and selling investments to a retail investor from the firm's account (*i.e.*, principal trading). Including these disclosures prominently, in one place, at or before the start of a retail investor's relationship with a firm or financial professional could facilitate retail investors' understanding of the incentives that may be present throughout the course of the relationship. Such disclosure of financial incentives could assist investors in matching their expectations when choosing a firm or professional and type of account to help to ensure they receive services that meet their expectations. In addition, to the extent that the specified conflicts of interest disclosures could draw retail investors' attention to conflicts, monitoring of firms and financial professionals by retail investors could be improved.

The first category of conflicts noted above makes the promotion of own and third party products more salient for retail investors. The possibility that an investor may request an explanation of a transaction regarding a recommended investment or strategy, and associated costs thereof, could serve as an additional disciplinary device for firms and financial professionals and align better their interests with the interests of retail investors. Similarly, the disclosures in the relationship summary about revenue sharing arrangements may induce retail

investors to more carefully pay attention to investments with such arrangements and request further information. Principal trading could also make retail investors vulnerable to transactions that transfer value from their accounts to the accounts of the firm, and so the disclosure of principal trading information could draw retail investors' attention to possible conflicts that could emerge from principal transactions and generate increased scrutiny of such transactions by investors.

While the Commission preliminarily believes that disclosures of conflicts of interest in the relationship summary could match retail investor expectations with the choices of firms and financial professionals, some studies have found that disclosures of conflicts of interest, in some cases, could undermine the motivations of people to behave ethically or to take moral license in their actions.[605] In the context of providing investment advice, the perception that an investor has been warned (via the disclosure) of a firm's and financial professional's potential bias may make them believe that they are less obligated to provide unbiased advice.[606] Further, other studies have suggested that disclosures of conflicts of interest could also make firms and financial professionals appear more trustworthy and as a result reduce the incentives for retail investors to examine additional information more carefully.[607] The Commission preliminarily believes, however, that the securities laws and existing rules and regulations thereunder, such as

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605 *See* Geneviève Helleringer, *Trust Me, I Have a Conflict of Interest! Testing the Efficacy of Disclosure in Retail Investment Advice*, Oxford Legal Studies Research Paper No. 14/2016 (Mar. 2016), *available at* https://ssrn.com/abstract=2755734; and Cain 2005 Article, *supra* note 581. As discussed above, existing and proposed rules and regulations for broker-dealers and investment advisers could mitigate the negative unintended consequences of disclosures of conflicts of interest.

606 *See supra* Section 0.

607 *See* Burden of Disclosure Article, *supra* note 584. Further, this "panhandler effect" suggests that in some cases disclosure of financial professionals' conflicts of interests (particularly in face-to-face interactions) may create social pressure on retail investors to meet the financial professionals' interests.

investment advisers' fiduciary duty,[608] broker-dealers' requirements under proposed Regulation Best Interest[609] standard, as well as under existing self-regulatory organizations' rules and the Exchange Act,[610] reduce the risk that broker-dealers and investment advisers might use the proposed relationship summary to exploit potential conflicts of interest between themselves and their retail investors because these regulations may raise the cost of misconduct.[611]

viii. Additional Information

To facilitate the layered disclosure that the relationship summary provides, we are proposing to require that firms include a separate section ("Additional Information") in the

608 Under the Advisers Act, an adviser is a fiduciary whose duty is to serve the best interest of its clients, including an obligation not to subrogate clients' interest to its own. *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. at 194 (the United States Supreme Court held that, under section 206 of the Investment Advisers Act of 1940, advisers have an affirmative obligation of utmost good faith and full and fair disclosure of all material facts to their clients, as well as a duty to avoid misleading them). Section 206 applies to all firms and persons meeting the Advisers Act's definition of investment adviser, whether registered with the Commission, a state securities authority, or not at all. *See also Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 17 (1979) ("[T]he Act's legislative history leaves no doubt that Congress intended to impose enforceable fiduciary obligations.").

609 *See* Regulation Best Interest Proposal, *supra* note 24. Proposed Regulation Best Interest would establish a standard of conduct for broker-dealers and associated persons of broker-dealers to act in the best interest of the retail customer at the time at recommendation is made without placing the financial or other interest of the broker-dealer or associated person of a broker-dealer ahead of the interest of the retail customer. The standard of conduct obligation shall be satisfied if the broker-dealer or associated person of the broker-dealer discloses at the time of the recommendation material facts relating to the scope and terms of the relationship, which may be satisfied in part by the relationship summary, and all material conflicts associated with the recommendation. In addition, broker-dealers would be required to satisfy the Care and Conflicts of Interest Obligations, as discussed more fully in the Regulation Best Interest Proposal.

610 For example, a broker-dealer may recommend a security even when a conflict of interest is present, but that recommendation must be suitable. *See* FINRA Rule 2111. The antifraud provisions of the federal securities laws and the implied obligation of fair dealing prohibit a broker-dealer from, among other things, making unsuitable recommendations and require broker-dealers to investigate an issuer before recommending the issuer's securities to a customer. *See, e.g., Hanly v. SEC*, 415 F.2d 589, 596 (2d Cir. 1969). *See also* Municipal Securities Disclosure, Exchange Act Release No. 26100 (Sept. 22, 1988), at n.75. The fair dealing obligation also requires a broker-dealer to reasonably believe that its securities recommendations are suitable for its customer in light of the customer's financial needs, objectives and circumstances (customer-specific suitability). *See* Release 8662, *supra* note 118, at 18 (involving excessive trading and recommendations of speculative securities without a reasonable basis).

611 Consistent with this belief, one study also finds that regulations and legal sanctions on conflicted advice can mitigate the effects of moral licensing discussed above. *See* Bryan Church & Xi Kuang, *Conflicts of Disclosure and (Costly) Sanctions: Experimental Evidence*, Journal of Legal Studies 38 2: 505-532 (Jun. 2009).

relationship summary outlining where retail investors can find more information about the firm's legal and disciplinary events, services, fees, and conflicts.

Retail investors may benefit from information on where to find disclosures of the disciplinary events of firms and financial professionals. For some retail investors, the disciplinary history of the firm or the financial professional may affect their choices related to obtaining investment advice. By providing information on whether the firm or financial professionals have disciplinary history and where to obtain more detailed information through layered disclosure may facilitate retail investors' ability to match their expectations with their choice of financial service provider. The required disclosure would succinctly state whether or not the firm or its financial professionals have legal and disciplinary events, based on whether or not they or their financial professionals currently disclose or are currently required to disclose certain legal or disciplinary events to the Commission, self-regulatory organizations, state securities regulators or other jurisdictions, as applicable. The Additional Information section would also highlight where retail investors can find more information about the disciplinary history of the firm and its financial professionals on "Investor.gov." While the disclosure of the existence of disciplinary events does not provide new information to the market,[612] this simple disclosure in the relationship summary, if applicable, could help retail investors more easily identify firms that have reported disciplinary events for themselves or their financial professionals and where to find more information about the events. By including this disclosure, in combination with the requirement to include a specific question for retail investors to ask about disciplinary history in the "Key Questions to Ask" section (discussed further below), the relationship summary would potentially make retail investors more likely to seek out disciplinary

612 *See* Parts 1 and 2 of Form ADV; Form BD; Form U4.

history information to use in their evaluation of firms and financial professionals and would make them better informed when they choose a firm and a financial professional. Finally, retail investors themselves have indicated that they consider disciplinary information important.[613]

Further, by drawing attention to disciplinary histories of financial professionals for retail investors, firms could become more selective in their employment decisions, which could benefit retail investors by having a potentially more trustworthy pool of financial professionals to select from when they choose providers of investment advice, and reduce potential harm to retail investors. As such, the overall quality of financial advice provided to retail investors could increase, to the extent that legal and regulatory compliance is correlated with advice quality.[614] As a consequence, such disclosures of disciplinary history could promote retail investor confidence in the market.

One potential cost of the increased salience of the existence of disciplinary events may be that retail investors could be deterred from hiring a firm or financial professional with a disciplinary record, even if they would be better off to do so, without further investigating the nature of the disciplinary event. Alternatively, an investor may also incorrectly assume that a firm that does not report legal/disciplinary history is a "better" or a "more compliant" firm than a firm that does report such history; i.e., the lack of currently reportable disciplinary history could signify a stamp of approval for some investors. Therefore, disclosures of the existence of disciplinary events could have an unintended consequence of keeping some investors out of the market for financial advice or by selecting financial professionals that could lead to a mismatch with the expectations of the retail investor.

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613 *See* 917 Financial Literacy Study, *supra* note 20.

614 *See* Mark Egan, Gregor Matvos & Amit Seru, *The Market for Financial Adviser Misconduct*, Journal of Political Economy (Dec. 14, 2017), *available at* https://ssrn.com/abstract=2739170.

This section would also include disclosure of how investors can contact the firm, the SEC, or FINRA (when applicable) if they have problems with their investments, investment accounts, or financial professionals. Highlighting this information may encourage more outreach by investors when they experience such problems, which may increase the likelihood of investors seeking resolution of their or the firm's problems. Further, to the extent investors' awareness of how to report problems is increased, it may have some incremental disciplining effect *ex ante* on financial professionals to the benefit of all retail investors in this market. For example, if retail investors, once aware of how to contact the Commission or FINRA are more likely to do so as a result of the information provided by the relationship summary, firms and financial professionals may improve standards and implement policies and procedures aimed at reducing conduct that would warrant potential outreach to regulators by retail investors.

Finally, this section would state where to find more information about the firm and its financial professionals. Broker-dealers would be required to direct retail investors to additional information about their brokers and services on BrokerCheck, their firm websites (if they have a website; if not, they would state where retail investors can find up-to-date information), and the retail investor's account agreement. Investment advisers likewise would be required to direct retail investors to additional information in the firm's Form ADV Part 2 brochure and any brochure supplement provided by a financial professional to the retail investor. If an adviser has a public website and maintains a current version of its firm brochure on the website, the firm would be required to provide the website address (if an adviser does not have a public website or does not maintain its current brochure on its public website, then the adviser would provide the IAPD website address). Making these links to websites available could be important given that

low levels of financial literacy could make it less likely that investors would effectively compile information on their own to use in decision making.

ix. Key questions to ask

The proposed relationship summary is expected to benefit retail investors either directly, by providing information about the corresponding firm and financial professional, or indirectly, by encouraging investors to acquire additional information. The relationship summary would also include suggested key questions to encourage retail investors to have conversations with their financial professionals about how the firm's services, fees, conflicts, and disciplinary events affect them.

Under the "Key Questions to Ask" heading, firms would be required to include ten questions,[615] as applicable to their particular business, to help retail investors to elicit more information concerning the items discussed in the relationship summary.[616] Given that standardization of disclosures limits personalization that may be valuable to retail investors, the Commission preliminarily believes that the proposed questions would serve an important purpose in the relationship summary – namely, to prompt retail investors to ask their financial professionals for more personalized information.

The proposed list of questions in the relationship summary may alter the actions not only of retail investors but also of firms and their financial professionals. In anticipation of having to answer these key questions, firms may find it in their self-interest to train their staff and develop

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615 We are proposing to allow firms to modify or omit portions of any of these questions that are not applicable to their business. We are also proposing to require a standalone broker-dealer and a standalone investment adviser, to modify the questions to reflect the type of account they offer to retail investors (*e.g.*, advisory or brokerage account). In addition, we are proposing that firms could include any other frequently asked questions they receive following these questions. Firms would not, however, be permitted to exceed fourteen questions in total. *See supra* Section 0.

616 *See* proposed Item 8 of Form CRS.

materials that could help them address the question in greater detail. Such a voluntary response by firms would likely benefit investors to the extent the answers given to the questions may become more informative and more accurate. However, some firms may develop standardized answers in anticipation of the key questions that become less informative to the retail investor than a back and forth conversation.

We believe the proposed set of questions cover a broad range of issues that are likely to be important to retail investors and provide benefits, such as a platform from which to begin a dialogue with their financial professional. However, potential costs may arise for some retail investors. One such potential cost of the proposed questions is that they may anchor the attention of retail investors to the list and reduce the likelihood that they would explore other potential questions that could be important to them based on their unique circumstances.[617] In addition, framing the questions as "Key Questions" could lead some retail investors to believe that any other questions they may have due to their own particular circumstances may be of second order importance, even if they may not be.[618]

x. Other benefits and costs to investors

As indicated in the 917 Financial Literacy Study, retail investors consider the proposed disclosures in the relationship summary to be important pieces of information. With respect to content, disclosure items identified as absolutely essential for retail investors were: adviser's fees (76%), disciplinary history (67%), adviser's conflicts of interest (53%), and adviser's methodology in providing advice (51%). Approximately 54% of investors also believe that

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617 Anchoring is a cognitive bias, whereby receivers of information strongly rely on the initial information received when making decisions, and do not sufficiently adjust to new information received. *See*, Anderson, Jorgen Vitting, *Detecting Anchoring in Financial Markets*, Journal of Behavior Finance 11, 129-133 (2010) *available at* https://www.tandfonline.com/doi/abs/10.1080/15427560.2010.483186.

618 *See, e.g.,* Tversky Kahneman Article, *supra* note 580, on the importance of framing.

disclosures that provided comparative adviser information would be useful. In light of this evidence, the Commission preliminarily believes the disclosure would provide valuable information to retail investors and potentially encourage further information gathering by retail investors that assist them in making an informed choice of what type of account matches their preferences and expectations.[619]

By providing specified disclosures in an abbreviated and simplified format, the proposed relationship summary could also improve the effectiveness of the communication between investors and investment advisers or broker-dealers. A more effective communication may enable retail investors to more quickly reach an understanding of what type of firm and financial professional or type of account offered by the broker-dealer or the investment adviser best matches their preferences. As a result, search costs may be reduced as retail investors may need to contact fewer broker-dealers or investment advisers and financial professionals given that they have access to information about those firms or financial professionals.[620] The inclusion of key questions as part of the relationship summary also could serve to reduce search costs as well as the potential for mismatched expectations borne by retail investors if such questions foster

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619 Although the 917 Financial Literacy Study indicated that nearly 90% of survey participants believed that certain disclosures would have been helpful to have in advance of their selection of their current adviser, under the current proposal, firms may and are highly encouraged, though not required, to deliver the relationship summary in advance of the time a retail investor enters into an advisory contract with an investment adviser or engages the services of a broker-dealer. Firms would be required to file the relationship summary with the Commission and the disclosure would be made available on public websites of broker-dealers and investment advisers, which indicates that prospective investors could have access to a given firm's relationship summary in advance of initial contact with the firm or its financial professionals. In general, however, the Commission preliminarily anticipates that most prospective retail investors would receive the relationship summary at the time that they meet with a financial professional to consider entering into an agreement or engaging services.

620 Insofar as retail customers may also search for other providers of financial advice, such as insurance companies or banks and trust companies, the reduction in search costs obtainable from the relationship summary would be lower.

greater discussion about the services, costs and fees, and possible conflicts associated with broker-dealer and investment adviser business models.

The Commission preliminarily believes that the proposed relationship summary could benefit not only the existing and prospective customers and clients of broker-dealers and investment advisers but also the public more broadly. First, recipients of the relationship summary, to the extent they discuss investing in general, may discuss the topics covered in the summary with family and friends and in the process increase the degree of public awareness about the issues discussed in the disclosure. Second, some prospective retail investors could access the relationship summary independently through the company website or the Commission's website.

The proposed relationship summary may also impose some additional costs on retail investors. As described more fully in the section that follows, brokers-dealers and investment advisers will bear compliance costs associated with the production and dissemination of the relationship summary. As a result of such increased costs, some firms or financial professionals may transfer retail investors from potentially lower cost transaction-based accounts to higher cost asset-based fee advisory accounts, if the firm or the financial professional is dually registered.

In addition to these compliance burdens which may indirectly be borne by retail investors, the disclosures themselves may impose certain indirect costs on retail investors. For example, since the proposed disclosures in the relationship summary are general and contain prescribed language in many parts, they could steer retail investor attention away from some specific and potentially important characteristics of the business practices of the firm or the financial professional. This potential cost is likely to be mitigated to the extent the required

Additional Information section employs layered disclosure and the Key Questions encourage more personalized information gathering on part of the retail investors.

b. Broker-Dealers and Investment Advisers

The proposed disclosure requirements would impose direct costs on broker-dealers and investment advisers, including costs associated with delivery, filing, preparation, and firm-wide implementation of the relationship summary, as well as training and monitoring for compliance.[621]

With respect to initial delivery, the relationship summary would need to be provided to retail investors[622] in the case of an investment adviser, before or at the time the firm enters into an advisory agreement or, in the case of a broker-dealer, before or at the time the retail investor first engages the firm's services. A dual registrant should deliver the relationship summary at the earlier of entering into an investment advisory agreement with the retail investor or the retail investor engaging the firm's services. Firms would be permitted to deliver the relationship summary (including updates) electronically, consistent with prior Commission guidance.[623] Firms would also be required to post their relationship summaries on their websites in a way that is easy for retail investors to find, if they maintain a public website. Firms that do not maintain a website would be required to include in their relationship summaries a toll-free number for investors to call to obtain documents. In addition, firms would be required to provide a relationship summary to an existing client or customer who is a retail investor before or at the time a new account is opened or changes are made to the retail investor's account(s) that would

621 *See infra* Section V.A. for estimates of some of these compliance costs for purposes of the Paperwork Reduction Act.

622 In addition to the firm's delivery requirements, firms would also file their relationship summary with the Commission, to be publicly available. *See supra* Section 0.

623 *See supra* Section 0.

materially change the nature and scope of the firm's relationship with the retail investor. Firms also would be required to implement a one-time delivery of the relationship summary to all existing retail investors within 30 days after the date the firm is first required to file its relationship summary with the Commission.[624]

Regardless of the method of delivery (e.g., paper or electronic delivery) firms would incur costs associated with delivering the relationship summary to retail investors. Such flexibility in the method of delivery, while being consistent with Commission guidance, could increase efficiency by allowing a firm to communicate with retail investors in the same medium by which it typically communicates other information. Further, firms could reduce costs by utilizing technologies to deliver information to retail investors at lower costs than they may face with paper delivery.[625] While we recognize that some firms are likely to use electronic delivery methods, and that these methods may be lower cost than paper delivery, some firms may still produce paper versions of the relationship summary, particularly if they have some retail investors that prefer delivery of disclosure in this method, or do not have access to the Internet, or if firms are delivering the relationship summary in the same format alongside other deliverables, such as Form ADV or account statements. Firms would also incur costs of posting the relationship summary on their websites and filing the summary with the Commission.

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624 Currently, investment advisers have approximately 29 million non-high net worth individual clients and 5 million high net worth individual clients, and the total number of individual clients of investment advisers has increased by 10 million since 2012. Therefore, investment advisers would need to deliver relationship summaries to approximately 35 million existing retail clients, and on average, would expect approximately 2.5 million new clients per year. Item 5.D of Form ADV. Although the Commission is unable to estimate the number of broker-dealer retail customers, we could assume that the number of relationship summaries for broker-dealer customers would be at least as many, if not more, than what would have to be delivered for investment advisers.

625 Firms would be required to create and maintain records of deliveries of the relationship summary. *See supra* Section 0. *See supra* Section II.E (discussing recordkeeping requirements relating to the relationship summary). If choosing electronic delivery, firms would have compliance costs in providing notice to retail investors that the relationship summary would be available electronically. *See supra* Section 0 (discussing elements of Commission guidance about electronic delivery of certain documents).

Beyond costs associated with delivery of the relationship summary to retail investors, firms would be required to prepare the relationship summary. The Commission preliminarily believes, however, that these costs would be limited for several reasons. First, the relationship summary is concise (limited to four pages in length or the equivalent length for electronic disclosure), and would contain a mandated set and sequence of topic areas, with much of the language to be prescribed, thus limiting the time required to prepare the disclosure. Second, the relationship summary will be uniform across retail investors and would not be customized or personalized to potential investors. Finally, the relationship summary would contain some standardized elements across investment advisers and broker-dealers, allowing for potential economies of scale for entities that may have subsidiaries that would also be required to produce the disclosure.

Further to the costs of preparing the relationship summary, we consider the implication of the disclosure requirements attributable to the DOL rules and exemptions, including the DOL's BIC Exemption, and the potential effects of those disclosures relative to the relationship summary for broker-dealers and investment advisers. The conditions of the DOL rules and exemptions, including the BIC Exemption, discussed above in the baseline section, are limited to retirement accounts. Although some firms may have voluntarily adopted disclosure requirements of the BIC Exemption for non-retirement accounts, the proposed relationship summary would apply to a broader array of relationships, spanning both retirement and non-retirement accounts for broker-dealers and investment advisers. To the extent that the information provided by the relationship summary would be duplicative of information that would be required by the BIC Exemption (or other DOL rules and exemptions) and provided to the same group of account holders that would receive the DOL required disclosures, the overall

benefits of the relationship summary could be reduced. Lastly, to the extent that some financial firms already have set up procedures and systems to comply with the DOL disclosure requirements, these firms may incur lower incremental compliance burdens. The Commission preliminarily believes, however, that the scope of the disclosure requirements under DOL rules and exemptions and the systems that firms would have put in place to accommodate such disclosures are unlikely to have a significant overlap with the relationship summary. Therefore, the Commission anticipates that any potential cost savings for firms to comply with disclosure obligations under DOL rules and exemptions and the relationship summary are likely to be minimal.

With respect to preparing and implementing the relationship summary, firms would also need to expend resources with respect to the required Key Questions in the relationship summary. Firms would bear costs of preparing responses the questions from the list and training their employees on how to respond. Financial professionals need to spend time to prepare their responses to the questions and to respond to these questions when asked. As a result, some firm employees or financial professionals could take away from the time they dedicate to investigate investment recommendations, which could inadvertently harm investors if financial professionals divert resources to answering key questions but reduce their time devoted to arriving at investment strategies. In this case, the quality of their recommendations could decline. In both cases, the possible additional costs to firms could be (partially) transferred to retail investors.

In addition to the costs associated with preparation, delivery, filing, and posting on websites of the initial relationship summary, firms would also bear costs for updating the relationship summary within 30 days whenever any information becomes materially

inaccurate.[626] The firm would be required to communicate updated information to retail investors who are existing customers or clients of the firm within 30 days whenever any information in the relationship summary becomes materially inaccurate.[627] Firms could communicate this information by delivering the amended relationship summary or by communicating the information another way to the retail investor. For example, if an investment adviser communicated a material change to information contained in its relationship summary to a retail investor by delivering an amended Form ADV brochure or Form ADV summary of material changes containing the updated information, this generally would support a reasonable belief that the information had been communicated to the retail investor, and the investment adviser generally would not be required to deliver an updated relationship summary to that retail investor. This requirement provides firms the ability to disclose changes without requiring them to duplicate disclosures and incur additional costs. The updated relationship summary would also need to be posted prominently to the firm's website if the firm has one and filed electronically with the Commission. In addition, firms could also incur some costs to keep records of how the updated relationship summary or the information in the updated relationship summary was delivered to retail investors.

We anticipate that the compliance costs associated with producing updates of the relationship summary would be also relatively minor given that the relationship summary uses largely prescribed language and updates of the relationship summary, which are only required for material changes, are expected to be infrequent. As a result, the costs of such updates are

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626 Along this line, firms could also incur some costs of modifying prescribed disclosure per the parameters of Instruction 3.

627 The requirement to communicate updated information to retail investors, rather than deliver an updated relationship summary could reduce the effectiveness of the information to the extent that the communication does not allow retail investors to see the context in which information was changed.

expected to be small relative to the costs associated with the initial production of the disclosure. Further, annual costs associated with communications regarding updates to the relationship summary are anticipated to be lower than the costs of the initial delivery to existing retail investors to the extent the frequency of updates is low or the firm communicates the updates through other ways than formal delivery. The Commission anticipates that some of the costs associated with preparation, delivery, filing, website posting, and updates to the relationship summary for an average broker-dealer or average dual registrant could exceed the costs for the average investment adviser. As Table 1 and Table 3 indicate, broker-dealers maintain a larger number of accounts than investment advisers do; therefore, delivery costs for broker-dealers could exceed those of investment advisers, if the number of accounts is a good indicator of the number of retail investor customers.[628] Similarly, given that the average dual registrant has more customer accounts than the average investment adviser, and that the preparation of relationship summaries for dual registrants may require more effort than for standalone broker-dealers or investment advisers, the compliance costs could be larger for these firms.

In addition, unlike investment advisers, which produce Part 2A of Form ADV, a broker-dealer currently is not required to prepare a narrative disclosure document for its retail investors, although under existing antifraud provisions of the Exchange Act, a broker-dealer may be liable if it does not disclose material information to its retail investors. Thus, broker-dealers could expend additional time and effort to aggregate the information required by the relationship summary relative to investment advisers. As a result, the Commission preliminarily believes that the investment advisers should be able to produce the relationship summary at a relatively lower

628 The Commission is unable to obtain from Form BD or FOCUS data information on broker-dealer numbers of customers, and instead, is only provided with the number of customer accounts. The number of customer accounts will exceed the number of customers as a customer could have multiple accounts at the same broker-dealer.

cost than broker-dealers, given investment advisers' experience with preparing and distributing Part 2A of Form ADV.[629]

The Commission preliminary believes that compliance costs would also be different across firms with relatively smaller or larger numbers of retail investors as customers or clients. For example, to the extent that developing the relationship summary entails a fixed cost, firms with a relatively smaller number of retail investors as customers or clients may be at a disadvantage relative to firms with a larger number of such customers or clients since the former would amortize these costs over a smaller retail investor base. Firms with a relatively larger number of existing retail investors would face higher costs of initial distribution of the relationship summary compared to firms with a relatively smaller retail investor base. Further, to the extent that certain costs associated with preparing different versions of the proposed relationship summary scale with the number of branches and associated financial professionals that a firm has, firms with a relatively larger number of branches and employees may bear higher costs than firms with a smaller number.

While the imposed four-page limit is expected to impose nominal compliance costs on market participants, it could also generate additional costs for some firms relative to others. For example, the four-page limit may be more costly for firms that have more complex business models because it will limit the information they can present within the relationship summary.[630] For example, a firm with a disciplinary history that provides exceptionally good customer service could be at a disadvantage compared to other firms with no disciplinary history because the

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629 For example, investment advisers may already have specialized staff dealing with disclosure issues.

630 Complexity is not necessarily linked to size – for example, there are large, simple firms and small, complex firms.

relationship disclosure may not summarize relevant information about the quality of customer service or the full scope of services offered by the firm.

Based on the estimates provided in Section V.A for Paperwork Reduction Act purposes, the average cost burden for an investment adviser to prepare the proposed Form CRS for the first time is estimated to range between approximately $1,300 and $3,400, depending on the extent to which external help is used.[631] The estimated aggregate combined internal and external costs to investment advisers industry-wide for initially preparing and filing the relationship summary would be approximately $22 million.[632] Similarly, for broker-dealers, the average cost to a firm for preparing Form CRS for the first time is estimated to range between approximately $4,000 and $6,100, based on the estimate provided in Section V.D.[633] The estimated aggregate combined internal and external costs to broker-dealers industry-wide of initially preparing and filing the relationship summary would be approximately $15 million.[634] In terms of the initial

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631 The lower end estimate is based on the assessment that, without additional external help, it will take an average investment adviser 5 hours to prepare the relationship summary for the first time, *see infra* Section V.A.2.a. We assume that performance of this function will be equally allocated between a senior compliance examiner and a compliance manager at a cost of $229 and $298 per hour, (*see infra* note 743 for how we arrived at these costs). Thus, the cost for one investment adviser to produce the relationship summary for the first time is estimated at $1,317 (2.5 hours x $229 + 2.5 hours x $298 = $1,317) if no external help is needed. In addition, we estimate that if the investment adviser needs external help, the average cost to an investment adviser for the most expensive type of such help (*i.e.*, compliance consulting services) would be $2,109, *see infra* note 732, which brings the total cost to $3,426.

632 *See infra* Sections V.A.2.a and V.A.2.b for estimates of aggregate internal and external costs, respectively, of the initial preparation and filing of the relationship summary.

633 The lower end estimate is based on the assessment that, without additional external help, it will take an average broker-dealer 15 hours to prepare the relationship summary for the first time, *see infra* Section V.D.2.a. We assume that performance of this function will be equally allocated between a senior compliance examiner and compliance manager at a cost of $229 and $298 per hour, respectively (*see infra* note 743 for how we arrived at these costs). Thus, the cost for one broker-dealer to produce the relationship summary for the first time is estimated a $3,953 (7.5 hours x $229 + 7.5 hours x $298 = $3,953) if no external help is needed. In addition, we estimate that if the broker-dealer needs external help, the average cost to a broker-dealer for the most expensive type of such help (*i.e.*, compliance consulting services) would be $2,109, see infra note 826, which brings the total cost to $6,062.

634 *See infr*a Sections V.D.2.a and V.D.2.b for estimates of aggregate internal and external costs, respectively, of the initial preparation and filing of the relationship summary.

cost of delivering the relationship summary to current retail investors, we estimate that the cost to existing and newly registered investment advisers would be approximately $43.4 million in aggregate, or approximately $5,350 per adviser.[635] For broker-dealers, the estimated initial cost of delivering the relationship summary to current retail investors would be approximately $121.5 million in aggregate, or approximately $42,500 per broker-dealer.[636] For both investment advisers and broker-dealers, the estimated annual costs of the requirement to deliver the relationship summary before or at the time a new account is opened, or changes are made to the retail investor's account(s) that would materially change the nature and scope of the firm's relationship with the retail investor, is approximately 10% of the respective estimated costs of the initial delivery to existing retail investors.[637]

Finally, the Commission believes that the proposed relationship summary would bring tangible benefits to many broker-dealers and investment advisers. Although the possibility of mismatched expectations for retail investors and their choice of financial firm or professional generally are most costly to the retail investors, such mismatch also imposes costs on broker-dealers and investment advisers. For instance, some investors who have mismatched their expectations of a financial services provider with the type of provider they have engaged may lodge complaints with the SEC or FINRA for perceived misconduct by their financial professional without understanding the nature of their relationship (e.g., an investor may file a

635 *See infra* Section V.C.2.b.i for the estimate of costs investment advisers would incur to deliver the relationship summary to their existing clients. Note that the analysis includes investment advisers that are dual registrants.

636 *See infra* Section V.D.2.d.i for the estimate of costs investment advisers would incur to deliver the relationship summary to their existing clients. Note that thee analysis includes broker-dealers that are dual registrants.

637 *See infra* Section V.C.2.b.ii for the estimate of these costs for investment advisers and *infra* Section V.D.2.d.ii for the analysis of these costs for broker-dealers.

complaint of discretionary trading in an investment advisory account because they did not understand the nature of the services for which they contracted). These complaints are costly to firms and financial professionals, and the Commission preliminarily believes that the relationship summary could alleviate search costs for investors and the likelihood of mismatch between investor expectations and their choice of firm or financial professional.

With respect to particular elements of the relationship summary, firms with relatively no currently reportable legal and disciplinary disclosures could benefit directly from the reporting in the relationship summary because the reporting would make these characteristics more salient for retail investors by prompting investors to research disciplinary history of firms with currently reportable legal and disciplinary disclosures. To the extent that including disciplinary history information in the relationship summary increases the propensity of retail investors to consider this information when selecting firms and financial professionals, it could also ultimately increase the cost of misconduct for firms and financial professionals (for example, by making it more difficult to attract retail investors), which would make it more likely that firms take disciplinary information into account when making employment choices, thereby potentially raising the overall quality of their workforce. The relationship summary could further exhibit some positive long-term effects on the markets for broker-dealers and investment advisers and we elaborate on these long-term effects in greater detail in the next subsection.

3. Impact on Efficiency, Competition, and Capital Formation

In addition to the specific benefits and costs discussed in the previous section, the Commission expects that the proposed disclosure could cause some broader long-term effects on the market for financial advice. Below, we elaborate on these possible effects, including a discussion of their impact on efficiency, competition, and capital formation.

The primary long-term effect of the disclosure on the market is that it could enhance the competitiveness of the broker-dealer and investment adviser markets. The increased transparency with respect to the nature of the relationship between broker-dealers or investment advisers and their retail investors may allow retail investors to better evaluate their firms and financial professionals as well as the options for financial services that are advertised by them, which may increase the overall level of retail investor understanding in the market. When retail investor understanding increases, the degree of competitiveness of the financial services industry may also increase because retail investors could better assess the types of services available in the market. Market competitiveness could be further enhanced by the fact that, by prompting investors to understand better and obtain more information on the services provided as well as the types of fees and costs associated with such services, the relationship summary may reduce search costs for retail investors associated with acquiring this information, thus allowing them to more readily identify less expensive services that match their preferences and expectations for financial services. The relationship summary also could cause additional competition around conflicts of interest, resulting in some firms changing their practices to decrease conflicts. Proposed Regulation Best Interest also requires broker-dealers to disclose all material facts relating to the scope and terms of the relationship, and all material conflicts of interest associated with the recommendation.[638] The Commission preliminarily believes that the relationship summary, which draws investor awareness to potential conflicts of interest at the outset of the relationship with a firm or financial professional, would address similar concerns related to the material facts associated with the scope and terms of the relationship as required by proposed

[638] Further, proposed Regulation Best Interest would establish policies and procedures to identify and at a minimum disclose or mitigate material conflicts of interest associated with such recommendations, as well as policies and procedures to identify, disclose and mitigate or eliminate material conflicts of interest arising from financial incentives associated with such recommendations.

Regulation Best Interest. Relative to the disclosures required by proposed Regulation Best Interest, the relationship summary conflicts of interest disclosures apply not only to broker-dealers and dually-registered firms, but also to investment advisers.

Increased competitiveness in the market for financial services could have ancillary effects as well, including reduced pricing power for firms and incentives for firms to innovate products and services. Reduced pricing power, as a result of increased competitiveness, could benefit retail investors through lower fees, effectively redistributing value from holders of financial firm equity to their retail investors.[639] We note, however, that this effect could be mitigated by the possibility that people may still be willing to pay higher prices for other reasons, including firm reputation. Competition also provides incentives for firms to develop and innovate. Additional competition among financial services firms could provide incentives for broker-dealers and investment advisers to seek alternative ways to generate profits. In the process, firms could develop new and better ways of providing services to retail investors, for example, by utilizing recent developments in information technologies to deliver information to retail investors at lower cost. In this way, innovation could thus improve the satisfaction of retail investors and the profitability of firms in the financial services provider market.

Another potential positive effect of the relationship summary is that, by reporting whether a firm or financial professional has currently reportable legal or disciplinary events, the relationship summary could prompt retail investors to seek out disciplinary information on their current and prospective firms and financial professionals and take that information into account when considering whom to engage for financial services. In this respect, the proposed relationship summary may also enhance competition if, for example, firms and financial

639 *See* Jean Tirole, *The Theory Of Industrial Organization*, M.I.T. Press (1989).

professionals with better disciplinary records outcompete those with worse records. We note, however, that reporting whether a firm or financial professional has currently reportable legal or disciplinary events may also bias firms toward hiring firms or financial professionals with fewer years of experience (i.e., fewer opportunities for customer complaints) and against hiring experienced financial professionals with some (minor) customer complaints. The expected economic impact of the above effect across small and large firms, however, is generally unclear. For investment advisers and broker-dealers, reportable disciplinary events are less common for smaller firms than for larger firms.[640]

However, in the market for financial services between investment advisers and broker-dealers, disclosing the existence of currently reportable legal and disciplinary events in the relationship summary may confer a small competitive advantage for investment advisers because broker-dealers are more likely to have to report that they have a disciplinary history due to broader broker-dealer disclosure obligations.[641] They are also more likely to report if they have more disciplinary issues. Reporting from Form BD with respect to broker-dealer disclosures of disciplinary actions taken by any regulatory agency or SRO shows that 308 (84%) out of 366 dual-registered broker-dealers disclosed a disciplinary action. By contrast, 1,650 (47%) out of 3,475 standalone broker-dealers have a disclosed disciplinary action. For investment advisers, Form ADV requires disclosures of any disciplinary actions taken in the past ten years. 289 (79%) out of 366 dual-registered investment advisers disclosed a disciplinary action. A much lower

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640 For example, while only 10% of registered investment advisers with less than $1 million of AUM disclose at least one disciplinary action as of January 1, 2018, 66% of registered investment advisers with more than $50 billion of AUM disclosed at least one disciplinary action that year. Form ADV. Similarly, while 89% of broker-dealers with less than $1 million in total assets disclose at least one disciplinary action as of January 1, 2018, 100% of broker-dealers with more than $50 billion total assets disclosed at least one disciplinary action that year. Form BD.

641 *See supra* notes 251, 253 – 255 and accompanying text.

fraction, 1,732 (14%) of 12,293, standalone investment advisers disclosed a disciplinary action.[642] The fact that broker-dealers have relatively more reportable legal and disciplinary events than investment advisers may cause retail investors to engage investment advisers rather than broker-dealers, thus creating a competitive advantage for some investment advisers.

Although the proposed relationship summary applies to SEC-registered broker-dealers and SEC-registered investment advisers, it could exhibit some spillover effects for other categories of firms not affected by the proposal such as investment advisers not registered with the SEC, bank trust departments, and others. In particular, the relationship summary could change the size of the broker-dealer and investment adviser markets – relative to each other, as well as relative to other markets. To the extent the relationship summary reduces retail investors' confusion and makes it easier for them to choose a relationship in line with their preferences and expectations, the Commission expects that this could attract new retail investors to these markets, coming from firms in other markets. Firms' current retail investors also may consider switching to a different type of firm if the relationship summary makes the different services provided and the fees and costs of investment advisory and brokerage services more prominent. The exact extent and direction of substitution between brokerage and advisory services is hard to predict and depends on the nature of the current mismatch between retail investor preferences and expectations and the type of services for which they have contracted.

The proposed relationship summary may also benefit financial markets more broadly.

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642 Source: Items 11C, 11D, and 11E of Form BD and Items 11.C., 11.D. and 11.E. of Form ADV. Form BD asks if the SEC, CFTC, other federal, state, or foreign regulatory agency, or a self-regulatory organization have ever found the applicant broker-dealer or control affiliate to have 1) made a false statement or omission, 2) been involved in a violation of its regulations or statues, 3) been a cause of an investment related business having its authorization to do business denied, suspended, revoked, or restricted, or 4) imposed a civil money penalty or cease and desist order against the applicant or control affiliate. Likewise, Form ADV asks similar questions of registered investment advisers and advisory affiliates.

Recent survey evidence suggests that 60% of all American households have sought advice from a financial professional.[643] Despite their prevalence and importance, however, financial professionals are often perceived as dishonest and consistently rank among the least trustworthy professionals.[644] This perception has been partly shaped by highly publicized scandals that have affected the industry over the past decade. Systematic mistrust may suppress household stock market participation below the optimal threshold predicted by academic investment theory, as documented in household survey based studies.[645] The Commission preliminarily believes that the increased transparency of the existing business practices of financial professionals could raise the level of investor trust in the market. The enhanced trust could promote retail investor participation in capital markets which could increase the availability of funds for businesses. Depending on the magnitude of the effect, greater availability of funds could lower firms' cost of capital, allowing firms to accumulate more capital over time.

We note a possible negative effect on the trust of some retail investors due to the disclosure on the relationship summary that a firm or financial professional has currently reportable legal or disciplinary events. The decrease in the trust levels of some retail investors, however, could also benefit these investors by bringing their expectations and perceptions in line

643 *See supra* note 541. Survey of Consumer Finances, 2016. The percentage aggregates all respondents indicating that they use at least one of the following sources in making saving and investment decisions – brokers, financial planners, accountants, lawyers, or bankers. 26% of the respondents indicate that they have used brokers or financial planners.

644 *See* Edelman Trust Barometer, *2015 Edleman Trust Barometer Executive Summary* (2015), *available at* https://www.edelman.com/2015-edelman-trust-barometer/; Anna Prior, *Brokers are Trusted Less than Uber Drivers, Survey Finds*, Wall Street Journal (Jul. 28, 2015), *available at* https://www.wsj.com/articles/brokers-are-trusted-less-than-uber-drivers-survey-finds-1438081201; Luigi Zingales, *Does Finance Benefit Society*, Journal of Finance 70, 1327-1363 (Jan. 2015).

645 *See, e.g.*, Luigi Guiso, Paola Sapienza & Luigi Zingales, *Trusting in the Stock Market*, The Journal of Finance, Vol. 63, No. 6, 2557-2600 (2012); and J. Campbell, *Household Finance*, The Journal of Finance, Vol. 61, No. 4, 1553-1604 (2006) ("Campbell Article").

with their choice of a firm or financial professional.[646]

Another possible long-term effect of the relationship summary is that it could decrease the prevalence of third-party selling concessions in the market by requiring broker-dealers and dual registrants to include prescribed disclosure about indirect fees associated with investments that compensate the broker-dealer, including mutual fund loads. Currently, selling concessions constitute a significant part of the compensation of broker-dealers selling mutual fund products.[647] For example, a mutual fund may provide a selling concession, in the form of a sales charge, some portion of which could be remitted to the broker-dealer that recommended the product.

Table 2, Panel A also indicates that selling concessions constitute a larger fraction of total revenue (commissions, fees, and sales of IC shares) for smaller broker-dealers – for example, selling concessions as a fraction of revenues represent around 20% for broker-dealers with total assets less than $1 million and less than 4% for broker-dealers with total assets in excess of $50 billion. To compensate for the potential loss of concession-based revenue, broker-dealers could try to switch customers to advisory accounts. As noted above, however, if the proposed disclosure also increases the competitiveness in the broker-dealer and investment adviser markets the increased competitiveness would create some downward price pressure in the market.

4. Alternatives to the Proposed Relationship Summary

This section highlights alternatives to the relationship summary concerning an amendment of existing Forms BD and ADV for broker-dealers and investment advisers,

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646 *See* Jeremy Ko, *Economics Note: Investor Confidence* (Oct. 2017), *available at* https://www.sec.gov/files/investor_confidence_noteOct2017.pdf.

647 *See supra* Table 2, Section IV.A.1.a.

respectively; the form and format of the relationship summary; extensiveness of disclosure; delivery; and communicating information about the updated relationship summary.

a. Amendment to Existing Disclosures

As proposed, the relationship summary would be a new, standalone disclosure produced by broker-dealers and investment advisers, in addition to the other required information disclosed by broker-dealers and investment advisers. As an alternative, the Commission could consider incorporating the relationship summary information into existing disclosures.

For example, Part 2A of Form ADV currently has 18 mandatory reporting elements, produced as a narrative discussion, as part of the disclosure "brochure" provided to prospective retail investors initially and to existing retail investors annually. Instead of requiring investment advisers to produce a completely new disclosure as a separate Form CRS, the Commission could instead make an amendment to Part 2A of Form ADV to require a brief summary at the beginning of the brochure in addition to the existing narrative elements, or to change certain of the disclosure requirements to reduce or eliminate redundancy. Similarly, broker-dealers could be required to deliver longer narrative disclosure to their retail investors with specified elements. Such disclosure could also be required as part of Form BD or a standalone requirement.[648] For example, the instructions to Form BD contain a section on the explanation of terms which could be extended to include basic (registrant-specific) information on the business practices of the registrant.

Although modifying existing disclosure and reporting in these ways could provide the same information to retail investors as the proposed relationship summary, the Commission

[648] We note, however, that Form BD is a registration/application form (rather than an existing brochure-type disclosure form).

believes that these approaches would be less suited for the objective of this disclosure, which is to provide a short, simple overview. The proposed relationship summary would provide disclosure in a standardized, simplified manner, that would allow retail investors not only to compare information within a category (*e.g.*, two investment advisers), but also across categories (*e.g.*, investment advisers and broker-dealers). Further, the relationship summary would be designed to be easily comprehensible by retail investors, relying on short, easy-to-read disclosure that would provide an overview of information about the firm and its financial professionals to retail investors when choosing a firm and account type. We believe that the proposed relationship summary would benefit retail investors by highlighting succinct information that is relevant to a decision to select a firm, financial professional, or account type and services, at the time such decisions are made, and relying on layered disclosure to provide additional detail.

b. Form and Format of the Relationship Summary

The Commission is proposing to require broker-dealers and investment advisers to create and deliver a short relationship summary to retail investors that would highlight specified information under prescribed headings in the same order to facilitate comparability. The relationship summary would be limited in length and would contain a mix of prescribed and firm-specific language. The proposal does not specify a single format for filing the disclosure.

The Commission could require the relationship summary be filed with the Commission in a specified format, such as an text-searchable PDF file or in some other format, for example, an unstructured PDF or HTML, structured PDF, a web-fillable form, XML, XBRL or Inline XBRL. Further to this alternative, the Commission could require that the relationship summary information be filed in a structured format to facilitate validation, aggregation and comparison of disclosures, and the Commission could then make the data available on IARD and EDGAR.

Structured format, such as XML, can enable the automatic generation of unstructured formats such as PDF, HTML, and others to meet the needs of those users who would prefer a paper-oriented layout.

As an alternative to the largely prescribed language for the relationship summaries, the Commission could instead allow broker-dealers and investment advisers to construct bespoke disclosure, while providing guidance to firms on the elements of the relationship disclosure that are required to be included. Although this disclosure would allow firms to tailor the discussion of the nature of the business, fees and costs, conflicts of interest, and disciplinary history specifically to their business model, this approach would likely be more costly to retail investors, as it would likely diminish the usefulness of a concise, simplified disclosure that is capable of being used by retail investors to understand firm types. Longer firm-specific disclosures could also increase the search costs for retail investors which could ultimately result in worse choices by lowering investor ability and incentives to screen a large number of firms. Higher search costs for investors could also lower the competitiveness of the market by allowing some firms with lower-quality services to maintain customers and sustain market share, even if better choices are available to retail investors. As discussed above in Section III.B, simplification of disclosures, in terms of size, presentation, and readability, allows for ease of processing of information, while standardization of the content would facilitate identification of information most useful to a retail investor. Finally, lengthier bespoke disclosure would be also costlier for firms to produce. As another alternative, the Commission could have required the relationship summaries to include only prescribed wording. However, the Commission believes that a mix of prescribed and firm-drafted language provides both information that is useful for retail investors in comparing different firms along with some flexibility for firms to determine how best to

communicate the information about their particular practices to retail investors.

c. Extensiveness of Disclosure

As currently proposed, the relationship summary would include high-level information on (i) introduction; (ii) the relationships and services provided in the firm's advisory accounts and brokerage accounts; (iii) the standard of conduct applicable to those services; (iv) the fees and costs that retail investors will pay, (v) comparison to other account types; (vi) specified conflicts of interest; (vii) where to find additional information, including whether the firm and its financial professionals currently have reportable legal or disciplinary events and who to contact about complaints; and (viii) key questions for retail investors to ask the firm's financial professional. As an alternative, the Commission could require the inclusion of additional topics or additional disclosures on one or more topics proposed to be covered by the relationship summary. These disclosures could be required as part of the relationship summary or as separate appendices.

With respect to the additional topics to be disclosed, the Commission could request that firms disclose additional information on their performance, investment style, or other business practices. Retail investors, however, may become overwhelmed if presented with a number of very lengthy disclosures, which therefore could bury the information that is most useful to investors and reduce the effectiveness of those disclosures.[649] With respect to the specific topics of additional information, evaluating the performance, investment style and business practices of a firm or financial could be subjective or speculative, and may be more suited for marketing

[649] *See also supra* note 50 and accompanying text (discussing comment letters to the 917 Financial Literacy Study regarding the length of disclosure documents).

materials rather than prescribed language in the relationship summary.[650] For all these reasons, we believe that these additional disclosure topics are not appropriate for inclusion in the relationship summary.

Regarding alternatives to the disclosure of fees and costs as proposed here, the relationship summary could require additional disclosures on one or more of these topics. For example, the relationship summary could include the firm's fee schedule, either as part of the body of the relationship summary or as an attachment. Alternatively, we could require each relationship summary to include a personalized fee schedule,[651] to be created for each retail investor, detailing the specific fees and costs associated with the retail investor's account, presented both in dollars and as a percentage of the value of the retail investor's account. These fee schedules could also include compensation received by the firm and its financial professionals related to the account, and the indirect fees that are payable by the retail investor to others (e.g., mutual fund and exchange-traded fund fees and expenses). However, ex ante identifying possible fee schedules for investors at the outset of a relationship as opposed to at the time of the transaction could impose costs to both investors and firms. For example, firms might need to outline a long list of possible transactions and the associated fee schedules, which in turn could be confusing to investors.

We could also require more comprehensive disclosures regarding conflicts of interest and disciplinary history, including requiring firms to summarize more or all of their conflicts of

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650 In terms of performance, studies have shown that investors take into account information about historic fund performance in their investment choice; s*ee, e.g.*, Choi Laibson Article, *supra* note 567.

651 One requirement of proposed Regulation Best Interest would be to provide to investors at the time of or prior to a recommendation the expected fees and costs, and possibly a fee schedule, associated with the individual transaction.

interest.[652] For example, firms could disclose potential conflicts of interest associated with execution services, such as those required to be reported in rule 606 disclosures.[653]

We could also require additional details about a firms' and its financial professionals' disciplinary history. Instead of requiring firms to disclose whether or not they have currently reportable legal or disciplinary history, as proposed, we could require firms to disclose the number of disciplinary events, expressed as a number or as a percentage of the size of the firm or the number of firm professionals. We could further differentiate the disclosures by requiring firms to disclose the existence and numbers of disciplinary histories within categories of disciplinary history.

More detailed disclosures about fees, compensation, conflicts and disciplinary history could help retail investors understand better the differences between types of accounts, and could facilitate the decision about the most appropriate account for each retail investor. As noted above, current disclosures on these topics cover only subsets of firms and relationships and could take different forms. For example, firms wishing to make investment recommendations to IRAs and participants of ERISA-covered plans may be subject to certain disclosure obligations.[654] This disclosure, however, does not apply to non-retirement accounts. Investment advisers also prepare a Form ADV Part 2A narrative brochure but such a retail disclosure document is not currently required for broker-dealers. As a result, the Commission preliminary believes that

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652 *See supra* Section II.B.6 for a discussion of conflicts, or specific details of conflicts, that would not be required to be disclosed in the proposed Form CRS.

653 *See* 17 CFR 242.606 (requiring that broker-dealers make publicly available a quarterly report on order routing information, including a discussion of the material aspects of their relationship with venues executing non-directed orders, including arrangements for payment for order flow and any profit-sharing arrangement).

654 *See supra* Section IV.A.1.c (discussing disclosure obligations under DOL rules and exemptions).

retail investors could benefit from the proposed relationship summary given its wide coverage, delivery method, and design.

In particular, the disclosures about types of fees and costs included in the relationship summary could help retail investors understand better the types of fees that they will pay and how those types of fees and costs affect their accounts. As discussed in the baseline, the 917 Financial Literacy Study highlighted that transparency and disclosure about fees charged by financial intermediaries was one of the most essential elements that investors would consider in making their decision about which financial professional to choose.[655]

Similarly, the information provided about conflicts of interest in the relationship summary could help retail investors understand how such conflicts that might be pertinent to their account. The disclosure about whether the firm or financial professional has currently reportable legal or disciplinary events could encourage retail investors to research the extensiveness and nature of the disciplinary history of a firm, therefore allowing retail investors to further evaluate firms based on the types of disciplinary events.

Although additional disclosures on account types, fees and compensation (including a fee/compensation schedule), conflicts of interest and disciplinary history could enhance retail investors' understanding of the accounts that are available to them, there are a number of additional costs associated with these alternatives. As noted earlier in the release, extensive empirical evidence suggests that as documents get lengthier and more complex, readers either stop reading or read less carefully.[656] Retail investors, therefore, may become overwhelmed if presented with lengthy disclosure, which could bury the information that is most important to

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655 *See supra* note 20.

656 *See, e.g.*, 917 Financial Literacy Study, *supra* note 20.

investors and reduce the effectiveness of those disclosures.[657] Further, the compliance and production costs of additional disclosure would increase significantly the overall compliance costs to broker-dealers and registered investment advisers.

As another alternative, the Commission could require a shorter relationship summary, limited to one page (or equivalent limit for electronic format) that would highlight important topics for retail investors and/or including only key questions for retail investors to ask. This alternative relationship summary would be highly readable, with prescribed formatting, and could highlight the differences between brokerage and advisory services and fees, and flag for retail investors the existence of firms' and financial professionals' conflicts of interest without discussing any specific conflicts. However, the one-page relationship summary would be the same or very similar across firms, and therefore likely would not facilitate detailed comparison across firms or provide enough information to highlight the differences for most retail investors.

We alternatively could require firms to create separate relationship summaries for each account type they offer to retail investors, and require firms to provide a retail investor only the relationship summary for the service being offered.[658] This would result in more detailed disclosures on specific account types, and would potentially provide retail investors with more relevant information about account types that they are interested in reviewing (and less extraneous information about account types that they are not interested in reviewing). However, providing such focused relationship summaries could decrease comparability across account types, as the relationship summary would not present, in one place, the differences in accounts

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657 *See also supra* note 50 and accompanying text (discussing comment letters to the 917 Financial Literacy Study regarding the length of disclosure documents).

658 *See* Comment letter of Fidelity responding to FINRA's Regulatory Notice 10-54 (Dec. 27, 2010), *available at* http://www.finra.org/sites/default/files/NoticeComment/p122723.pdf.

and services offered.[659] In addition, this would result in more costs to firms with multiple advisory and brokerage services, as they would be required to prepare several relationship summaries, although they may also have the resources to do this. The Commission preliminarily believes that, as a tool for layered disclosure, the relationship summary as proposed facilitates retail investors' ability to obtain more detailed disclosures on account types by encouraging retail investors to ask questions and request more information.

d. Delivery

As currently proposed, firms would be required to deliver the relationship summary before or at the time an investment adviser enters into an advisory agreement with a retail investor, or, for broker-dealers, before or at the time the retail investor first engages the firm's services. Dual registrants would be required to deliver the relationship summary at the earlier of entering into an investment advisory agreement with a retail investor or the retail investor engaging the firm's services. As with other disclosure, a firm would be permitted to deliver the relationship summary (including updates) electronically, consistent with the Commission's guidance regarding electronic delivery. In addition, firms would be required to implement a one-time delivery of the relationship summary to existing retail investors as a transition requirement. We are also proposing a requirement for firms to post their relationship summaries on their websites in a way that is easy for retail investors to find, if they maintain a public website. Firms that do not maintain a website would be required to include in their relationship summaries a toll-free number for investors to call to obtain documents.

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659 We note that firms with multiple account types within brokerage or advisory would not have the flexibility to describe/distinguish the different account types (e.g., a brokerage firm that offers a range of accounts – from completely self-directed to mutual-fund only to full-service).

In addition, a firm would be required to provide a relationship summary to an existing client or customer who is a retail investor before or at the time a new account is opened or changes are made to the retail investor's account(s) that would materially change the nature and scope of the firm's relationship with the retail investor, as described in more detail in Section III.C.2 above. A firm would also be required to deliver the relationship summary to a retail investor within 30 days upon request. Furthermore, firms would be required to file current relationship summaries with the Commission, which would be made publicly available, and would be required to post a current version of their relationship summary on their website, if they maintain one.

As an alternative regarding delivery, the Commission could require that the relationship summary would only be available through electronic delivery, such as an email attachment, an email with the full text of the relationship summary in the body of the text, or an email with a hyperlink to the firm's website. Although alternatives relying exclusively on electronic delivery could reduce costs associated with the production of those disclosures, the proposed approach would give the potential benefits of providing information to retail investors in a timely fashion in order to help retail investors select a financial professional or firm, while recognizing the proliferation of the various means of communications, electronic or otherwise, available to firms and retail investors. Our approach also recognizes that some retail investors may not have Internet access or may prefer delivery in paper.

The Commission could have also eliminated the requirement for firms to post the relationship summary on their websites and file the disclosure with the Commission. However, we believe that the relatively minimal cost to firms for posting and filing is outweighed by the

benefit of providing easily accessible information to retail investors to assist them in deciding among firms and financial professionals.

Another possibility would have been also not to require a one-time delivery of the relationship summary to existing retail investors. The Commission believes that since the information in the relationship summary is potentially valuable to new investors it would be also potentially valuable for the existing customers of broker-dealers and investment advisers. While existing retail investors would face higher costs to change from an existing financial services provider to a new one than new potential investors would, most existing investors would be still able to reevaluate their relationships with their current firm and investment professionals. Furthermore, there is an inherent cost to retail investors when the services they receive do not meet their expectations. To the extent delivery of the relationship summary to existing retail investors fosters greater understanding and decreases the mismatch, this could mitigate any costs of changing financial service providers. Distributing the relationship summary to a larger group of initial investors further increases the group of individuals that could become familiar with the disclosure indirectly through interactions with family and friends.

As another alternative, the Commission could have proposed only a delivery requirement for the relationship summary, like Form ADV Part 2B, instead of also requiring that firms file it with the Commission. As discussed also in Section III.A above, although not requiring the summaries to be filed with the Commission could reduce the costs to firms for preparing the document to be filed, the Commission believes that public access to relationship summaries benefits prospective retail investors by allowing them to compare firms when deciding whether to engage a particular firm or financial professional or open an advisory or brokerage account, particularly if the summaries can be located on a single point of access. Further, filing the

relationship summary with the Commission provides public access regardless of whether a particular firm has a website with which to provide public access to the disclosure.

e. Communicating Updated Information

As currently proposed, firms would need to update their relationship summary within 30 days whenever any information in the relationship summary becomes materially inaccurate. Our proposal would also require firms to communicate the information in the amended relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge. The communication can be made by delivering the relationship summary or by communicating the information in another way to the retail investor.[660] Each firm would also be required to post the updated relationship summary prominently on its website (if it has one) and electronically file the current version of the summary with the Commission.

Alternatively, the Commission could require that the relationship summary also be updated and delivered annually, which would be similar to the current requirements for investment advisers to provide an updated "brochure" derived from Part 2A of Form ADV to their existing retail investors both annually and upon any changes to the Item 9 of Part 2A (disciplinary information). The Commission preliminarily believes that the benefits of preparing and delivering an annual relationship summary, regardless of the format of that delivery, would not outweigh the costs to produce and distribute. As noted earlier, the Commission anticipates that the terms of the business relationship between most firms and their retail investors would be relatively stable over time, except when a new account is opened or a significant amount of assets is moved from one type of account to another that is different from the retail investor's

660 *See supra* Section 0.

existing accounts, or other changes are made that result in a material change to the nature and scope of the firm's relationship with the retail investor. As a result, every new delivery would bring relatively small amount of information to retail investors.

We believe that mere public posting of the updated summary would not itself adequately inform retail investors about material changes to the relationship summary, and that firms providing communication of information about relationship summary updates to investors as described above is therefore necessary.

Finally, instead of proposing that firms may choose to communicate information about updated relationship summaries to existing retail investors instead of delivering an updated relationship summary, the Commission could have proposed that firms must deliver the updated relationship summary to each existing retail investor regardless of whether or not it communicated the information to retail investors in another way. While delivering the summary would provide retail investors with the full scope of changes being made to the summary in the context of existing information, the Commission preliminarily believes that allowing firms to communicate information about the updates as well as making the current version of the summary publicly available, via a firm's website (if the firm has a website) and on the Commission's website, provides flexibility for firms to utilize existing communication methods and reduces the costs of delivery on firms while providing adequate notice to retail investors about the updates to the relationship summary, as well as access to the updated summaries.

5. Request for Comments

The Commission requests comment on all aspects of the economic analysis, including the analysis of: (i) potential benefits and costs and other economic effects; (ii) long-term effects of the proposed relationship summary on efficiency, competition, and capital formation; and (iii)

reasonable alternatives to the proposed regulations. We also request comments identifying sources of data and that could assist us in analyzing the economic consequences of the proposed regulations.

In addition to our general request for comment on the economic analysis, we request specific comment on certain aspects of the proposal:

- Do commenters agree with the overall assessment that the relationship summary would benefit retail investors and assist them in making a choice of what type of account matches their preferences? Do commenters believe there are alternatives to the structure and content of the relationship summary that we have not considered that could make it more beneficial to retail investors? Are there any unintended costs of the relationship summary for retail investors that that we have not considered?
- Do commenters believe that the proposed disclosures about relationships and services and fees are clear and effective enough? How would you recommend altering the presentation of these disclosures in order to increase their effectiveness?
- Do commenters agree the proposed disclosure of the categories of conflicts of interest would be beneficial to retail investors? How would you recommend altering the presentation of the conflicts of interest information so that costs are minimized?
- What additional costs and benefits do you envision with extending the disclosure of disciplinary history?
- Are there alternative key questions we should consider recommending that retail investors ask their financial professional? Are there questions we should exclude, and, if so, why? Do commenters agree with the concern that there could be potential costs associated with the list of proposed questions, such as anchoring the attention of retail

investors to the list and thereby reducing the likelihood that they would explore other potential questions that could be important to them?

- What costs do commenters anticipate that firms and financial professionals will incur in implementing and complying with the proposed Form CRS, both initial and ongoing? Please provide estimates of the time and cost burdens for preparing, delivering and filing the proposed form. What costs do commenters expect firms and financial professionals will incur to prepare answers to the "Key Questions to Ask" in the proposed Form CRS? Please provide estimates of the time and cost burden for preparing to answer the questions.
- How do commenters anticipate that the benefits and costs of the proposed rule will be shared between broker-dealers and their clients; or between investment advisers and their clients?
- Do commenters anticipate that the benefits and costs of the proposed rule would be different across broker-dealers and investment advisers? What about dually-registered firms?
- Are retail investors likely to access and download relationship summaries of broker-dealers through EDGAR and investment advisers through IAPD?
- Are there other reasonable alternatives that the Commission should consider? If so, please provide additional alternatives and how their costs and benefits would compare to the proposal.

C. Restrictions on the Use of Certain Names and Titles and Required Disclosures

As discussed above, several studies suggest that retail investors may lack financial literacy and are confused about the differences between broker-dealers and investment

advisers.[661] Part of this confusion may be related to the current use of professional names and titles as indicated by these studies and commenters.[662] This proposal would seek to reduce investor confusion related to the use of certain terms in firm names and professional titles and prevent retail investors from potentially being misled that their firm or financial professional is an investment adviser, resulting in investor harm. In particular, our proposed rule seeks to restrict a broker or dealer, and any natural person who is an associated person of such broker or dealer, when communicating with a retail investor, from using as part of its name or title the words "adviser" or "advisor" unless such broker or dealer is registered as an investment adviser under the Advisers Act or with a state, or such natural person who is an associated person of a broker or dealer is a supervised person of an investment adviser registered under section 203 of the Advisers Act or with a state, and such person provides investment advice on behalf of such investment adviser.[663] In addition to the restriction on the use of certain names and titles, we are proposing rules that require both broker-dealers and investment advisers to prominently disclose their registration status with the Commission and for their financial professionals to disclose their association with such firm in all print and electronic retail investor communications. Dual registrants would be required to disclose both registration statuses.

This section provides an analysis of the economic effects of the proposed rules relative to the baseline, including a discussion of the benefits and costs to the affected parties and the

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661 *See* Siegel & Gale Study, *supra* note 549 and RAND Study, *supra* note 5. Although these studies do not limit the types of financial professionals exclusively to broker-dealers or investment advisers, the majority of the survey questions focus on differences between advisory services versus brokerage services.

662 *Id. See supra* note 4.

663 *See* section 202(a)(25) of the Advisers Act [15 U.S.C. 80b-2(a)(25)] defining "supervised person" as any partner, officer, director (or other person occupying a similar status or performing similar functions), or employee of an investment adviser, or other person who provides investment advice on behalf of the investment adviser and is subject to the supervision and control of the investment adviser.

impact on efficiency, competition and capital formation. We also discuss reasonable alternatives to the proposed rules.

1. Broad Economic Considerations

The economic tradeoffs involved in the choice of names and titles by firms and financial professionals are complex and affected by a wide range of factors. In this section, we discuss under what conditions firm names and financial professionals' titles may convey information that is important to retail investors when they are searching for a provider of financial advice, as well as factors that are likely to matter for firms and financial professionals when choosing their names and titles. We also discuss some conditions where investor confusion over the information conveyed by the names and titles chosen by firms and financial professionals may lead to investor harm.

We believe that investors fall into a spectrum of knowledge about the providers in the market for financial advice. On one end of the spectrum, there are investors who may understand and correctly distinguish the types of services and standard of conduct provided by different types of firms and financial professionals. If firms and financial professionals use names that accurately describe their regulatory type, these types of investors would understand and expect that "broker-dealers," or close synonyms thereof, would provide the services of, and be subjected to the standard of conduct applicable to, a broker-dealer, while "investment advisers," or similar names and titles, would provide the services of, and be subject to the standard of conduct applicable to, an investment adviser. On the other end of the spectrum there are less knowledgeable investors who do not understand that there are different types of services that can be provided by firms or financial professionals, or differing applicable standards of conduct. These investors may not be able to discern from the name or title what type of service

will be provided by a firm or financial professional. As a result, these investors may bear costs associated with their confusion, such as increased time and effort ("search costs") to identify the right type of financial professional,[664] or harm associated with inadvertently selecting, or potentially being misled to select, a type of firm and financial professional that is not consistent with their preferences and expectations. The harm from a mismatched relationship could be, for example, a higher-than-expected cost of services or reduced protection for the investor.

In addition to confusion over firm names and professional titles, and what they may represent, some investors may also have confusion over the type of brokerage, advisory and other services and standard of conduct that best match their preferences. Retail investors, therefore, can also be categorized based on whether they know the type of advice relationship (and associated payment model) that they would prefer, regardless of whether they understand the names and titles of firms and professionals. For instance, some investors may know that they prefer to receive and pay for advice on a per transaction basis, such as that provided typically by a broker-dealer, while others know they prefer an ongoing advisory relationship with an asset-based fee model, such as that typically provided by an investment adviser. On the other hand, some other investors may only understand that they are seeking financial advice but do not understand that there are different types of advice relationships, and different ways to pay for advice, and may not correctly identify the type of advice relationship that would be most consistent with their preferences. This dimension of investor confusion could also lead to investor harm such as increased search costs, an overall mismatch in the type of advice relationship, or paying more than expected for services received.

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[664] According to the 2009 National Survey Initial Report (*see supra* note 275), of the 816 survey respondents that used a financial professional in the last five years, 56% indicated that when looking for a financial professional, they met or talked with more than one professional before making their choice.

In principle, firm names and professional titles used by financial intermediaries, to the extent that names and titles accurately reflect the financial services provided, may serve as a search tool for some investors when they initially select which financial professionals to approach. In particular, for investors that both understand and correctly interpret company or professional names and titles and also know the type of investment advice relationship that they prefer, names and titles of firms and financial professionals that are mainly associated with one type of financial services could be used as an initial sorting mechanism that may reduce search costs. For example, to the extent names and titles accurately reflect the type of firms and financial professionals, knowledgeable investors that prefer only brokerage services could lower their search costs by using names and titles to increase the likelihood they would contact broker-dealers rather than investment advisers in their search. Similarly, knowledgeable investors looking to hire an investment adviser would more easily be able to contact investment advisers and avoid contacting broker-dealers simply by observing the firm or professional names and titles. We also note that investors who understand the differences between broker-dealers and investment advisers generally are unlikely to face a mismatch in the selection of a financial professional, and that the names and titles, in this case primarily serve to reduce search costs.

Less knowledgeable investors may face confusion over either the information conveyed by firm or professional names and titles or the preferred scope of their advice relationship. To the extent that names or titles used by financial intermediaries accurately reflect services provided, any reduction in search costs or reduction of the risk of investors matching with the wrong type of firm and financial professional will depend on the nature of the investor confusion, as we discuss in more detail below.

When selecting firm or professional names and titles, financial services providers may account for the level of investor understanding (or confusion). For example, they may be aware that some investors are informed by the use of particular names and titles, and the implications for the services provided and applicable standard of conduct, while other investors may face confusion over the use of particular names and titles or the type of advice relationship they seek. The incentives of financial intermediaries are two-fold: (1) they seek to build their client/customer base; and (2) they desire to reduce the costs associated with building that client/customer base, such as the time, effort, and marketing costs incurred in the initial client acquisition process. Therefore, financial intermediaries would rationally choose titles that effectively attract the attention of potential investors, while reducing the likelihood of "false starts" with investors that are not the right match (and understand what type of advice that they seek). For example, if investors that fully understand the differences between different types of financial intermediaries are a significant majority of the potential investor pool, then profit maximizing financial intermediaries would likely choose names and titles that clearly identify the nature of services provided and applicable standard of conduct. These knowledgeable investors will then be able to identify from that choice of name or title whether the firm or financial professional will meet their preferred type of investment advice relationship, and therefore, the unambiguous choice of title by the financial professional both reduces search costs incurred by these investors and reduces the effort expended by the financial professionals to build their customer base.

Continuing the same example, the remainder of the investor pool would then consist of less knowledgeable investors, which would represent a small portion of the aggregate investor pool. These investors, in particular those who are confused about the differences among firms

and financial professionals and what type of investment advice relationship they should seek, may be unlikely to understand from names or titles alone how well the financial intermediary would match their preferences, and therefore, will bear search costs and the possibility of mismatch even when names and titles provide little ambiguity for informed investors. However, we expect that when the hypothetical investor pool predominantly consists of investors who fully understand the differences between different financial intermediaries, as we assumed for this example, overall costs borne by both investors (*e.g.*, search costs) and financial intermediaries (*e.g.*, customer acquisition costs) are minimized by the use of distinct names and titles clearly identifying financial intermediary type.

As the hypothetical pool of less knowledgeable investors that face confusion over company names, titles, or services increases, the choice of names and professional titles by financial intermediaries become more complex to analyze and depends on a number of factors related to investors. These factors include, among others: (i) whether and how much these investors infer information from titles about the type of advisory or other services provided; (ii) the source of investors' confusion, such as (a) a lack of understanding about the type of service they would prefer, (b) an inability (in the absence of additional information) to understand the differences in the services offered and their associated payment models, or (c) a lack of knowledge about professional titles and information provided therein; (iii) how easily investors can learn, upon meeting with a financial professional, about whether the type of advice or other services provided by the financial professional meets their preferences; (iv) whether investors could be persuaded to choose a type of advisory service that is not consistent with the investor's preferences after meeting with a financial professional; (v) investors willingness or ability to keep searching for a financial professional until they find one that best matches their preferences;

and (vi) the distribution in the investor pool of investors with different levels of knowledge and understanding as described above.

When less knowledgeable investors are confused not only about what services broker-dealers and investment advisers provide, but also are confused about the types of services that they would prefer, the factors noted above may lead firms and financial professionals of either type to rationally choose generic or common terms in names and titles. Consider the example where retail investors know they would benefit from financial advice in a general sense, but are confused about which type of investment advice relationship and associated payment model would be best for them.[665] A portion of these investors are also persuadable, to some degree, to contract for whatever service is offered to them by any given financial professional they contact, regardless of whether that type of service matches the investors' preferences.

In this case, and in order to maximize the number of investors that a firm or financial professional may be able to contract with, both broker-dealers and investment advisers facing these less knowledgeable investors would have incentives to pick names and titles that are the most effective at getting these investors to approach them, to the extent that names or titles alone have any impact on the choices made by these investors.[666] Once these investors make contact, a

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665 The assumptions underlying this hypothetical example are meant to be illustrative of the incentives of firms and financial professionals to pick certain names and titles when their pool of potential customers is relatively uninformed. Should the relationship summary disclosure be provided to potential and existing customers, we believe that some of the confusion regarding the nature of services would be addressed/mitigated; however, some investors may still, even in the event that the relationship summary is provided be confused about what type of firm or financial professional or which particular service is best for their investing situation.

666 Although a number of studies discussed in the baseline provide survey evidence that investors are confused about titles, we are unaware of any direct evidence that titles alone affect the choice of firms or financial professionals that are contacted or eventually hired. However, in conjunction with the proposed relationship summary , we expect that investors would gain better understanding of the services provided by, and standards of conduct applicable to, broker-dealers and investment advisers, which could lead to more informed decision making about choosing the type of financial intermediary that best matches to the investors' own expectations regarding services and standard of conduct.

firm and financial professional hypothetically may be able to persuade the investor to hire them regardless of the type of financial advice relationship offered, to the extent that the investor cannot distinguish the characteristics of different types of advice relationships that best fit their preferences, does not know the most cost effective way to pay for that relationship, and cannot easily distinguish between the types of relationships that are offered by different firms and their financial professionals. In order to attract this type of investors, firms may favor titles that indicate their financial professionals' ability to dispense guidance and advice. For example, they may select titles that include the word "adviser" or "advisor," such as "financial advisor".[667]

In addition to potential search costs expended by less knowledgeable investors, these investors also bear a greater risk of mismatch between the type of advice relationship that best fits their preference and the actual advisory service for which they contract. However, in this example, the mismatch arises because of investor confusion over the type of relationship that best would meet their preference, and this confusion itself may lead the investor to, by chance, seek out a type of firm or financial professional that is inconsistent with the investor's preference, rather than any confusion directly related to the firm's or financial professional's use of a common name or title. Conversely, generic names and titles may make it easier for less knowledgeable investors to identify a broader class of firms or financial professionals that can meet their perceived need for financial advice to some extent.[668] In situations where the pool of less knowledgeable investors is likely to be large, one likely outcome is that many firms and

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667 Alternatively, these firms may choose relatively generic names or titles that in other ways suggest an advisory service, such as "financial planner" or "financial consultant," which are not subject to the present rulemaking proposal.

668 To the extent generic titles in use today such as "financial planner" and "financial consultant" make it more likely less knowledgeable investors can identify both investment advisers and broker-dealers that offer advice, there may be benefits to some of these investors if they in their contacts with financial professionals of both types learn about which relationship and payment models is most consistent with their preferences.

financial professionals could end up using similar names or titles, which would potentially increase search costs for those more knowledgeable investors who otherwise may use names and titles as an initial sorting mechanism.

Other particular kinds of investor confusion, which could impose costs on some investors, may provide benefits, such as increased customer flow, to only a certain type of firm or financial professional. For example, some investors may be fully aware of the type of advice relationship that they prefer, but are confused about which firm or professional names and titles are associated with that type of advice relationship. In particular, consider a situation where investors know that they would like an advice relationship that is provided by investment advisers. In this case, some broker-dealers may have incentives to use titles such as "advisor" that suggest such an advice relationship to maximize their customer flow. As a result, some less knowledgeable investors may be misled to wrongly approach broker-dealers rather than investment advisers in their search for advice, and bear both potentially higher search costs and an increased likelihood of a mismatch between the type of advice that is received and the type of advice that is preferred. The risk of a mismatch and associated harm in this case would be especially large for any of these investors that primarily base their choice of firm and financial professional on names and titles, rather than any information they would receive from a firm or financial professional about the type of services or applicable standards of conduct.

In addition to the factors related to investors discussed above, the selection of names and titles by financial intermediaries also depend on other factors specific to the intermediary. For example, competitive concerns may cause some financial intermediaries to simply choose terms in names and titles that are commonly used by other financial intermediaries of their type. Alternatively, firms may choose names and titles that distinguish them from their competitors.

Some firms or financial professionals may choose ambiguous generic titles, such as "financial consultant," in order to capture a larger fraction of the investor pool, thinking that investors may seek information if the title does not clearly identify the kinds or levels of services provided or the applicable standard of conduct. We acknowledge that these factors could also be important determinants of the choice of names and titles.

2. Economic Effects of the Proposed Restrictions on the Use of Certain Titles and Required Disclosures

In this section we discuss the potential economic effects from the proposed rules to the directly affected parties: investors, standalone broker-dealers, standalone investment advisers, dually registered firms, and financial professionals. Potential economic effects on indirectly-affected parties, in particular financial intermediaries not regulated by the Commission, are discussed in the next section.

a. Investors

The objective of the proposed rules is to reduce retail investor confusion and limit the ability for retail investors to be misled that a firm or financial professional is an investment adviser as a result of the use of firm and financial professional names and titles that contain either "adviser" or "advisor". Specifically, our proposed rule seeks to enable retail investors to be able to discern more fully whether a particular firm or financial professional will offer advisory or other services provided by investment advisers versus those provided by broker-dealers. In this section, we discuss the potential benefits to investors as a result of the proposed rules, while considering the potential costs that could be borne by investors. In general, we expect the benefits and costs are unlikely to be evenly distributed among investors, but will rather depend on both the differences in investors' preferences for broker-dealer or investment

adviser services, and investors' individual degree of understanding what services any given firm or financial professional is providing and the standard of conduct that is applicable.

i. Benefits of Restrictions on the Use of Certain Names or Titles

The proposed restriction on the use of the terms "adviser" and "advisor" in names and titles of broker-dealers who are not also dually registered as investment advisers and of financial professionals who are not supervised persons of investment advisers and who provide advice on behalf of such advisers, may reduce investor confusion about what type of firm or financial professional is likely to match with their preferences for a particular type of investment advice relationship. The proposed rule may also reduce corresponding search costs for some investors under certain conditions. Moreover, the proposed rule may reduce the likelihood that a mismatch between an investor's preferences and the services offered by a firm or financial professional occur.[669] Specifically, to the extent investors looking for an advice relationship of the type provided by investment advisers, and believe that names or titles containing the terms "adviser" or "advisor" are associated with this type of advice relationship, the proposed rule would make it easier to identify firms and financial professionals that offer such advice relationships, thereby reducing investor confusion, search costs, and any mismatch in the advice relationship that may occur from the potential misleading nature of such names or titles, as well as any associated harm with such mismatch.[670]

As a result of the proposed restriction on the use of certain terms, we expect the greatest potential reduction in search costs for retail investors who know that they specifically want the

669 We note that a potential mismatch could occur because investors may contact the wrong type of firm or financial professional and may not fully understand the type of financial advice that best match their preferences (even if the proposed relationship summary is made available), may be persuaded to hire the wrong type of firm or financial professional, or may be misled that a firm or financial professional will provide the type of service that the investor prefers, but in fact, does not.

670 *See supra* discussion in Section IV.C.1.

services provided by investment advisers and also would use names and titles in their search. The proposed rule would potentially make it easier for such investors to distinguish firms and professionals providing investment adviser services from firms and professionals providing brokerage services. The proposed rules may also reduce search costs for investors that prefer brokerage services, if standalone registered broker-dealers and financial professionals who are not supervised persons of an investment adviser or who are supervised persons but do not provide investment advice on behalf of such investment adviser are using names or titles including "adviser" and "advisor," would choose new names and titles due to the proposed rule that more distinctly indicate the types of services they provide, such as "broker" or "broker representative."

However, the reduction in search costs for retail investors as a result of the proposed rule would be limited to the extent the firms and financial professionals covered by the restriction on the use of the terms "adviser" or "advisor" are not currently using the proposed terms in their names and titles. Further, the potential impact of the proposed rule on search costs is likely to be mitigated to the extent the proposed rule is limited to firm names and job titles, and would not itself affect the use of terms, such as "advisory services" in other communications or using those terms in metadata to attract internet search engines.[671] Moreover, beyond registered investment advisers, dual registrants, and their supervised persons, other types of financial services providers, such as insurance companies and banks, may also continue to use the terms "adviser" and "advisor" in their names and professional titles, and any confusion and search costs borne by investors related to the use of such names and titles by financial intermediaries not affected by

[671] As discussed above, these other communications by firms and financial professionals would continue to be subject to antifraud rules. *See supra* note 309.

this proposed rule would not be reduced. As noted above, the Commission recognizes that terms such as "financial advisor" or "financial consultant" may be used by banks, trust companies, insurance companies, and commodities professionals.[672]

As discussed above in Section IV.C.1, some investors may be confused by names and titles and believe that certain names and titles are likely to specifically signal the type of advice services provided by firms and financial professionals that use those names and titles and the associated standard of conduct.[673] In particular, investors that prefer the type of investment advice relationship and the associated standard of conduct offered by investment advisers may believe that names or titles containing the terms "adviser" or "advisor" are only associated with that type of advisory relationship. If some of these investors are persuaded by financial professionals associated with broker-dealers (who are not themselves investment advisers or supervised persons of investment advisers who provide advice on behalf of such adviser) that they could have a similar type of advice relationship as they would with an investment adviser, a potential mismatch between investor preferences and the advice relationship received may occur, which in turn may lead to investor harm such as higher payments for the services by the investor than necessary.[674] Thus, the proposed prohibition on the use of "adviser" or "advisor" by certain broker-dealers may reduce the risk of a mismatch between investors seeking advisory services of the type provided by investment advisers and the type of services for which they contract, as

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672 *See supra* note 400. Further, as identified by Commission staff, as of December 2017, approximately 546 broker-dealers reported at least one type of non-securities business, such as insurance, retirement planning, and real estate; *see supra* note 459.

673 As discussed in Section IV.A.3.b, survey evidence suggest that many investors in general do not have a clear understanding about the differences in the nature of the advisory services provided by, and standard of conduct applicable to, different types of financial professionals.

674 Broker-dealers may elect to provide some services similar to those of many investment advisers, such as ongoing monitoring, thereby potentially mitigating any mismatches between preferred services and the services provided.

these investors under the proposed restriction would be potentially less likely to be misled or inadvertently approach and hire a type of firm or financial professional that does not match with their preferences and expectations.

Because mismatch in investor preferences and the type of advice relationship they receive can potentially be very costly for investors by resulting in inefficient advice relationships, reducing this cost could be a potential benefit of the proposed rule for some investors. In particular, if an investor seeks an advice relationship of the type offered by investment advisers, but mismatches to a brokerage relationship, then the frequency of advice received may not be the most appropriate, or the cost for the advice may be too high if it leads to frequent trading, and could result in suboptimal investment decisions or lower investment returns net of costs. The Commission preliminarily believes this reduction in mismatch risk would mainly apply to those investors seeking a relationship similar to that provided by investment advisers, as discussed above. However, for at least some investors requiring advice on a per-transaction basis, the confusion about the use of titles or the services provided by financial professionals could potentially lead them to inadvertently select investment advisers even if they truly want a broker-dealer. To the extent the proposed rule would also help these investors more clearly distinguish between broker-dealers and investment advisers, they may avoid inadvertently hiring an investment adviser and thereby avoid paying potentially higher fees for that type of advice relationship.

At this time the Commission is unable to estimate how many investors have contracted for services that do not meet their preferences, or are paying more than they would have preferred for services, due to confusion about the names and titles of financial intermediaries. Further, to the extent that confusion exists among retail investors regarding the names and titles

used by firms and their financial professionals, surveys of retail investors with brokerage accounts suggest that they tend to be satisfied with their firms and financial professionals, and also believe that services provided by these firms and financial professionals are valuable, which further complicates any estimate of the incidence or magnitude of harmful mismatch.[675]

As discussed above with respect to search costs, any reduction in mismatch risk associated with investor confusion over names and titles would be limited to the extent that standalone registered broker-dealers and their associated natural persons do not use the proposed prohibited terms in their names and titles. This would also be the case to the extent that registered representatives of dually-registered broker-dealers who are not themselves supervised persons of an investment adviser or who are supervised persons but do not provide investment advice on behalf of such investment adviser do not use those terms. The potential reduction in mismatch risk due to this proposed rule would also be limited to extent the rule is limited to firm name and individual job titles, and would not itself affect firms and financial professionals from using terms such as "advisory" in other content. Moreover, other types of financial intermediaries may use the terms "adviser" and "advisor" in their names and titles, such as banks, trust companies, insurance companies, and commodities professionals.[676] Therefore, the potential gains associated with a reduction in mismatch risk due to the prohibition on certain names and titles may be limited because some confused investors seeking an advice relationship from investment advisers could continue to inadvertently hire these other types of financial intermediaries that also use "adviser" or advisor" in their names and titles.

675 *See* RAND Study, *supra* note 5, at 98.

676 *See supra* note 400.

Another potential limitation of the proposed restriction on the use of certain titles is that a dual registrant could still call itself an "adviser" or "advisor," but then only offer brokerage services to investors that may not be legally and financially sophisticated enough to understand the differences in types of relationships and standards of conduct available.[677] Finally, for retail investors that rely on professional or personal recommendations in their search for financial professionals, the proposed prohibition on the use of certain titles is likely to have a limited effect on both search costs and the risk of mismatch in the advice relationship.

ii. Costs of the Restriction on the Use of Certain Titles

Although the Commission preliminarily believes that the proposed rule would decrease investor confusion, search costs, and mismatch for some segment of the investor pool that search for professionals based on names or titles, investor confusion and search costs could increase for those that would have, in the absence of the rule, selected broker-dealers and associated natural persons that would have to change their company names or titles as a result of the proposed rule.[678] For example, prospective customers familiar with a firm's name or financial professional's title may be especially confused by a change of either name or title to the extent that the term "adviser" or "advisor" is part of the firm's name brand or the titles of the professionals. Any increase in confusion as a result of the rule along these lines would likely be larger if the changed names or titles of broker-dealer firms that currently contain the words

677 As discussed above, however, financial professionals who are not themselves investment advisers or supervised persons of investment advisers and who provide advice on behalf of such advisers would also not be able to use the terms "adviser" or "advisor" in their professional titles.

678 As discussed in the baseline, several studies indicate that many investors receive personal or professional referrals in the selection of their broker-dealer or investment advisor. However, even these investors may investigate these referrals prior to undertaking outreach, and therefore, may avoid certain financial professionals as a result of the name or title change.

"adviser" or "advisor" are widely recognized as brands by investors.[679] Further, even if the broker-dealer name or title is unlikely to change, some investors may remove certain firms from their search list as professional names or titles change as a result of the rule. If, for example, a prospective investor is using the search term "financial advisor" to search for firms and financial professionals located in their city, some firms and financial professionals will be removed from any possible searches by these investors as a result of the proposed rule, even though these financial professionals might have been the best match to the preferences and expectations of the investor. However, these kind of potential costs to some current investors are likely to be limited to the extent that proposed rule is limited to firm name or title and individual job name or title and would not require firms and financial professionals to remove the restricted terms from other content, if they are not using such terms as a name or a title.

The proposed rule may also increase investor confusion to the extent some firms and financial professionals invent new names or titles to substitute for the restricted ones. Studies already indicate that the wide variety of names and titles used by firms and financial professionals causes general investor confusion about the market for investment advice. The magnitude of such costs is hard to predict, but would likely increase search costs for less knowledgeable retail investors that use names or titles to search for financial professionals or firms, and may also increase the likelihood of a mismatch for some of these investors between the type of advice relationship they prefer and the type of firm and financial professional they hire.

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679 As discussed in the baseline, approximately 87 broker-dealers that are not dually registered as investment advisers and do not report non-securities business use the words "adviser," "advisor," or "advisory" as part of their current company name. These firms would likely have to change their company name as a result of this proposed rule. However, any loss in brand value due to this change could be mitigated to the extent the prohibited terms are not an important part of the firm's brand.

Investors seeking advice from broker-dealers may also face potential harm if some broker-dealers change their business model as a result of the proposed rule. As discussed above, we believe that most broker-dealers that would be subject to the restrictions of the proposed rule have chosen names and titles to build their customer base. Given that the market for investment advice overall appears to be relatively competitive, with respect to the number of firms and financial professionals, firms and financial professionals likely have chosen names or titles that they view as effective in marketing their services to investors. Therefore, being forced to switch names or titles could reduce the potential customer flow for some broker-dealers (and registered representatives of dual registrants who are not supervised persons of an investment adviser or who are supervised persons but do not provide investment advice on behalf of such investment adviser) who currently are using name or titles which include the term "adviser" and "advisor" and who serve retail investors. In lieu of adopting a new name or title without "adviser" or "advisor," these firms or financial professionals might respond by exiting the retail investor market, or may bypass the compliance and other costs associated with this proposed rule by also registering as investment advisers or becoming supervised persons of an investment adviser who provide investment advice on behalf of such investment adviser, which would change their incentives to market their brokerage services to investors.[680] Either of these changes to business practices could reduce the availability of broker-dealer services for investors.[681] To the extent

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680 Some firms could potentially increase their profits by moving some customers from a brokerage account to an advisory account (*e.g.*, customers who rarely trade). Such firms would have incentives to cut back on marketing of existing brokerage services to such customers and instead market the new advisory services.

681 For example, in the event of exit by a broker-dealer, investors who want broker-dealer services would be forced to undertake search costs to find another firm and financial professional to meet their perceived needs, but also bear an increased cost associated with mismatch if they choose the wrong type of firm and financial professional. In the event of a switch from a brokerage model to an advisory model, investors may be forced to bear the costs associated with an advisory account that could exceed costs associated with services provided by a broker-dealer, or face costs associated with search and mismatch if they choose to change financial intermediaries, as discussed above.

the costs of exiting the retail investor market or associated initial and ongoing costs of becoming a registered investment adviser (or a supervised person of an investment adviser who provides investment advice on behalf of such investment adviser) are greater than the costs associated with complying with the proposed rule, the likelihood of exit from the retail market or a change to the existing business model from a brokerage to advisory model would be low. In this case, the anticipated effect on investors from the loss of existing broker-dealer advice is expected to be limited. However, if it is costlier to change names or titles than to switch business model for broker-dealers, we expect some investors may experience a reduction in supply of broker-dealer advice services. Finally, because the Commission recognizes that a standalone broker-dealer can provide advice to retail investors without being regulated as an investment adviser provided that such advice is merely "solely incidental to" its brokerage business and the broker-dealer receives no "special compensation" for the advice, the proposed restriction would not prevent standalone broker-dealers from conveying the services that they provide in other content, without using the titles or names "adviser" or "advisor." This may also limit the likelihood of exit from the retail market or a change to the existing business model from a brokerage to an advisory model.

The proposed rule could, however, also increase the risk of mismatch for some investors by removing standalone registered broker-dealers and registered representatives of dual registrants who are not supervised persons of an investment adviser from the pool of financial intermediaries that use the terms "adviser" or "advisor" in names and titles, while not affecting the use of these terms by other types of financial intermediaries, including banks, trust companies, insurance companies, and commodities professionals. Investors who are seeking financial services from either investment advisers or broker-dealers could instead inadvertently

hire other types of financial intermediaries that would continue use these terms "adviser" or "advisor," thereby potentially exacerbating the degree of mismatch between the type of relationship that they seek and what they receive. Further, neither this rule nor the proposed relationship summary would address the potential mismatch because these entities and natural persons are outside of the scope of the Commission rules. The Commission is not able to estimate the scope of this continuing potential for mismatch because we do not have access to information on the extent to which retail investors include these other types of financial intermediaries (deliberately or inadvertently) in their search for financial advice, nor the extent to which they see the services provided by these other financial intermediaries as substitute for the services provided by investment advisers or broker-dealers.

Another potential cost for investors is that affected broker-dealers may attempt to directly pass through any costs they would incur due to the proposed restriction on certain names and titles. A broker-dealer's incentives for such pass-through behavior would be attenuated the more competitive the broker-dealer's local market is in the sense that price sensitivity of demand is high.

Finally, we note that many of the costs and benefits to investors that we discussed above depend on the extent that titles and names affect investors' selection of their financial professional. The evidence discussed in Section IV.A.3.a suggests that between 40% and 50% of investors find their financial professionals through personal recommendations.[682] For this set of investors, the proposed rule would likely have little impact on search costs or potential for mismatch between their preferences and expectations and the type of advisory service for which they contract. We also note that we are not able to provide quantitative estimates of potential

[682] RAND Study, *supra* note 5 and 917 Financial Literacy Study, *supra* note 20.

changes in search costs. Search costs for investors as well as costs due to mismatch would depend on a large set of individual specific factors, such as exactly what procedures investors use to search for financial professionals, what restrictions they put on their search (for example, choice of market, how many firms or professionals they are willing to sample before making a decision), the method they use to evaluate different alternative financial professionals they have identified, etc. The costs will to a large part not be monetary in nature but rather in the form of time and effort spent. The monetized value of that time and effort will also be individual specific. We do not have access to data that would provide us with this type of information, which we would need to estimate search costs. Similarly, we also are unable to provide estimates of changes in costs due to changes in the potential for mismatch as we do not currently have data on the percentage of the investor population that is mismatched, or the extent of harm that comes from mismatch.[683] For example, we don't have an analysis of how well someone would have done in their portfolio (especially after costs) if they had been correctly matched.

iii. Benefits and Costs of the Required Disclosures about Regulatory Status of a Financial Services Provider

We anticipate the proposed requirements for broker-dealers and investment advisers and their associated natural persons and supervised persons to prominently disclose their registration (or firm association for financial professionals) status in retail investor communications would reduce investor confusion as well as search costs associated with locating and hiring a firm, which could reduce the probability of mismatch for investors seeking advice. In particular, for investors who understand the meaning of the registration status and know they want to hire either

683 To estimate the potential harm from mismatch we would need to analyze how well someone could have done in their portfolio (after costs) if they had been correctly matched. This requires a rich set of investor characteristics as well as information about the investment menus and fee structures of potential alternative firms and financial professionals investors could have hired. We do not currently have access to such detailed information.

a registered broker-dealer or a SEC-registered investment adviser, we expect the search for the correct type of firm will be made both clearer and less time consuming, as these investors will more readily observe the registration status. Search costs for investors for whom the registration status has little meaning, however, are not expected to experience a decrease in either confusion or search costs due to these disclosure requirements. Disclosure may also reduce the possibility of mismatch of hiring the wrong type of firm for investors who understand the meaning of the registration status and know what type of financial intermediary they want to hire, although we note that the likelihood for such mismatch is likely lower in the first place for such investors compared to less knowledgeable investors. For the pool of investors that are confused by both the type of advice relationship that they prefer, including how they want to pay for it, as well as professionals' titles, disclosure of registration status alone may not be sufficient to alleviate confusion in the type of advisory services provided by or the standard of conduct applicable to firms or financial professionals. Finally, for retail investors that rely on professional or personal recommendations in their search for financial professionals, the disclosure requirement is likely to have a limited effect on both search costs and the risk of mismatch in the advice relationship. As discussed above, we do not have access to information that would allow us to provide quantitative estimates of the potential costs and benefits to the investor from these proposed disclosure requirements.

In general, we do not anticipate any costs to investors from the proposed rules to disclose registration status. However, it could be that firms may attempt to pass through any compliance costs to investors through higher fees, in particular those that operate in markets where the price sensitivity of demand may be lower. Given that compliance costs would be of a one-time nature, as discussed above, we believe the likelihood and magnitude of such pass-through would be low.

b. Standalone Registered Broker-Dealers

The proposed rule would restrict broker-dealers who are not dually registered as investment advisers and their associated natural persons who are not themselves investment advisers or supervised persons of investment advisers that provide advice on behalf of such advisers from using the terms "adviser" or "advisor" when communicating with retail investors. As described previously in Section IV.A.1, approximately 87% of retail facing broker-dealer firms and 50% of registered representatives are not dually registered as investment advisers, and therefore potentially could be affected by the proposed restriction. The fraction of standalone broker-dealer firms that are currently using the terms "adviser" or "advisor" in their firm names or titles and do not report a non-securities business, is only approximately 3.5%.[684] When it comes to names or titles by registered representatives at standalone broker-dealers, the RAND Study evidence discussed in Section IV.A.1.f suggests that around 31% of professionals providing only brokerage services used titles containing the terms "adviser" or "advisor." If the evidence presented in the baseline, is representative of the overall universe of standalone registered broker-dealers, the fraction of firms and associated natural persons that would be affected by the proposed prohibition may be relatively low.[685]

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684 As discussed in *supra* Section IV.A.1.f, there are 87 (103 - 16 = 87) retail facing standalone broker-dealers without non-securities business that are currently using one of these terms in their firm names, which represents approximately 3.5% of the 2,497 retail acing standalone broker-dealers (2,857 - 360 = 2,497; *see supra* Table 1, Panel B). If we go beyond firm names and instead look at how firms' publicly describe themselves on their websites, the evidence presented in Section IV.A.1.f suggests that of the sampled standalone broker-dealers, less than 10% describe themselves using the terms "adviser" or "advisor." Although some of these website descriptions may still be allowed under the proposed rule, it suggests that the fraction of standalone broker-dealers that rely on these terms to describe themselves may be relatively low.

685 We estimate that approximately 226,132 (942,215 x 0.24 = 226,132; *see supra* Table 6) registered representatives of broker-dealers are not also registered as investment advisory representatives. Among these registered representatives, approximately 119,729 are employed by dually registered firms (494,399 x 0.61 x 0.397 = 119,729; *see supra* Section IV.A.1.e), which means 106,403 are employed by standalone broker-dealers. Further, if only 31% of broker-dealer registered representatives that are not dual-hatted (*see supra* Table 8) use titles containing the terms "adviser" or "advisor," then we estimate that the total

If the proposed restriction on certain names or titles would reduce potential investor confusion and prevent retail investors from potentially being misled, it could have some positive benefits for the subset of broker-dealers that would be impacted by this restriction but are not marketing advice services to attract business. In particular, these broker-dealers may be able to better attract customer flow and more efficiently target their marketing and advertising campaigns to reduce the likelihood of "false starts" associated with the potential mismatch with retail investors. Moreover, broker-dealers that are not dually registered may similarly benefit from the requirement to prominently display registration status as that may also help reduce investor confusion. Firms and financial professionals may also realize a limited benefit from this disclosure such that they can more effectively signal their type in communications, even when the firm or professional names or titles are not perfectly aligned with the registration status.[686]

For the segment of broker-dealers that would be affected by a restriction of using the terms "adviser" or "advisor," we anticipate potentially substantial, one-time costs associated with the proposed rule. Broker-dealer firms subject to the restrictions on the use of certain names or titles would be required to change current company names or titles (if the company name or title

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number of non-dual hatted registered representatives that would be potentially subject to this proposed prohibition would be 70,101, which is approximately 15.5% of all registered representatives. Of these representatives, 32,985 (0.31 x 106,403 = 32,985) are employed by standalone broker-dealers and approximately 37,116 (0.31 x 119,729 = 37,116) are employed by dual registrants. Note, the number of non-dual hatted registered representatives at dual registrants that would be potentially affected by the rule is likely lower than the estimated 37,166 because some of these representatives may be supervised persons providing advisory service without being dual-hatted. We are not able to estimate how large the fraction of such registered representatives would be. On the other hand, we do not have information about how many dual-hatted registered representatives among dual registrants that they are not supervised persons providing advisory services despite being dual-hatted, and therefore would also be subject to the proposed restriction on the use of certain titles.

686 Note that any such benefits from the proposed rules relies on an assumption that some broker-dealers are not currently optimizing to receive such benefits by voluntarily changing names and titles or prominently display their registration status. However, as noted above, we expect in an efficient market, firms have already chosen names and titles that they view as effective marketing tools. As a result, we expect this benefit will be limited to the extent firms are currently rationally optimizing their choice of names and titles.

contains "adviser/advisor"), and marketing materials, advertisements (*e.g.*, print ads or television commercials), website and social media appearances that use the current company name or title, among other items, resulting in direct compliance costs. Similarly, all personal communications tools used by financial professionals, such as business cards, letterhead, social media profiles, and signature blocks would need to be amended to reflect new company and financial professionals' names or titles. The proposed requirement to prominently disclose registration status in print or electronic retail investor communications is also expected to require changes to the same set of materials and communication tools, and therefore, also would have to be modified to incorporate the registration status in the manner the rule prescribes.[687]

To the extent that the costs discussed above have a fixed-cost component (*i.e.*, a print ad would likely cost the same regardless of the size of the firm), the costs associated with producing new communication and advertising materials would be disproportionately higher for smaller broker-dealer firms. Other costs, however, may increase with the size of the broker-dealer, such as costs associated with revisions to each individual representative's communication and advertising materials, and therefore would increase with a broker-dealer's size.

In addition to direct compliance costs associated with producing new materials, broker-dealers would likely bear costs associated with contacting current and prospective customers, whether by email, mass mailings, one-on-one meetings, or telephone conversations, to inform them of changes to names and titles. Such outreach on behalf of the broker-dealer or the individual representatives would inform existing and prospective investors of a name or title change, and whether or not any services have changed and may be necessary in order to

687 *See infra* Section V.G for estimates of some of these compliance costs developed for the purpose of the Paperwork Reduction Act.

minimize any confusion among current and prospective customers that could potentially lead to a loss of business during a "changeover" period.[688] This kind of outreach, however, could be costly to financial professionals and firms if it diverted time and resources away from the core business of the broker-dealer.[689] Further, the greater the name recognition of a current company or the larger the size of the company, the costlier such an outreach is likely to be as more current and prospective customers would need to be informed of the name change. Finally, to the extent that a broker-dealer's company name is recognized as a brand in the market and therefore represents a valuable intangible asset to the firm, some of its "brand value" may be lost following a company name change.[690] We note that the number of broker-dealer firms whose brand value may be negatively affected by the rule is relatively limited, as only around 3.5% of the broker-dealer firms that would be subject to the rule are using any of the prohibited terms in their company names.[691]

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688 In particular, without outreach, some broker-dealers could experience a temporary reduction in the flow of prospective customers that would have relied on the use of titles prohibited by the proposed rule. In the absence of the prohibitions, these investors would have ended up contracting with the broker-dealers, but due to confusion over new company names and titles that would be required to be used, these investors may avoid broker-dealers subject to the change in names and titles, and these broker-dealers could earn less revenue. Only after the potential customer base becomes familiar with the new names and titles associated with a given broker-dealer and its financial professionals, or the search costs associated with these new titles decline, could these firms potentially recover a portion of the prospective customer base that was originally lost during the name transition period as a result of the changeover confusion. The Commission does not have access to the type of detailed customer information of individual broker-dealers that would allow us to estimate the percentage of customers that might be confused as a result of the name change or what fraction of these customers might eventually be recovered by a broker-dealer.

689 Although such outreach is not required by the proposed rule, we anticipate that at least some percentage of affected broker-dealers or financial professionals would undertake such efforts in order to maintain good relationships with existing customers.

690 Academic evidence suggest corporate brands are valuable intangible assets to firms; *see, e.g.*, M. E. Barth, M. B. Clement, G. Foster, & R. Kasznik, *Brand values and capital market valuation*, Review of Accounting Studies, 3(1), 41-68 (1998).

691 *See supra* note 648. Specifically, 3% refers to the total number of broker-dealers that do not report non-securities business.

Likewise, broker-dealers facing no constraints on their choice of names and titles may choose the names and titles that they believe are the most effective at helping attract customers, and may best describe their business model, and reduce the effort associated with building a customer base, as described above.[692] Therefore, a segment of broker-dealers that are currently using terms that would be restricted under the proposed rule could experience a reduction in the efficiency of their marketing efforts, which in turn might lead to fewer customers and a loss of revenue compared to the baseline. In particular, those broker-dealers that rely on advice services as an important part of their value proposition to retail investors and directly compete with investment advisers may lose competiveness, if names and titles become less descriptive of this aspect of their business in the eyes of retail investors. These marketing efficiency costs would be mitigated to the extent the broker-dealers would use new names and titles that are equally efficient at conveying they are providing advice, or to the extent that the proposed restriction would not affect the use of terms such as "advisory services" in other content, or using them in metadata to attract internet search engines.[693]

Although we recognize that a significant fraction of a broker-dealer's customer base is attributed to referrals, as noted in the 917 Financial Literacy Study, approximately 25% of survey respondents rely on broker-dealer or financial professional names or titles in selecting their current advisor.[694] Depending on how effective the terms "adviser" or "advisor" are at attracting

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692 *See* discussion in Section IV.C.1.

693 Note that to the extent affected broker-dealers would choose other names and titles that convey a similar signal to investors as those containing the terms "adviser" or "advisor," it would reduce the efficiency of the proposed prohibition. In Section IV.C.4.a we discuss an alternative that would prohibit a broker-dealer from otherwise "holding out" as an investment adviser, which would potentially also prevent the use of some similar names and titles.

694 *See supra* note 20.

customers, costs associated with the loss of certain titles or names could be substantial for some broker-dealers.[695]

One way that affected broker-dealers could potentially mitigate the costs associated with the potential loss of titles or names could be for these firms to dually register as investment advisers. However, dual registration imposes an additional layer of regulatory oversight and compliance and need for training and licensing of employees to work as investment adviser representatives, which would also be costly. A broker-dealer would likely pursue such a strategy only if it expected the costs of regulation as an investment adviser were lower than the expected costs of modifying names and titles. We do not have access to data that would allow us to estimate either the total costs for modifying names and titles for broker-dealers, or the total costs of becoming an investment adviser for these broker-dealers.

c. Investment Advisers (including Dual Registrants)

The proposed restriction on the use of the terms "adviser" and "advisor" in names and titles does not apply to registered investment advisers, whether they are solely registered as investment advisers or whether they are dually registered. Consequently, there would be no compliance costs for registered investment advisers associated with the restriction on the use of certain terms in names or titles. Some benefits could accrue to investment advisers at the expense of impacted broker-dealers. However, supervised persons of investment advisers who are dually registered but do not provide investment advice on behalf of such investment adviser

695 For example, if investors know that they are seeking advice related to individual transactions (*e.g.*, the type of mutual fund or exchange-traded fund in which to invest), they may have a preference for terms such as "financial advisor" compared to terms such as "financial planner" or "investment strategist," depending on their colloquial understanding of what an these terms might imply for the level of service and standard of conduct. If certain broker-dealers are restricted from using "financial advisor," these firms may lose these potential customers. Moreover, these investors could potentially expend search costs as they sort through investment advisers that use the term "financial advisor" until the investor is able to match with the right type of financial professional.

would be prohibited from using the terms, which could lead to costs for those financial professionals or their firms.

Because the proposed restriction would force some standalone registered broker-dealers to change their names and titles in a way that may lead to less efficient marketing aimed at attracting potential investors, as discussed above, some customer flow that might have gone to these broker-dealers could be permanently diverted to investment advisers who will not be required to change their names.[696] As a result, some investment advisers could experience an increase in revenues due to an increase in customer flow. The benefits may also be larger for investment advisers or dual registrants that are able to continue to use names or titles that include the term "adviser" or "advisor" as these terms could be the draw that currently attracts customer flow to certain firms and financial professionals, and that would be diverted due to a restriction on the use of these terms by standalone registered broker-dealers. In addition, assuming that small broker-dealers and investment advisers select geographic areas where competition from larger firms is low, then, as result of the proposed rule restricting the use of certain names or titles by broker-dealers, small investment advisers could especially benefit at the expense of small broker-dealers in these locations.

In terms of additional potential benefits, investment advisers and dual registrants, like standalone broker-dealers, will be subject to the required disclosure of their registration status, as part of the proposed rules. As we discussed in the case of standalone registered broker-dealers

696 To the extent that investor confusion about the market for financial services generally increases during the period when affected firms and financial professionals remove the term "adviser" or "advisor" from their names and titles, investment advisers that are not required to change their names or titles may see an increase in the diversion of customer flow from broker-dealers to investment advisers until investor confusion over the change in titles subsides. To the extent that some investors that are not currently making an efficient choice of a broker-dealer as indicated by investor confusion about titles and associated standards of conduct, and would choose an investment adviser after the proposed rules were adopted, this proposed rule change may assist them in making a more efficient choice to a service they would prefer.

above, the prominent display of registration status could help reduce investor confusion, and could be used by both firms and their financial professionals as a marketing tool. Moreover, firms may benefit from this disclosure such that they can more effectively signal their type, even if the firm or professional names or titles are not perfectly aligned with the registration status. These potential benefits may be larger for dual registrants, as the prominent display of both their registrations may help attract investors that are looking for both types of services or investors who are generally unsure about which type of services they want.[697]

The proposed restriction on the use of certain names and titles would apply to financial professionals of dual registrant investment advisers who are not supervised persons of an investment adviser or who are supervised persons of an investment adviser but who do provide investment advice on behalf of such investment adviser, which could lead to costs for those financial professionals or their firms. Consistent with the discussion of standalone registered broker-dealer firms above, this segment of persons associated with dual registrants, and the dual registrants themselves, could bear a potentially substantial, one-time costs associated with the proposed rule to change marketing materials and other communications to remove the restricted terms and to explain the change to their customers. Further, some financial professionals using the restricted terms could experience a reduction in the efficiency of their marketing efforts. This could happen to the extent the terms were optimally chosen in the first place from a marketing perspective. This, in turn, might lead to fewer customers for the financial professional and his or her associated firm and a loss of revenue compared to the baseline. Furthermore, financial professionals that are not currently supervised persons of an investment adviser, or

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697 However, as noted previously, all firms and financial professionals can already voluntarily choose to prominently display their registration status, therefore implying that the direct benefits to firms and financial professionals from the proposed rule requiring disclosure of registration status may be limited.

cannot immediately qualify to be hired in such a professional role may become less attractive to retain or hire by dual registrants, to the extent their services would be less valuable to dual registrants if they cannot use the terms "adviser" or "advisor" in their names or titles. These financial professionals could potentially mitigate the costs associated with the potential loss of names or titles by becoming a supervised person of an investment adviser and providing investment advice on behalf of such investment adviser. A financial professional would likely pursue such a strategy only if it expected the costs of becoming a supervised person of an investment adviser who provides investment advice on behalf of such investment adviser were lower than the expected costs of modifying their professional names or titles.

We expect the proposed requirements to prominently disclose registration status to impose one-time direct compliance costs associated with changes to written and electronic retail investor communications on both investment advisers and dually registered financial firms.[698] Similar to standalone registered broker-dealers, we expect that to the extent the required changes have a fixed-cost component, smaller investment adviser firms would incur relatively higher costs associated with this disclosure. Larger investment advisers and dual registrants, however, would likely bear an increase in the variable costs associated with such disclosures, as the amount of revisions associated with individual representative's and firm's communications will rise.[699]

3. Impact on Efficiency, Competition, and Capital Formation

In addition to the specific benefits and costs discussed in the previous section, the

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698 *See infra* Section V.H. for estimates of some of these compliance costs developed for the purpose of the Paperwork Reduction Act.

699 Consistent with this argument, we estimate in the Paperwork Reduction Act analysis in *infra* Section V.H.2, that the initial one-time burden for complying with the disclosure requirements would be 72 hours per large investment adviser and 15 hours per small investment adviser.

Commission expects that the proposed disclosure could cause some broader long-term effects on the market for financial advice. Below, we elaborate on these possible effects, specifically discussing the impact on efficiency, competition and capital formation.

a. Efficiency

As discussed above, the proposed rules have the potential to reduce investor confusion about the meaning of the names and titles used by firms and their financial professionals and to improve the matching between investor preferences and types of services they receive. To the extent retail investors use titles and names in their search for firms and financial professionals, the potential reduction in search costs would improve the overall efficiency of the market for financial advice by making the search process shorter in time and more cost effective. Moreover, to the extent the proposed rules would reduce the risk of any mismatch between investor preferences and the type of relationship their financial professional provides, it could lead to potentially improved efficiency in retail investors' asset allocation as investors would be more likely to receive investment advice that is optimal for their individual situation. A reduced risk of mismatch in the relationship would also make it less likely that investors pay more than necessary for the services they receive, which could lead to higher investment returns net of cost.

Alternatively, as discussed previously, investor confusion may increase rather than decrease under certain circumstances, which would increase search costs for investors. In this case, we would instead expect a negative effect on efficiency. Moreover, there could also be negative effects on efficiency to the extent affected broker-dealers start using new names and titles that potentially convey the same information to investors as the restricted terms. Under such circumstances, the proposed rules would then only impose cost increases on broker-dealers without achieving any reduction of investor confusion. These costs may or may not be passed

through to investors. In addition, some of the other potential costs outlined previously could have negative effects on efficiency. For example, this proposed rule could have a direct negative impact on efficiency in the registered broker-dealer segment of the market by making marketing less efficient for any affected broker-dealers (including any affected dual registrants with affected registered representatives). Further, any compliance costs or increased marketing costs may be passed through to investors in local markets where the competitive pressure is relatively low – for example, due to, a relatively low supply of financial professionals – and some investors may then face higher costs for broker-dealer services as a result. Finally, some affected firms and financial professionals may decide to exit the market if their costs of doing business go up substantially, which could decrease supply and increase costs of brokerage services for retail investors in some segments of the market. Any such increases in costs of broker-dealer services may also price some investors with limited ability to absorb a cost increase out of the brokerage market altogether, thereby limiting their access to advice and investment choices offered by broker-dealers and potentially hurting the efficiency of their investment allocation.

Because of the complexity associated with the use of names or titles by firms and their financial professionals, and their potential importance for investors both with respect to investor confusion and as a selection mechanism for hiring financial professionals, coupled with the lack of data on how investors could react to a restriction of the use of certain names and titles among broker-dealers and their associated natural persons, we are unable to provide estimates for the potential effects on efficiency. However, we preliminarily believe that any potential effects on the overall efficiency in the market for financial advice, or in segments of this market, are likely to be limited because of several factors that would mitigate the potential impact on investor confusion and/or the potential costs imposed on firms and financial professionals from the

proposed restriction: (i) only a fraction of standalone registered broker-dealers and their associated natural persons, as well as registered representatives working for dual registrants that are not dual-hatted are currently using the terms "adviser" and "advisor" in names and titles;[700] (ii) the extent to which the proposed restriction would not affect the use of terms such as "advisory services" in communications which do not convey a name or title; (iii) financial intermediaries and professionals not regulated by the Commission could still use the terms "adviser" or advisor" in their names and titles.[701]

The proposed requirements to disclose a firm's regulatory status and a financial professional's association may increase the efficiency in the search and matching process in the market for financial advice to the extent retail investors understand the meaning of the registration status and would use it in their search for financial professionals. Among firms, the potential efficiency benefits may be larger for dual registrants, as the prominent display of both types of registrations may help attract investors that are looking for both brokerage services and an investment advice relationship, or investors who are in general unsure about which type of services they want.

b. Competition

The proposed rules could affect competition in the market for financial advice through potential effects on both demand and supply in the market. In terms of potential effects on demand, to the extent search costs are reduced for investors, it may raise the price elasticity of demand and consequently we would expect the competition between firms in this market to

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700 The use of names and titles by firms and financial professionals is discussed in Section IV.A.1.f. Only around 87 current standalone broker-dealers with retail investors use the terms "advisor" or "adviser" in their company names. Further, around 31% of professionals providing only brokerage services used titles containing the terms "adviser" or "advisor" according to the RAND Study.

701 *See* discussion of other such financial intermediaries and professionals in *supra* Section III.B.1.

increase.[702] To the extent it is primarily investors who prefer the services provided by investment advisers who would experience a reduction in search costs, we would expect in particular an increase in the average price elasticity of demand for investment adviser services and therefore greater competition in the investment adviser market segment. However, a reduction in search cost may also increase retail investor participation in the market for financial advice. Investors at the high end of the search cost distribution who previously may have refrained from seeking financial advice altogether may enter the market for financial advice if there is a reduction in search costs. Because these new entrants to the market for financial advice would likely have higher search costs than the existing investors in the market, average investor demand elasticity may go down, which in turn would reduce competition at the margin.[703] To the extent it is mainly investors that prefer investment adviser services who would experience a reduction in search costs; we expect the new entrants to primarily belong to this group of investors. Therefore, the average demand elasticity may potentially decrease in particular for investment adviser services and reduce competition in the investment adviser market segment.

Conversely, if investor confusion and associated search costs instead are increased by the proposed rules, which as we discussed previously may happen under certain circumstances, it would likely lower price elasticity of demand among current retail investor market participants

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[702] All else equal, we would expect customers in a marketplace with differentiated products to prolong their search for the right product at the right price if search costs are reduced. The resulting increase in demand elasticity would increase downward pressure on prices in the market, *see, e.g.* S. Anderson & R. Renault, *Pricing, Product Diversity, and Search Costs: A Bertrand-Chamberlin-Diamond Model*, The RAND Journal of Economics, 30, 719-735 (1999).

[703] For a theoretical model on how lower search costs may increase the average price elasticity of demand in this manner, *see, e.g.*, J. L. Moraga-González, Z. Sándor, & M.R. Wildenbeest, *Prices and heterogeneous search costs*, The RAND Journal of Economics, 48, 125–146 (2017). A study of the U.S. mutual fund industry also provide empirical evidence consistent with this type of effect; *see* A. Hortaçsu & C. Syverson, *Product differentiation, search costs, and competition in the mutual fund industry: A case study of S&P 500 Index funds*, The Quarterly Journal of Economics, Vol. 119, Issue 2, 403–456 (May 2004).

and reduce competition in the market for financial advice. However, if search costs are increased to the extent that current investors at the high end of the search cost distribution are induced to exit the market for financial advice altogether, it could instead increase average demand elasticity and increase competition among the firms in this market, as the remaining investors would be those at the lower end of the search cost distribution and consequently would have higher price sensitivity. To the extent it is mainly investors that prefer broker-dealer services who would experience an increase in search costs we expect the investors exiting the market to primarily be such investors. Therefore, the average demand elasticity may potentially increase in particular for broker-dealer adviser services and increase competition in the broker-dealer market segment.

In terms of the effect on the supply of advice services, to the extent the proposed restriction on the use of certain names or titles would cause affected broker-dealers to register as investment advisers and start promoting that side of their business, or perhaps completely move to an investment adviser model, there would likely be a shift in the mix of supply of advice services, where the supply of broker-dealer (and associated registered representative) services could potentially decrease and the supply of investment adviser services could increase. Such a shift in the mix of the supply of advice services could potentially raise brokerage account prices, reduce choice for investors who prefer to pay for execution of trades on a transactional basis, and lower the costs of advisory accounts with investment advisers. However, to the extent some broker-dealers would exit the market for retail investors altogether, the overall supply of advice services could go down and we may see a decrease in competition not only in the market for broker-dealer services but also in the overall market for investment adviser services, assuming that retail investors view broker-dealer and investment adviser services as substitutes for one

another, thereby increasing costs and limiting choices for retail investors. This potential negative effect on competition would be mitigated to the extent other firms (whether other broker-dealers or investment advisers) decide to compete for the customers of any broker-dealers exiting the market.

Further, to the extent the proposed restriction would make standalone broker-dealers services more costly and marketing less effective, non-affected standalone broker-dealers (*i.e.*, broker-dealers that do not use the restricted terms), dual-registrants, investment advisers, and financial intermediaries that are not registered as investment advisers (such as banks, trust companies, insurance companies, commodity trading advisers, and municipal advisors) may to a varying degree gain business at these affected firms expense. That is, by only affecting a subset of firms, the proposed restriction on the use of certain names and titles may change competitive positions among different suppliers in the market for financial advice. In addition, the proposed requirement to disclose registration status may benefit the competitive positon of dual registrants, as the prominent display of both types of registrations may help attract investors that are looking for both brokerage services and an investment advice relationship, or investors who are in general unsure about which type of services they want.

In addition, assuming that small broker-dealers and investment advisers select geographic areas where competition from larger firms is low, then any reduction of competition in the broker-dealer market due to a switch to an investment adviser business model would be particularly large in such geographic areas. Similarly, any reduction in competition due to exit of standalone registered broker-dealer altogether from the retail market would be particularly large in such geographic areas, where smaller investment advisers and dual registrants could especially see competitive benefits at the expense of small standalone registered broker-dealers.

We are not able to assess the magnitude of the potential demand or supply related effects as we do not have access to information that would allow us to do so, such as the distribution of search costs across the population of retail investors, estimates of the effect of the proposed rules on search costs, the internal cost functions of broker-dealers, etc. However, we preliminarily believe that the impact of any effects on the overall competitive situation in the market for financial advice is likely to be limited because of the same three mitigating factors we discussed above regarding the potential impact on efficiency. [704]

c. Capital Formation

Some aspects of the proposed rules could lead to increased capital formation, if, for example, retail investors are better able to allocate capital due to a better match with financial professionals or more retail investors enter the market for financial advice and start investing in securities. However, as discussed above, if some broker-dealers exit the market or move to an advisory business model as a result of the proposed rules, some investors may lose access to the market for advice serviced by broker-dealers, which may cause them to exit the market for financial advice altogether and reduce their (direct or indirect) investments in productive assets, thereby reducing capital formation. Alternatively, any investors who lose access to broker-dealers services may switch to an investment adviser relationship, which could reduce their investment returns net of costs to the extent the broker-dealer payment model was more optimal for their investment preferences, thereby also potentially reducing capital formation. Overall, the Commission is unable to determine how these countervailing effects could impact capital formation, and what the likely magnitude of those impacts would be. However, we preliminarily believe that the proposed rules would have a limited impact on capital formation because of the

[704] *See* discussion of mitigating factors in *supra* Section IV.C.3.a.

same three mitigating factors we discussed above regarding the potential impact on efficiency.[705]

4. Alternatives to the Proposed Rules

As discussed above, the proposed rule would restrict broker-dealers and their associated natural persons from using as part of a name or title the term "adviser" or "advisor," unless such broker-dealer is dually registered as an investment adviser or the associated natural person is a supervised person of an investment adviser and provides advice on behalf of such investment adviser. Further, our proposed rules would also require both broker-dealers and investment advisers to disclose their registration status in print or electronic retail investor communications. Finally, the proposed rules would require associated natural persons of a broker-dealer and supervised persons of an investment adviser to disclose their association with a particular firm in print or electronic retail investor communications. Below, the Commission describes several alternatives to the proposed rules, , including the continued ability of broker-dealers to rely on section 202(a)(11)(C) of the Advisers Act (the "Solely Incidental" exclusion), prohibitions on a broker-dealer "holding out" as an investment adviser, disclosure of the registration status only, or additional requirements for dual registrants.

a. No "Solely Incidental" Exclusion

As an alternative to the proposed rule restricting the use of the term "adviser" or "advisor" in names and titles, the Commission could propose a rule that stated that a broker-dealer cannot be considered to provide investment advice solely incidental to the conduct of its business as a broker-dealer under section 202(a)(11)(C) of the Advisers Act if the broker-dealer used the term "adviser" or "advisor" in names or titles, and therefore, would not be excluded from the definition of investment adviser. This alternative would rely on the assumption that a

[705] *See* discussion of mitigating factors in *supra* Section IV.C.3.a.

broker-dealer that uses these terms in its name to market or promote its services is doing so because its advice is significant or even instrumental to its brokerage business, and consequently, the broker-dealer's provision of advice is therefore no longer solely incidental to its brokerage business. Similarly, it would also rely on the assumption that if a broker-dealer invests its capital into marketing, branding, and creating intellectual property in using the terms "adviser" or "advisor" in its name or title, the broker-dealer is indicating that advice is an important part of its broker-dealer's business.

This alternative, like the proposed rule, would not permit an associated natural person of a dually registered firm to use the terms "adviser" or "advisor" in their names or titles unless such person was a supervised person of a registered investment adviser who provides investment advice on behalf of such investment adviser. For standalone broker-dealers, and their associated natural persons as well as associated natural person of a dually registered firm that are not supervised persons of a registered investment adviser providing advice on behalf of such investment adviser, that are currently marketing their services to retail investors using the terms "adviser" and "advisor," in their name or title, the economic effects of this alternative would be expected to be substantially the same as under the proposed restriction on the use of the terms in names and titles.

b. Prohibit Broker-Dealers from Holding Themselves Out as Investment Advisers

Instead of prohibiting a broker-dealer from using certain names or titles, we could propose a rule to preclude a broker-dealer from relying on the solely incidental exclusion of section 202(a)(11)(C) if a broker-dealer "held itself out" as an investment adviser to retail investors.. This approach could encompass a broker-dealer and its associated natural persons representing or implying through any communication or other sales practice (including through

the use of names or titles) that they are offering investment advice subject to a fiduciary relationship with an investment adviser.

This approach would reduce the risk that by only proscribing "adviser" and "advisor," or any other specific names and titles, new names and titles could arise with similar, confusing connotations. Moreover, this alternative could promote informed investor choices by focusing more comprehensively on broker-dealer marketing and titles that may confuse or mislead investors into believing that a brokerage relationship is an advice relationship of the type provided by investment advisers. Relative to either the baseline or the proposed rule, the "holding out" alternative could have a broader application because it could capture any communication or other sales practices that may lead to confusion by investors in believing that their firms or financial professionals provide more or different services than they provide. As a result, investor confusion and associated costs may be reduced more compared to the proposed rule.

This alternative, however, could create uncertainty for broker-dealers as to which activities (and the extent of such activities) would be permissible and not considered "holding out" as an investment adviser and therefore triggering the need to register as such. As a result of a "holding out" alternative, broker-dealers may feel compelled to avoid fully describing even the types of advisory services they are allowed to provide in their communications and marketing efforts and may also limit or reduce allowable advice provided by broker-dealers to avoid any instances where the advice provided could be misconstrued that such person is "holding out" as an investment adviser. Given that broker-dealers under the current regulatory environment are permitted to provide incidental advice related to recommendations of securities or investment strategies, investor confusion may be increased and some investors may believe that as a result of

the "holding out" alternative that this advice could no longer be offered, and could face a mismatch in their preferences and expectations if they sub-optimally choose to hire investment advisers and avoid broker-dealers. Therefore, implementing a rule along these lines could have significant competitive effects for broker-dealers, and could reduce the effectiveness in how investors choose their firms and financial professionals. As a result of increased investor confusion, both search costs and costs associated with choosing the wrong type of firm and financial professional could be increased under this alternative. Moreover, if some broker-dealers avoid providing advice as a result of this alternative, some retail investors may be shut out of the advice market entirely or may have to incur higher costs that may be associated with investment advisory services.

From a compliance cost perspective, broker-dealers that could be subject to the "holding out" alternative would face costs in revising their communications and advertisements in order to eliminate any discussion about them implying they are offering investment advice subject to a fiduciary relationship with an investment adviser. To the extent such revisions have a significant fixed cost component or there are other economies of scale, such as decreasing variable costs for printed material as the number of copies increase, we would expect smaller broker-dealers to face relatively higher costs following the implementation of this alternative. There could also be increased costs under this alternative from training and monitoring of associated natural persons to ensure compliance with the rule, as the restrictions would be more principles-based than prescriptive compared to the proposed rule.

c. Disclosure of Registration Status Only

The proposed rules both prohibit certain names or titles and require disclosure of broker-dealer or investment adviser registration status in all written and electronic retail investor

communications of broker-dealers and SEC-registered investment advisers, including those of individual representatives, such as business cards, social media profiles, and signature blocks on paper or electronic correspondence. As an alternative to the proposed rules, the Commission could not propose a restriction on the use of certain names or titles by standalone registered broker-dealers, and solely propose requiring disclosure of registration status in all written and electronic retail investor communications given by the firm or its representatives.

Although both broker-dealers and SEC-registered investment advisers would have to bear the cost of including a disclosure of their registration status in all written and electronic retail investor communications under this alternative, they would have to bear this cost under the proposed rules, as well. This alternative, however, would allow broker-dealers to continue to use titles or names that include "Adviser/Advisor" and therefore would likely result in a lower overall cost of rebranding their financial professionals or the firm itself in all other communications.

While the costs of compliance with a disclosure of registration status only requirement would be lower than under the proposed rules, and would apply uniformly to all broker-dealers and investment advisers, this alternative could be less effective in reducing investor confusion over the titles or names used by financial professionals and firms, and the implications of the types of services provided by, or standard of conduct applicable to, these professionals to the extent the registration status is uninformative to retail investors because they do not understand the regulatory implications of a firm being registered as either a broker-dealer or an investment adviser.

Another potential, related, alternative would be to limit the disclosure of registration status only to certain marketing communications. The overall compliance costs to broker-

dealers, particularly small broker-dealers that are less likely to produce advertising campaigns in either print media, television/radio broadcasts, mass mailings, or on websites, would be lower than under the requirements of the proposed rules for disclosure of registration status in all communications. This alternative, however, would likely reduce the potential benefits to retail investors, as only "advertisements" would be required to produce the disclosure of registration status, and could increase both search costs and the possibility of mismatch associated with choosing the wrong type of financial firm or professional. To the extent small broker-dealers or investment advisers are less likely to use these types of marketing communications to reach potential customers relative to larger broker-dealers and investment advisers (*e.g.*, because there are fixed costs in producing an advertisement, the reduction in benefits is more likely to affect retail investors that use such small broker-dealers or investment advisers). Therefore, the Commission preliminarily believes that the potential compliance cost savings for limiting communications that would require such disclosure do not justify the reduced level of investor protection under such alternative.

Another "disclosure only" alternative to the proposed restriction on the use of the terms "adviser" and "advisor" in names and titles would be to propose a rule that would provide that when any broker-dealer not registered under the Advisers Act chooses to distribute advertisements or other communications using the term "adviser" or "advisor" as part of a name or title, each use of the term would have to include an asterisked disclaimer clarifying its registration status. Under this alternative broker-dealers and their associated natural persons could continue to use these terms in their names and titles in retail investor communications, but investors would be potentially alerted by the asterisk to the actual registration status of the broker-dealer, which may reduce investors confusion about the type of services provided the

associated standard of care to the extent they understand the meaning of the registration status. One limitation of this alternative, as well as the other alternatives discussed in this section, compared to the proposed rule is that some of the evidence on investor perceptions discussed previously in Section IV.A.3 suggest that many retail investors may not fully understand the meaning of the registration status. Moreover, the asterisked declaimer may not be salient enough to attract investors' attention to the disclaimer.

d. Additional Requirements for Dual Registrants

We estimate that the number of dual registrants represents approximately 13% of all retail broker-dealer firms and that approximately 65% of registered representatives of retail broker-dealers work at these dual registrants.[706] Although the proposed rule restricts supervised persons of dual registrants who do not provide investment advice on behalf of such investment adviser, a percentage of dually registered firms would not be affected by the proposed restriction of certain names and titles. To address this issue, we considered an alternative to the proposed rule which would prohibit the name or title containing the terms "adviser" or "advisor" unless a "a substantial part of the business consists of rendering investment supervisory services."[707] We also considered limiting dual registrants' use of the term "adviser" or "advisor" to when they provide advice to a retail investor in the capacity as an investment adviser, and prohibiting dual

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706 As shown in *supra* Table 1, Panel B those broker-dealer firms that were registered in a dual capacity were 360 of approximately 2,857 firms (about 13%) as of December 31, 2017. Using data from Form ADV filings, these 360 dually-registered firms had approximately $4.3 trillion of AUM. As discussed in Section IV.A,1.e, almost all registered financial professionals at dual registrants are either dual-hatted or registered representatives. Because dual registrants employ approximately 61% of all licensed financial professionals (see *supra* Table 5) and approximately 94% of all financial professionals are either dual hatted or registered representatives (48/51 = 0.94; *see supra* Table 6), it means that approximately 65% (0.61/0.94 = 0.65) of all registered representatives, whether dual hatted or not, work at dual registrants.

707 *See* section 208(c) of the Advisers Act.

registrants from using such terms when acting in the capacity of a broker-dealer to a particular customer.

Under this alternative, some of the investor pool may face reduced confusion in their communications with their financial professional with regard to the use of specific names and titles, because these names and titles containing the term "adviser" or "advisor" would be limited only to the accounts or the instances in which the financial professional actually serves in the capacity as an investment adviser. However, these alternatives for dual registrants would create substantial compliance challenges for dual registrants. For example, dual registrants would have to ensure the appropriate name or title is being used when the financial professional is engaging in multiple capacities with investors. Moreover, requiring financial professionals that are dual registrants to tailor their names or titles based on what capacity they are acting in could increase confusion to investors, given that some dual registrants might act in broker-dealer and investment adviser capacities for a single investor. For example, a retail investor may have both a brokerage account and an advisory account, and may receive advice related to both brokerage recommendations as well as ongoing advice in the advisory account in a single communication.

5. Request for Comments

The Commission requests comment on all aspects of the economic analysis, including the analysis of: (i) potential benefits and costs and other economic effects; (ii) long-term effects of the proposed restriction on the use of certain titles and required disclosure of registration status on efficiency, competition, and capital formation; and (iii) reasonable alternatives to the proposed regulations. We also request comments identifying sources of data and that could assist us in analyzing the economic consequences of the proposed regulations.

In addition to our general request for comment on the economic analysis, we request specific comment on certain aspects of the proposal:

- Do commenters agree with our assessment that the main potential benefits to retail investors are reduced search costs and a lower risk of mismatch? Are there other benefits of the proposed rule that have not been identified in our discussion and that warrant consideration? Are the assumptions that form the basis of our analysis of the benefits appropriate? Can commenters provide data that supports or opposes these assumptions?
- Do commenters agree with our characterization of the costs? Are the assumptions that form the basis of our analysis of the costs appropriate? Are there other costs to investors of the proposed rule that have not been identified in our discussion and that warrant consideration? Can commenters provide data that supports or opposes these assumptions?
- We request additional information on how retail investors search for financial professionals. In particular, are there studies, evidence or data available on how investors use company names and titles of representatives in their search for a financial professional?
- We request comments on our characterization of the benefits and costs to broker-dealers and investment advisers of the proposed rule. Do commenters agree with our characterization of the benefits and costs? Are there other benefits or costs of the proposed rule that have not been identified in our discussion and that warrant consideration? Are the assumptions that form the basis of our analysis of the benefits and costs appropriate? Can commenters provide data that supports or opposes these assumptions?

- We specifically request comments on the costs to broker-dealers from having to change their company names as a result of the rule. How costly do commenters believe it would be for affected entities that would be required to their change current company names, including the costs of marketing materials and advertisements? Do broker-dealer company names have significant brand value? To what extent does the brand value lie in terms such as "adviser" or "advisor"?
- Do commenters believe standalone broker-dealers that would be affected by the proposed rule may decide to register as an investment advisers? Are there any specific types of standalone broker-dealers that would be more likely to respond in this way? Do you believe standalone broker-dealers registering as investment advisers would affect their supply of brokerage services? What are the compliance and indirect costs for broker-dealers who would seek to register as an investment adviser? Is there additional data to estimate such costs, either initially or on an ongoing basis?
- Are there any effects on efficiency, competition, and capital formation that are not identified or are misidentified in our economic analysis? Please be specific and provide data and analysis to support your views.
- Do commenters believe that the alternatives the Commission considered are appropriate? Are there other reasonable alternatives that the Commission should consider? If so, please provide additional alternatives and how their costs and benefits would compare to the proposal.

D. Combined Economic Effects of Form CRS Relationship Summary and Restrictions on the Use of Certain Titles and Required Disclosures about a Firm's Regulatory Status

Above, we have described the anticipated standalone economic effects of the proposed Form CRS relationship summary and the proposed restrictions on the use of certain titles and required disclosures about a firm's regulatory status relative to the current baseline. In this section, we discuss how we anticipate these economic effects could change when considering both these proposed rules in combination.

To the extent that investors may be confused and potentially misled about what type of investment advice relationship is best for their investing situation, being provided with the proposed Form CRS, along with the proposed restriction on names and titles, could incrementally reduce some of the investor confusion and mismatch risk. In particular, if a retail investor communicates with a financial professional associated with a dual registrant and the professional has a name or title containing either of the terms "adviser" or "advisor" but solely provides brokerage services, such investor would likely receive the dually registered firm's relationship summary. Because Form CRS would include a description of both business models, without the restriction on names and titles and the requirement of disclosure of registration status, some retail investors might incorrectly match the services they would receive from this financial professional to the description in the relationship summary of *investment advisory* services. In this case, the proposed restriction on names or titles and the requirement to disclose regulatory status would increase the effectiveness of Form CRS by reducing the risk of any mismatch between investor preferences and type of services received due to this kind of misunderstanding, which in turn may lead to harm such as the investor paying too much for advice if it if it leads to frequent trading. To the extent investors who received a relationship summary shares it with family and friends, the potential importance of having the restriction on

the use of certain names and titles would be increased, because it could also reduce the risk of this type of misunderstanding being spread to a greater set of retail investors.

However, for those investors whose confusion about the differences between broker-dealers' and investment advisers' services and standards of conduct would be substantially reduced once receiving and reading a firm's relationship summary we expect a reduced overall incremental benefit of the proposed restriction on the use of certain names and titles. Specifically, because such investors would learn about the differences between broker-dealer and investment adviser services through the relationship summary, they may be unlikely to hire the wrong type of firm or financial professional even without the proposed restriction on the use of certain names or titles.

With respect to the initial search costs borne by investors, we do not believe that the relationship summary would alter the incremental effects the proposed restriction on certain names and titles may have on search costs, because the proposed Form CRS would generally be provided at a later stage in the search process (e.g., after initial contact with a financial professional is made) relative to the initial stage where names and titles of firms and financial professionals may be a useful search tool to investors. Similarly, we do not believe that the relationship summary would alter the incremental effects on search costs from the proposed requirement to disclose registration status in retail investor communications, because investors would likely encounter communications disclosing a firm's registration status prior to being provided a firm's relationship summary.

We believe that the proposed Form CRS and the proposed required disclosures of registration status would complement each other because both are designed to reduce investor confusion. In particular, for less knowledgeable investors, the disclosure of registration status

may raise awareness about the different forms of registration among financial intermediaries and their associated natural persons and prompt questions about the difference between registered broker-dealers and registered investment advisers. The relationship summary potentially could work in concert with the disclosure of registration status to facilitate investors' learning about the different types of financial firms and professionals because it would highlight many of the key differences between investment advisers and broker-dealers in different communications and different times, consistent with the layered approach to disclosure that the relationship summary is designed to further. Likewise, if the disclosure of registration status makes such status more salient to less knowledgeable investors, such disclosure may induce a more careful reading of related parts in the relationship summary or provide incentives to discuss the information contained in disclosure with a financial professional. Thus, the combination of the disclosure of registration status and the relationship summary may further help facilitate the search process also for investors initially confused about the difference between broker-dealers and investment advisers, and help them ultimately better match to an appropriate financial professional.

However, for more knowledgeable investors, there may be some overlap in function that could reduce the potential benefits to either the relationship summary or the disclosure of regulatory status without offsetting anticipated costs. As discussed previously, the disclosure of registration status may help to reduce search costs for investors who already understand the meaning of the registration status. These relatively knowledgeable investors may therefore already be familiar with some of the information in relationship summary by having encountered the disclosure of the registration status beforehand. In this case, the relationship summary may provide fewer additional benefits for these investors in either reducing search costs or the

likelihood of mismatch, but would impose costs on both broker-dealers and investment advisers that must produce both the relationship summary and the disclosures of registration status.

Finally, we note that any complementarities between the proposed restrictions on the use of certain names and titles, required disclosures about a firm's regulatory status, and the proposed relationship summary would be constrained by the fact (1) the relationship summary does not need to be provided by state-registered standalone investment advisers and (2) these state-registered investment advisers (and their supervised persons) would not be required to provide registration status disclosures in retail investor communications pursuant to this proposed rule.

V. PAPERWORK REDUCTION ACT ANALYSIS

Certain provisions of our proposal contain "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").[708] The Commission is submitting these collections of information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The titles for the existing collections of information that we are proposing to amend are (i) "Form ADV" (OMB control number 3235-0049), (ii) "Rule 204-2 under the Investment Advisers Act of 1940" (OMB control number 3235-0278), (iii) "Rule 17a-3; Records to be Made by Certain Exchange Members, Brokers and Dealers" (OMB control number 3235-0033) and (iv) "Rule 17a-4; Records to be Preserved by Certain Exchange Members, Brokers and Dealers" (OMB control number 3235-0279). The new collections of information relate to (i) "Rule 204-5 under the Investment Advisers Act of 1940," (ii) "Form CRS and rule 17a-14 under the Exchange Act," (iii) "Rule 15l-3 under the Securities Exchange Act," and (iv) "Rule 211h-1 under the Investment Advisers

[708] 44 U.S.C. 3501 *et seq.*

Act of 1940." An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number. The Commission is also including a short-form tear sheet for investors to provide feedback on the relationship summary.[709]

A. Form ADV

Form ADV (OMB Control No. 3235-0049) is currently a two-part investment adviser registration form. Part 1 of Form ADV contains information used primarily by Commission staff, and Part 2 is the client brochure. We are not proposing amendments to Part 1 or 2. We use the information to determine eligibility for registration with us and to manage our regulatory and examination programs. Clients use certain of the information to determine whether to hire or retain an investment adviser. The collection of information is necessary to provide advisory clients, prospective clients and the Commission with information about the investment adviser and its business, conflicts of interest and personnel. Rule 203-1 under the Advisers Act requires every person applying for investment adviser registration with the Commission to file Form ADV. Rule 204-4 under the Advisers Act requires certain investment advisers exempt from registration with the Commission ("exempt reporting advisers") to file reports with the Commission by completing a limited number of items on Form ADV. Rule 204-1 under the Advisers Act requires each registered and exempt reporting adviser to file amendments to Form ADV at least annually, and requires advisers to submit electronic filings through IARD. The paperwork burdens associated with rules 203-1, 204-1, and 204-4 are included in the approved annual burden associated with Form ADV and thus do not entail separate collections of

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709 *See* Appendix F. The Commission determines that using this short-form tear sheet to obtain information from investors is in the public interest and will protect investors. *See* Securities Act section 19(e).

information. These collections of information are found at 17 CFR 275.203-1, 275.204-1, 275.204-4 and 279.1 (Form ADV itself) and are mandatory. Responses are not kept confidential.

We are proposing to amend Form ADV to add a new Part 3, requiring certain registered investment advisers to prepare and file a relationship summary for retail investors. As with Form ADV Parts 1 and 2, we will use the information to determine eligibility for registration with us and to manage our regulatory and examination programs. Similarly, clients can use the information required in Part 3 to determine whether to hire or retain an investment adviser, as well as what types of accounts and services are appropriate for their needs. The collection of information is necessary to provide advisory clients, prospective clients and the Commission with information about the investment adviser and its business, conflicts of interest and personnel. The proposal requiring investment advisers to deliver the relationship summary is contained in a new collection of information under proposed new rule 204-5 under the Advisers Act, which estimates are discussed in Section V.B below. We are not proposing amendments to Part 1 or 2 of Form ADV.[710]

1. Respondents: Investment Advisers and Exempt Reporting Advisers

The respondents to current Form ADV are investment advisers registered with the Commission or applying for registration with the Commission and exempt reporting advisers.[711]

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[710] We are proposing conforming technical amendments to the General Instructions of Form ADV to add references to the Part 3, but these amendments would not affect the burden of Part 1 or Part 2. *See* proposed amendments to Form ADV: General Instructions.

[711] An exempt reporting adviser is an investment adviser that relies on the exemption from investment adviser registration provided in either section 203(l) of the Advisers Act because it is an adviser solely to one or more venture capital funds or 203(m) of the Advisers Act because it is an adviser solely to private funds and has assets under management in the United States of less than $150 million. An exempt reporting adviser is not a registered investment adviser and therefore would not be subject to the relationship summary requirements.

As of December 31, 2017, 12,721 investment advisers were registered with the Commission, and 3,848 exempt reporting advisers report information to the Commission.

As discussed in Section II above, we propose to adopt amendments to Form ADV that would add a new Part 3, requiring certain registered investment advisers to prepare and file a relationship summary for retail investors. Only those registered investment advisers offering services to retail investors would be required to prepare and file a relationship summary. Based on IARD system data, the Commission estimates that 7,625 investment advisers provide advice to individual high net worth and individual non-high net worth clients.[712]

This would leave 5,096 registered investment advisers that do not provide advice to retail investors[713] and 3,848 exempt reporting advisers that would not be subject to Form ADV Part 3 requirements, but are included in the PRA analysis for purposes of updating the overall Form ADV information collection.[714] We also note that these figures include the burdens for 366 registered broker-dealers that are dually registered as investment advisers as of December 31, 2017.[715]

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712 Based on responses to Item 5.D. of Form ADV. These advisers indicated that they advise either high net worth individuals or individuals (other than high net worth individuals), which includes trusts, estates, and 401(k) plans and IRAs of individuals and their family members, but does not include businesses organized as sole proprietorships. The proposed definition of retail investor would include a trust or other similar entity that represents natural persons, even if another person is a trustee or managing agent of the trust. We are not able to determine, based on responses to Form ADV, exactly how many advisers provide investment advice to these types of trusts or other entities; however, we believe that these advisers most likely also advise individuals and are therefore included in our estimate.

713 12,721 registered investment advisers – 7,625 = 5,096 registered investment advisers not providing advice to retail investors.

714 Based on IARD system data.

715 *See supra* note 457.

2. Changes in Burden Estimates and New Burden Estimates

Based on the prior revision of Form ADV,[716] the currently approved total aggregate annual hour burden estimate for all advisers of completing, amending and filing Form ADV (Part 1 and Part 2) with the Commission is 363,082 hours, or a blended average of 23.77 hours per adviser,[717] with a monetized total of $92,404,369, or $6,051 per adviser.[718] The currently approved annual cost burden is $13,683,500. This burden estimate is based on: (i) the total annual collection of information burden for SEC-registered advisers to file and complete Form ADV (Part 1 and Part 2); and (ii) the total annual collection of information burden for exempt reporting advisers to file and complete the required items of Part 1A of Form ADV. Broken down by adviser type, the current approved total annual hour burden is 29.22 hours per SEC-registered adviser, and 3.60 hours per exempt reporting adviser.[719] The proposed amendments would increase the current burden estimate due in part to the proposed amendments to Form ADV to add Form ADV Part 3: Form CRS (the relationship summary) and the increased number of investment advisers and exempt reporting advisers since the last burden estimate. We are not proposing any changes to Part 1 or Part 2 of Form ADV.

The proposed amendments to Form ADV to add Part 3 would increase the information collection burden for registered investment advisers with retail investors. As discussed above in Section II, we propose to adopt amendments to Form ADV, under Part 3, that would require certain registered investment advisers to prepare and file a relationship summary for retail investors. Only those registered investment advisers providing services to retail investors would

716 *See* Form ADV and Investment Advisers Act Rules, Final Rule, Investment Advisers Act Release No. 4509 (Aug. 25, 2016) [81 FR 60418 (Sep. 1, 2016)] ("2016 Form ADV Paperwork Reduction Analysis").

717 363,082 hours / (12,024 registered advisers + 3,248 exempt reporting advisers) = 23.77 hours.

718 $92,404,369 hours / (12,024 registered advisers + 3,248 exempt reporting advisers) = $6,051.

719 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR 60454.

be required to prepare and file a relationship summary. We propose to require that those investment advisers file their relationship summaries with the Commission electronically through IARD in the same manner as they currently file Form ADV Parts 1 and 2. Investment advisers also would need to amend and file an updated relationship summary within 30 days whenever any information becomes materially inaccurate.

As noted in Section V.A.1 above, not all investment advisers would be required to prepare and file the relationship summary. For those investment advisers, the per adviser annual hour burden for meeting their Form ADV requirements would remain the same, in particular, 29.22 hours per registered investment adviser without relationship summary obligations. Similarly, because exempt reporting advisers also would not have relationship summary obligations, the annual hour burden for exempt reporting advisers to meet their Form ADV obligations would remain the same, at 3.60 hours per exempt reporting adviser. However, although we are not proposing changes to Form ADV Part 1 and Part 2, and the per adviser information collection burden would not increase for those without the obligation to prepare and file the relationship summary, the information collection burden attributable to Parts 1 and 2 of Form ADV would increase due to an increase in the number of registered investment advisers and exempt reporting advisers since the last information collection burden estimate. In this section, we discuss the increase in burden for Form ADV overall attributable to the proposed amendments, *i.e.*, new Form ADV Part 3: Form CRS, and the increase due to the updated number of respondents that would not be subject to the proposed amendments.

a. Initial Preparation and Filing of Relationship Summary

For investment advisers that provide advice to retail investors, we estimate that the initial first year burden for preparing and filing the relationship summary would be five hours per

registered adviser. As discussed above, much of the language of the proposed relationship summary is prescribed. Furthermore, much of the information proposed to be required in the relationship summary overlaps with that required by Form ADV Part 2 and therefore should be readily available to registered investment advisers because of their existing disclosure obligations. Investment advisers also already file the Form ADV Part 2 brochure on IARD, and we have considered this factor in determining our estimate of the additional burden to file Form ADV Part 3: Form CRS. In addition, the narrative descriptions required in the relationship summary should be narrowly tailored and brief, and the relationship summary must be limited to four pages (or equivalent limit if in electronic format). Thus, while we recognize that different firms may require different amounts of time to prepare the relationship summary, we believe that this is an appropriate average number for estimating an aggregate amount for the industry for purposes of the PRA analysis. Moreover, a considerable amount of language within each topic area also would be prescribed, thereby limiting the amount of time required to prepare the relationship summary. Based on these factors, we believe that the estimate of five hours to prepare and file the relationship summary is appropriate. We therefore estimate that the total burden of preparing and filing the relationship summary would be 38,125 hours.[720] As with the Commission's prior Paperwork Reduction Act estimates for Form ADV, we believe that most of the paperwork burden would be incurred in advisers' initial preparation and submission of Part 3: Form CRS, and that over time this burden would decrease substantially because the paperwork burden would be limited to updating information.[721] As under the currently approved collection, the estimated initial burden associated with preparing the relationship summary would be

[720] 5.0 hours x 7,625 investment advisers = 38,125 total aggregate initial hours.

[721] We discuss the burden for advisers making annual updating amendments to Form ADV in Section V.A.3 below.

amortized over the estimated period that advisers would use the relationship summary, *i.e.*, over a three-year period.[722] The annual hour burden of preparing and filing the relationship summary would therefore be 12,708.[723] In addition, based on IARD system data, the Commission assumes that 1,000 new investment advisers will file Form ADV with us annually. Of these, we estimate that 477 would be required to prepare and file the relationship summary.[724] Therefore, the aggregate initial burden for newly registered advisers to prepare the relationship summary would be 2,385[725] and, amortized over three years, 795 on an annual basis.[726] In sum, the annual hour burden for existing and newly registered investment advisers to prepare and file a relationship summary would be 13,503 hours,[727] or 1.67 hours per adviser.[728]

b. Estimated External Costs for Investment Advisers Preparing the Relationship Summary

The currently approved total annual collection of information burden estimate for Form ADV anticipates that there will be external costs, including (i) a one-time initial cost for outside legal and compliance consulting fees in connection with the initial preparation of Part 2 of Form ADV, and (ii) the cost for investment advisers to private funds to report the fair value of their private fund assets.[729] We do not anticipate that the amendments we are proposing today will

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722 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716.

723 5.0 hours x 7,625 investment advisers / 3 = 12,708 total annual aggregate hours.

724 The number of new investment advisers is calculated by looking at the number of new advisers in 2016 and 2017 and then determining the number each year that serviced retail investors. (455 for 2016 + 499 for 2017) / 2 = 477.

725 477 new RIAs required to prepare relationship summary x 5.0 hours = 2,385 hours for new RIAs to prepare relationship summary.

726 477 x 5.0 hours / 3 = 795.

727 (38,125 + 2,385) / 3 years = 13,503 annual hour burden for existing and new advisers to prepare and file relationship summary.

728 13, 503 hours / (7,625 existing advisers + 477 new advisers) = 1.67 hours per year.

729 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR 60452. We do not anticipate that the amendments we are proposing to add Form ADV Part 3 will affect those per adviser cost

affect the per adviser cost burden for those existing requirements but anticipate that some advisers may incur a one-time initial incremental cost for outside legal and consulting fees in connection with the initial preparation of the relationship summary. We do not anticipate external costs to investment advisers in the form of website set-up, maintenance, or licensing fees because they would not be required to establish a website for the sole purpose of posting their relationship summary if they do not already have a website. We also do not expect other ongoing external costs for the relationship summary. Although advisers would be required to amend the relationship summary within 30 days whenever any information becomes materially inaccurate, given the standardized nature and prescribed language of the relationship summary, we expect that amendments would be factual and require relatively minimal wording changes. We believe that the investment adviser would be more knowledgeable about these facts than outside legal or compliance consultants and would be able to make these revisions in-house. Therefore, we do not expect that investment advisers will need to incur ongoing external costs for the preparation and review of relationship summary amendments. Although advisers that would be subject to the relationship summary requirement may vary widely in terms of the size, complexity and nature of their advisory business, we believe that the amount of disclosure required would not vary substantially among advisers. Accordingly, we believe that the amount of time, and thus cost, required for outside legal and compliance review is unlikely to vary substantially among those advisers who elect to obtain outside assistance.[730]

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burden estimates for outside legal and compliance consulting fees. The estimated external costs of outside legal and consulting services for the relationship summary are in addition to the estimated hour burden discussed above.

730 We estimate that an external service provider would spend 3 hours helping an adviser prepare an initial relationship summary. In estimating the external cost for the initial preparation of Form ADV Part 2, we estimated that small, medium, and large advisers would require 8, 11, and 26 hours of outside assistance, respectively, to prepare Form ADV Part 2. In comparison, as discussed above, the relationship summary is

Most of the information proposed to be required in the relationship summary is readily available to investment advisers from Form ADV Part 2, and the narrative descriptions are narrowly tailored and brief or prescribed. As a result, we anticipate that a quarter of advisers will seek the help of outside legal services and half will seek the help of compliance consulting services in connection with the initial preparation of the relationship summary. We estimate that the initial per existing adviser cost for legal services related to the preparation of the relationship summary would be $1,416.[731] We estimate that the initial per existing adviser cost for compliance consulting services related to the preparation of the relationship summary would be $2,109.[732] Thus, the incremental external cost burden for existing investment advisers is estimated to be $10,739,813, or $3,579,938 annually when amortized over a three-year period.[733] In addition, we assume that 1,000 new advisers will register with us annually, 477 of which would be required to prepare a relationship summary. For these 477 new advisers, we estimate

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limited to four pages in length (or equivalent limit if in electronic format) and is standardized across investment advisers in terms of the mandated selection and sequence of topic areas. While we recognize that different firms may require different amounts of external assistance in preparing the relationship summary, we believe that this is an appropriate average number for estimating an aggregate amount for the industry purposes of the PRA analysis. *See* Brochure Adopting Release, *supra* note 157, at 75 FR at 49257.

731 External legal fees are in addition to the projected hour per adviser burden discussed above. $472 per hour for legal services x 3 hours per adviser = $1,416. The hourly cost estimate of $472 is based on an inflation-adjusted figure and our consultation with advisers and law firms who regularly assist them in compliance matters.

732 External compliance consulting fees are in addition to the projected hour per adviser burden discussed above. Data from the SIFMA Management and Professional Earnings Report, modified to account for an 1,800-hour work year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead, and adjusted for inflation ("SIFMA Management and Professional Earnings Report"), suggest that outside management consulting services cost approximately $703 per hour. $703 per hour for outside consulting services x 3 hours per adviser = $2,109.

733 25% x 7,625 existing advisers x $1,416 for legal services = $2,699,250 for legal services. 50% x 7,625 existing advisers x $2,109 for compliance consulting services = $8,040,563. $2,699,250 + $8,040,563 = $10,739,813 in external legal and compliance consulting costs for existing advisers. $10,739,813 / 3 = $3,579,938 annually.

that they will require $671,855 in external costs to prepare the relationship summary.[734] In summary, the annual external legal and compliance consulting cost for existing and new advisers relating to relationship summary obligations is estimated to total $4,251,792, or $525 per adviser.[735]

c. Amendments to the Relationship Summary and Filing of Amendments

The current approved information collection burden for Form ADV also includes the hour burden associated with annual and other amendments to Form ADV, among other requirements. We anticipate that the proposed relationship summary would increase the annual burden associated with Form ADV by 0.5 hours[736] due to amendments to the relationship summary,[737] for those advisers required to prepare and file a relationship summary. We do not expect amendments to be frequent, but based on the historical frequency of amendments made on Form ADV Parts 1 and 2, estimate that on average, each adviser preparing a relationship summary will likely amend the disclosure an average of 1.80 times per year.[738] The collection of information burden of 0.5 hours for amendments to the relationship summary would include filing it. Based on the number of other-than-annual amendments filed by investment advisers

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734 25% x 477 new advisers x $1,416 for legal services = $168,858. 50% x 477 new advisers x $2,109 for compliance consulting services = $502,997. $168,858 + $502,997 = $671,855 annually in external legal and compliance consulting costs for newly registered advisers.

735 $3,579,938 in external legal and compliance consulting costs for existing advisers + $671,855 for new advisers = $4,251,792 annually for existing and new advisers. $4,251,792 / ($7,625 existing advisers + 477 new advisers) = $525 per adviser.

736 We have previously estimated that investment advisers would incur 0.5 hours to prepare an interim (other-than-annual) amendment to Form ADV. *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR at 60452. We believe that an amendment to the relationship summary would take a similar amount of time, if not less.

737 Similarly, we estimated that 0.5 hours would be required for interim updating amendments to Form ADV Part 2. *See* Brochure Adopting Release, *supra* note 157, at 75 FR at 49257.

738 This estimate is based on IARD system data regarding the number of filings of Form ADV amendments.

with retail investors last year, we estimate that advisers will file an estimated total of 1.80[739] relationship summary amendments per year for an estimated total paperwork burden of 6,878 hours per year.[740]

d. Incremental Increase to Form ADV Hourly and External Cost Burdens Attributable to Proposed Amendments

For existing and newly-registered advisers with relationship summary obligations, the additional burden attributable to amendments to Form ADV to add Part 3: Form CRS, (including the initial preparation and filing of the relationship summary and amendments thereto) totals 20,381 hours,[741] or 2.52 hours per adviser,[742] and a monetized cost of $5,248,193, or $648 per adviser.[743] The incremental external legal and compliance cost is estimated to be $4,251,792.[744]

3. Total Revised Burden Estimates for Form ADV

a. Revised Hourly and Monetized Value of Hourly Burdens

As discussed above, the currently approved total aggregate annual hour burden for all registered advisers completing, amending, and filing Form ADV (Part 1 and Part 2) with the

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739 Based on IARD data, 7,625 investment advisers with retail clients filed 13,756 other-than-annual amendments to Form ADV. 13,756 other-than-annual amendments / 7,625 investment advisers = 1.80 amendments per investment adviser.

740 7,625 investment advisers amending relationship summaries x 1.80 amendments per year x 0.5 hours = 6,878 hours.

741 13,503 hours for initial preparation and filing of the relationship summary + 6,878 hours for amendments to the relationship summary = 20,381 total aggregate annual hour burden attributable to the Form ADV amendments to add Part 3: Form CRS.

742 20,381 hours / (7,625 existing advisers + 477 newly registered advisers) = 2.52 hours per adviser.

743 20,381 total aggregate annual hour burden for preparing and filing a relationship summary. We expect that performance of this function will most likely be equally allocated between a senior compliance examiner and a compliance manager. Data from the SIFMA Management and Professional Earnings Report suggest that costs for these positions are $229 and $298 per hour, respectively. 20,381 hours x 0.5 x $229 = $2,211,375. 20,381 hours x 0.5 x $298 = $3,036,819. $2,211,375 + $3,036,819 = $5,248,193. $5,248,193 / (7,625 existing registered advisers + 477 newly registered advisers) = $648 per adviser.

744 *See supra* note 735.

Commission is 363,082 hours, or a blended average per adviser burden of 23.77 hours, with a monetized cost of $92,404,369, or $6,051 per adviser. This includes the total annual hour burden for registered advisers of 351,386 hours, or 29.22 hours per registered adviser, and 11,696 hours for exempt reporting advisers, or 3.60 hours per exempt reporting adviser. For purposes of updating the total information collection based on the proposed amendments to Form ADV, we consider three categories of respondents, as noted above: (i) existing and newly-registered advisers preparing and filing a relationship summary, (ii) registered advisers with no obligation to prepare and file a relationship summary, and (iii) exempt reporting advisers.

For existing and newly-registered advisers preparing and filing a relationship summary, including amendments to the disclosure, the total annual collection of information burden for preparing all of Form ADV, updated to reflect the proposed amendments to Form ADV, equals 31.74 hours per adviser, with 2.52 hours attributable to the proposed amendments.[745] On an aggregate basis, this totals 257,122 hours for existing and newly registered advisers, with a monetized value of $66,208,857.[746]

As noted above, we estimate 5,096, or approximately 40% of existing registered advisers, would not have retail investors; therefore, they would not be obligated to prepare and file relationship summaries, so their annual per adviser hour burden would remain unchanged.[747] To

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745 29.22 hours + 2.52 hours for increase in burden attributable to initial preparation and filing of, and amendments to, relationship summary = 31.74 hours total.

746 31.74 hours x 7,625 existing RIAs required to prepare a relationship summary + 477 newly registered RIAs required to prepare a relationship summary = 257,122 total aggregate annual hour burden for preparing, filing and amending a relationship summary. We expect that performance of this function will most likely be equally allocated between a senior compliance examiner and a compliance manager. Data from the SIFMA Management and Professional Earnings Report suggest that costs for these positions are $229 and $298 per hour, respectively. 257,122 hours x 0.5 x $229 = $27,897,712. 257,122 hours x 0.5 $298 = $38,311,144. $27,897,712 + $38,311,144 = $66,208,857.

747 12,721 registered investment advisers – 7,625 registered investment advisers with retail investors = 5,096 registered investment advisers without retail investors.

that end, using the currently approved total annual hour estimate of 29.22 hours per registered investment adviser to prepare and amend Form ADV, we estimate that the updated annual hourly burden for all existing and newly-registered investment advisers not required to prepare a relationship summary would be 164,187,[748] with a monetized value of $43,263,322.[749] The revised total annual collection of information burden for exempt reporting advisers, using the currently approved estimate of 3.60 hours per exempt reporting adviser, would be 15,653 hours,[750] for a monetized cost of $4,124,513, or $949 per exempt reporting adviser.[751]

In summary, factoring in the proposed amendments to Form ADV to add Part 3, the revised aggregate burden for Form ADV for all registered advisers and exempt reporting advisers would be 436,962,[752] for a monetized cost of $115,139,422.[753] This results in a blended average per adviser burden for Form ADV of 26.37 hours[754] and $6,949 per adviser.[755] This is an

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748 29.22 hours x (5,096 existing and 523 newly-registered investment advisers without retail investors) = approximately 164,187 total annual hour burden for RIAs not preparing a relationship summary.

749 We expect that performance of this function for registered advisers will most likely be equally allocated between a senior compliance examiner and a compliance manager. Data from the 2018 SIFMA Management and Professional Earnings Report suggest that costs for these positions are $229 and $298 per hour, respectively. 164,187 hours x 0.5 x $229 = $18,799,432. 164,187 hours x 0.5 x $298 = $24,463,890. $18,799,432 + $24,463,890 = $43,263,322.

750 3.60 hours x 3,848 exempt reporting advisers currently + 500 new exempt reporting advisers = 15,653 hours.

751 As with preparation of the Form ADV for registered advisers, we expect that performance of this function for exempt reporting advisers will most likely be equally allocated between a senior compliance examiner and a compliance manager. Data from the 2018 SIFMA Management and Professional Earnings Report suggest that costs for these positions are $229 and $298 per hour, respectively. 15,653 hours x 0.5 x $229 = $1,792,246. 15,653 hours x 0.5 x $298 = $2,322,267. $1,792,246 + $2,322,267 = $4,124,513. $4,124,513 / (3,848 exempt reporting advisers currently + 500 new exempt reporting advisers) = $949 per exempt reporting adviser.

752 257,122 annual hour burden for RIAs preparing relationship summary + 164,187 annual hour burden for RIAs not preparing relationship summary + 15,653 annual hour burden for exempt reporting advisers = 436,962 total updated Form ADV annual hour burden.

753 $66,208,857 for RIAs preparing relationship summary + $43,263,890 for RIAs not preparing relationship summary + $4,124,513 for exempt reporting advisers = $115,139,422 total updated Form ADV annual monetized hourly burden.

754 436,962 / (12,721 registered investment advisers + 3,843 exempt reporting advisers) = 26.37 hours per adviser.

increase of 73,880 hours, [756] or $22,735,053 [757] in the monetized value of the hour burden, from the currently approved annual aggregate burden estimates, increases which are attributable primarily to the proposed burden estimates on the larger registered investment adviser and exempt reporting adviser population since the most recent approval, adjustments for inflation, and the amendments to Form ADV.

b. Revised Estimated External Costs for Form ADV

The currently approved total annual collection of information burden estimate for Form ADV anticipates that there will be external costs, including (i) a one-time initial cost for outside legal and compliance consulting fees in connection with the initial preparation of Part 2 of Form ADV, and (ii) the cost for investment advisers to private funds to report the fair value of their private fund assets.[758] The currently approved annual cost burden for Form ADV is $13,683,500, $3,600,000 of which is attributable to external costs incurred by new advisers to prepare Form ADV Part 2, and $10,083,500 of which is attributable to obtaining the fair value of certain private fund assets.[759] We do not expect any change in the annual external costs relating to new advisers preparing Form ADV Part 2. Due to the slightly higher number of registered advisers with private funds, however, the cost of obtaining the fair value of private fund assets may be

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755 $115,139,422 / 12,721 registered investment advisers + 3,843 exempt reporting advisers) = $6,949 per adviser.

756 436,962 hours estimated – 363,082 hours currently approved = 73,880 hour increase in aggregate annual hourly burden.

757 $115,139,422 monetized hourly burden - $92,404,369 = $22,735,053 increase in aggregate annual monetized hourly burden.

758 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR 60452. We do not anticipate that the amendments we are proposing to add Form ADV Part 3 will affect those per adviser cost burden estimates for outside legal and compliance consulting fees. The estimated external costs of outside legal and compliance consulting services for the relationship summary are in addition to the estimated hour burden discussed above.

759 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR at 60452-53. The $10,083,500 is based on 4,469 registered advisers reporting private fund activity as of May 16, 2016.

higher. We estimate that 6% of registered advisers have at least one private fund client that may not be audited. Based on IARD system data as of December 31, 2017, 4,670 registered advisers advise private funds. We therefore estimate that approximately 281 registered advisers may incur costs of $37,625 each on an annual basis, for an aggregate annual total cost of $10,572,625.[760]

In summary, taking into account (i) a one-time initial cost for outside legal and compliance consulting fees in connection with the initial preparation of Part 2 of Form ADV, (ii) the cost for investment advisers to private funds to report the fair value of their private fund assets, and (iii) the incremental external legal or compliance costs for the preparation of the proposed relationship summary, we estimate the annual aggregate external cost burden of the Form ADV information collection would be $18,424,417, or $1,448 per registered adviser.[761] This represents a $4,740,917 increase from the current external costs estimate for the information collection.[762]

B. Rule 204-2 under the Advisers Act

Under section 204 of the Advisers Act, investment advisers registered or required to register with the Commission under section 203 of the Advisers Act must make and keep for prescribed periods such records (as defined in section 3(a)(37) of the Exchange Act), furnish copies thereof, and make and disseminate such reports as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors.

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760 6% x 4,760 = 281 advisers needing to obtain the fair value of certain private fund assets. 281 advisers x $37,625 = $10,572,625.

761 $3,600,000 for preparation of Form ADV Part 2 + $10,572,625 for registered investment advisers to fair value their private fund assets + $4,251,792 to prepare relationship summary = $18,424,417 in total external costs for Form ADV. $18,424,417 / 12,721 total registered advisers as of December 31, 2017 = $1,448 per registered adviser.

762 $18,424,417 - $13,683,500 = $4,740,917.

Rule 204-2 sets forth the requirements for maintaining and preserving specified books and records. We are proposing amendments to rule 204-2 that would require registered advisers to retain copies of each relationship summary. Investment advisers would also be required to maintain each amendment to the relationship summary as well as to make and preserve a record of dates that each relationship summary and each amendment was delivered to any client or to any prospective client who subsequently becomes a client, as well as to any retail investor before such retail investor opens an account. These records would be required to be maintained in the same manner, and for the same period of time, as other books and records required to be maintained under rule 204-2(a), to allow regulators to access the relationship summary during an examination. Specifically, investment advisers would be required to maintain and preserve a record of the relationship summary in an easily accessible place for not less than five years from the end of the fiscal year during which the last entry was made on such record, the first two years in an appropriate office of the investment adviser. This collection of information is found at 17 CFR 275.204-2 and is mandatory. The Commission staff uses the collection of information in its examination and oversight program. Requiring maintenance of these disclosures as part of the firm's books and records would facilitate the Commission's ability to inspect for and enforce compliance with firms' obligations with respect to Form CRS. The information generally is kept confidential.[763]

The likely respondents to this collection of information are all of the approximately 12,721 advisers currently registered with the Commission. We estimate that based on updated IARD data as of December 31, 2017, 7,625 existing advisers will be subject to the amended

[763] *See* section 210(b) of the Advisers Act (15 U.S.C. 80b-10(b)).

provisions of rule 204-2 to preserve the relationship summary as a result of the proposed amendments.

1. Changes in Burden Estimates and New Burden Estimates

The approved annual aggregate burden for rule 204-2 is currently 2,199,791 hours, with a total annual aggregate monetized cost burden of approximately $130,316,112, based on an estimate of 12,024 registered advisers, or 183 hours per registered adviser.[764] We estimate that the proposed amendments would result in an increase in the collection of information burden estimate by 0.2 hours[765] for each of the estimated 7,625 registered advisers with relationship summary obligations,[766] resulting in a total of 183.2 hours per adviser. This would yield an annual estimated aggregate burden of 1,396,900 hours under amended rule 204-2 for all registered advisers with relationship summary obligations,[767] for a monetized cost of $85,476,311.[768] In addition, the 5,096 advisers[769] not subject to the proposed amendments would continue to be subject to an unchanged burden of 183 hours under rule 204-2, or a total aggregate

764 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR at 60454-55.

765 In the Paperwork Reduction Act analysis for amendments to Form ADV adopted in 2016, we estimated that 1.5 hours would be required for each adviser to make and keep records relating to (i) the calculation of performance the adviser distributes to any person and (ii) all written communications received or sent relating to the adviser's performance. Because the burden of preparing of the relationship summary is already included in the collection of information estimates for Form ADV, and because the relationship is a short, standardized document, we assume that recordkeeping burden for the relationship summary would be considerably less than 1.5 hours and estimate that 0.2 hours would be appropriate.

766 *See supra* note 674.

767 7,625 registered investment advisers required to prepare relationship summary x 183.2 hours = 1,396,900 hours.

768 As with our estimates relating to the previous amendments to rule 204-2 (*see* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR at 60454-55, we expect that performance of this function will most likely be allocated between compliance clerks and general clerks, with compliance clerks performing 17% of the function and general clerks performing 83% of the function. Data from the SIFMA Office Salaries in the Securities Industry Report, modified to account for an 1,800-hour work year and multiplied by 2.93 to account for bonuses, firm size, employee benefits, and overhead ("SIFMA Office Salaries Report), suggest that costs for these position are $67 and $60, respectively. (17% x 1,396,9001 hours x $67) + (83% x 1,396,900 hours x $60) = $85,476,311.

769 *See supra* note 681.

annual hour burden of 932,568,[770] for a monetized cost of $57,063,836.[771] In summary, taking into account the estimated annual burden of registered advisers that would be required to maintain records of the relationship summary, as well as the estimated annual burden of registered advisers that do not have relationship summary obligations and whose information collection burden is unchanged, the revised annual aggregate burden for all respondents to rule 204-2, under the proposed amendments, would be estimated to be 2,329,468 total hours,[772] for a monetized cost of $142,540,147.[773]

2. Revised Annual Burden Estimates

As noted above, the approved annual aggregate burden for rule 204-2 is currently 2,199,791, hours based on an estimate of 12,024 registered advisers, or 183 hours per registered adviser.[774] The revised annual aggregate hourly burden for rule 204-2 would be 2,329,468[775] hours, represented by a monetized cost of $142,540,147,[776] based on an estimate of 7,625 registered advisers with the relationship summary obligation and 5,096 registered advisers without, as noted above. This represents in an increase of 129,677[777] annual aggregate hours in

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770 5,096 registered investment advisers not required to prepare the relationship summary x 183 hours = 932,568.

771 As with our estimates relating to the previous amendments to rule 204-2 (*see* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716, at 81 FR at 60454-55, we expect that performance of this function will most likely be allocated between compliance clerks and general clerks, with compliance clerks performing 17% of the function and general clerks performing 83% of the function. Data from the SIFMA Office Salaries Report suggest that costs for these position are $67 and $60, respectively. (17% x 932,568 hours x $67) + (83% x 932,568 hours x $60) = $57,063,836.

772 7,625 registered investment advisers required to prepare relationship summary x 183.2 hours = 1,396,900 hours. 5,096 registered investment advisers not required to prepare the relationship summary x 183 hours = 932,568 hours. 1,396,900 hours + 932,568 hours = 2,329,468 hours.

773 $85,476,311 + $57,063,836 = $142,540,147.

774 2,199,791 hours / 12,024 registered advisers = 183 hours per adviser.

775 *See supra* note 772.

776 *See supra* note 773.

777 2,329,467 hours – 2,199,791 hours = 129,677 hours.

the hour burden and an annual increase of $12,224,035 from the currently approved total aggregate monetized cost for rule 204-2.[778] These increases are attributable to a larger registered investment adviser population since the most recent approval and adjustments for inflation, as well as the proposed rule 204-2 amendments relating to the relationship summary as discussed in this proposing release.

C. Rule 204-5 under the Advisers Act

Proposed new rule 204-5 would require an investment adviser to deliver the relationship summary to each retail investor before or at the time the adviser enters into an investment advisory agreement (even if the adviser's agreement with the retail investor is oral) as well as to existing clients one time within a specified time period after the effective date of the proposed amendments. The adviser also would deliver the relationship summary to existing clients before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's existing account(s) that would materially change the nature and scope of the adviser's relationship with the retail investor, as further discussed in Section II.C.2 above. In addition, advisers would be required to post a current version of their relationship summary prominently on their public website (if they have one). Investment advisers would be required to communicate any changes in an updated relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge. The communication can be made by delivering the relationship summary or by communicating the information in another way to the retail investor.

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[778] $142,540,073 – $130,316,112 = $12,224,035.

Proposed new rule 204-5 contains a collection of information requirement. The collection of information is necessary to provide advisory clients, prospective clients and the Commission with information about the investment adviser and its business, conflicts of interest and personnel. Clients would use the information contained in the relationship summary to determine whether to hire or retain an investment adviser and what type of accounts and services are appropriate for their needs. The Commission would use the information to determine eligibility for registration with us and to manage our regulatory and examination programs. This collection of information would be found at 17 CFR 275.204-5 and would be mandatory. Responses would not be kept confidential.

1. Respondents: Investment Advisers

The likely respondents to this information collection would be the approximately 7,625 investment advisers registered with the Commission that would be required to deliver a relationship summary per proposed new rule 204-5. We also note that these figures include the 366 registered broker-dealers that are dually registered as investment advisers.[779]

2. Initial and Annual Burdens

a. Posting of the Relationship Summary to Website

Under proposed new rule 204-5, advisers would be required to post a current version of their relationship summary prominently on their public website (if they have one). We estimate that each adviser would incur 0.5 hours to prepare the relationship summary, such as to ensure proper electronic formatting, and to post the disclosure to the adviser's website, if the adviser has

[779] *See supra* note 457 and accompanying text.

one.[780] Based on IARD system data, 91.1% of investment advisers with individual clients report at least one public website. Therefore, we estimate that 91.1% of the 7,625 existing and 477 newly-registered investment advisers with relationship summary obligations would incur a total of 3,690 aggregate burden hours to post relationship summaries to their websites,[781] with a monetized cost of $221,428.[782] As with the initial preparation of the relationship summary, we amortize the estimated initial burden associated with posting the relationship summary over a three-year period.[783] Therefore, the total annual aggregate hourly burden related to the initial posting of the relationship summary is estimated to be 1,230 hours, with a monetized cost of $73,809.[784] We do not anticipate external costs to rule 204-5 because investment advisers without a public website would not be required to establish or maintain one. External costs for the preparation of the relationship summary are already included for the collection of information estimates for Form ADV, in Section V.A, above.

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780 This estimate is based upon staff experience. *See e.g*., Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47 ("we estimate, as we did in the proposing release, that rule 498 will impose a ½ hour burden per portfolio annually associated with the compilation of the additional information required on a cover page or at the beginning of the Summary Prospectus. Rule 498 also imposes annual hour burdens associated with the posting of a fund's Summary Prospectus, statutory prospectus, SAI, and most recent report to shareholders on an Internet website. We estimate that the average hour burden for one portfolio to comply with the Internet website posting requirements will be approximately one hour annually.") Because rule 204-5 pertains to one document, the relationship summary, which is much shorter than the several documents to which rule 498 applies, we estimate that each adviser on average would incur approximately 0.5 hours for the preparation of the relationship summary for posting, and for the posting itself.

781 0.5 hours to prepare and post the relationship summary x 91.1% x (7,625 existing advisers + 477 newly-registered advisers with relationship summary obligations) x 0.5 hours = 3,690 hours.

782 Based on data from the SIFMA Office Salaries Report, we expect that requirement for investment advisers to post their relationship summaries to their websites will most likely be performed by a general clerk at an estimated cost of $60 per hour. 0.5 hours per adviser x $60 = $30 in monetized costs per adviser. $30 per adviser x (7,625 existing advisers + 477 newly registered advisers = $221,428 total aggregate monetized cost.

783 *See* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 716.

784 43,688 hours / 3 years = 1,230 hours annually. $221,428 / 3 years = $73,809 in annualized monetized costs.

b. Delivery to Existing Clients

i. One-Time Initial Delivery to Existing Clients

The burden for this proposed rule is based on each adviser with retail investors having, on average, an estimated 4,461 clients who are retail investors.[785] Although advisers may either deliver the relationship summary separately, in a "bulk delivery" to clients, or as part of the delivery of information that advisers already provide, such as the annual Form ADV update, account statements or other periodic reports, we base our estimates here on a "bulk delivery" to existing clients. This is similar to the approach we took in estimating the delivery costs for amendments to rule 204-3 under the Advisers Act, which requires investment advisers to deliver their Form ADV Part 2 brochures and brochure supplements to their clients.[786] As with the estimates for rule 204-3, we estimate that advisers would require approximately 0.02 hours to deliver the relationship summary to each client.[787] Based on IARD data as of December 31, 2017, we estimate that advisers with the obligation to deliver the relationship summary under proposed rule 204-5 have, on average, 4,461 clients who are retail investors, per adviser. Thus, we estimate the total burden hours for 7,625 advisers for initial delivery of the relationship to existing clients to be 89.22 hours per adviser, or 722,860 total aggregate hours, for the first year after the rule is in effect,[788] with a monetized cost of $5,353[789] per adviser or $43,339,507 in

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785 Based on IARD system data as of December 31, 2017.

786 *See* Brochure Adopting Release, *supra* note 157, at 75 FR at 49259.

787 This is the same estimate we made in the Form ADV Part 2 proposal and for which we received no comment. Brochure Adopting Release, *supra* note 157, at 75 FR at 49259 We note that the burden for preparing relationship summaries is already incorporated into the burden estimate for Form ADV discussed above.

788 (0.02 hours per client x 4,461 retail clients per adviser) = 89.22 hours per adviser. 89.22 hours per adviser x (7,625 existing advisers + 477 newly registered advisers) = 722,860 total aggregate hours.

789 Based on data from the SIFMA Office Salaries Report, we expect that initial delivery requirement to existing clients of rule 204-5 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 89.22 hours per adviser x $60 = $5,353 in monetized costs per adviser. We estimate that advisers

aggregate.[790] Amortized over three years, the total annual hourly burden is estimated to be 29.74 hours per adviser, or 240,953 annual hours in aggregate,[791] with annual monetized costs of $1,784 per adviser, or $14,457,209 in aggregate.[792] We do not expect that investment advisers will incur external costs for the initial delivery of the relationship summary to existing clients because we assume that advisers will make such deliveries along with another required delivery, such as an interim or annual update to the Form ADV Part 2.

ii. Delivery for New Account Types or Material Changes in the Nature or Scope of the Advisory Relationship

As noted above, investment advisers also would be required to deliver the relationship summary to existing clients before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's existing account(s) that would materially change the nature and scope of the adviser's relationship with the retail investor, as further discussed in Section II.C.2. With respect to delivery of the relationship summary in the event new account types are opened or material changes occur in the nature or scope of the advisory relationship, we expect that such delivery would take place among 10% of an adviser's retail investors annually. We would therefore estimate a total annual hourly burden of 9 hours per adviser and 72,286 hours in total annual

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will not incur any incremental postage costs because we assume that they will make such deliveries with another mailing the adviser was already delivering to clients, such as interim or annual updates to the Form ADV, or will deliver the relationship summary electronically.

790 $5,353 in monetized costs per adviser x (7,625 existing advisers + 477 newly registered advisers) = $43,339,507 in total aggregate costs.

791 89.22 initial hours per adviser / 3 = 29.74 total annual hours per adviser. 722,860 initial aggregate hours / 3 = 240,953 total annual aggregate hours.

792 $5,353 in monetized costs per adviser / 3 = $1,784 annualized monetized cost per adviser. $43,339,507 initial aggregate monetized cost / 3 = $14,14,457,209 in total annual aggregate monetized cost.

aggregate hours,[793] with a monetized cost of $535 per adviser[794] and $4,337,163 in aggregate.[795] We do not expect advisers to incur external costs related to deliveries of the relationship summary due to new account type openings, or material changes to the nature or scope of the relationship, because we assume that advisers will deliver the relationship summary along with new account agreements and other information normally required in such circumstances.

iii. Posting of Amended Relationship Summaries to Websites and Communicating Changes to Amended Relationship Summaries, Including by Delivery

Investment advisers would be required to amend their relationship summaries within 30 days when any of the information becomes materially inaccurate. We do not expect amendments to be frequent, but based on the historical frequency of amendments made on Form ADV Parts 1 and 2, estimate that on average, each adviser preparing a relationship summary will likely amend the disclosure and average of 1.81 times per year.[796] As above, we estimate that preparation of the relationship summary for posting to the web and the posting itself will require 0.5 hours. Therefore, once again using the same percentage of investment advisers reporting public websites, 91.1% of 7,625 advisers would incur a total annual burden of 0.91 hours per adviser, or

793 10% of 4,461 retail clients per adviser x .02 hours to deliver the relationship summary = 9 hours per adviser. 9 hours x (7,625 existing advisers + 477 new advisers) = 72,286 total aggregate hours.

794 Based on data from the SIFMA Office Salaries Report, we expect that delivery requirements of rule 204-5 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 9 hours per adviser x $60 = $535 per adviser. We estimate that advisers will not incur any incremental postage costs in the delivery of the relationship summary to existing clients for changes in accounts, because we assume that advisers will make such deliveries with another mailing the adviser was already delivering to clients, such as new account agreements and other documentation normally required in such circumstances.

795 $535 in monetized costs per adviser x (7,625 existing advisers + 477 newly registered advisers) = $4,337,163 in total aggregate costs.

796 This estimate is based on IARD system data regarding the number of filings of Form ADV amendments. *See also supra* note 702 and accompanying text.

6,286 hours in aggregate,[797] to post the amended relationship summaries to their website. This translates into an annual monetized cost of $54.30 per adviser, or $377,188 in the aggregate for existing registered advisers with relationship summary obligations.[798] Investment advisers also will be required to communicate any changes in an amended relationship summary to existing clients who are retail investors. The communication can be made by delivering the relationship summary or by communicating the information in another way. For this requirement, we estimate that 50% of advisers will choose to deliver the relationship summary to communicate the updated information, and that the delivery will be made along with other disclosures already required to be delivered, such as an interim or annual Form ADV update. We therefore estimate a burden of 615,674[799] hours, or 161.5 hours per adviser,[800] at a monetized cost of $36,940,426 in aggregate,[801] or $9,689 per adviser,[802] for the 50% of advisers that choose to deliver amended

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797 0.5 hours to post the amendment x 1.81 amendments annually = 0.91 hours per adviser annually to post amendments to the website. 0.91 x 7,625 existing advisers amending the relationship summary x 91.1% of advisers with public websites = 6,286 aggregate annual hours to post amendments of the relationship summary.

798 Based on data from the SIFMA Office Salaries Report, we expect that the posting requirements of rule 204-5 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 0.91 hours per adviser x $60 = $54.30 per adviser. $54.30 per adviser x 91.1% x 7,625 existing advisers = $377,188 in annual monetized costs.

799 7,625 advisers amending the relationship summary x 4,461 retail clients per adviser x 50% delivering the amended relationship summary to communicate updated information x 0.02 hours per delivery x 1.81 amendments annually = 615,674 hours to deliver amended relationship summaries.

800 4,461 retail clients per adviser x 0.02 hours per delivery x 1.81 amendments annually = 161.5 hours per adviser.

801 Based on data from the SIFMA Office Salaries Report, we expect that delivery requirements of rule 204-5 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 615,674 hours x $60 = $36,940,426. We estimate that advisers will not incur any incremental postage costs to deliver the relationship summary for communicating updated information by delivering the relationship summary, because we assume that advisers will make the delivery along with other documents already required to be delivered, such as an interim or annual update to Form ADV, or will deliver the relationship summary electronically.

802 Based on data from the SIFMA Office Salaries Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, we expect that delivery requirements of rule 204-5 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 161.5 hours per adviser x $60 per hour = $9,689 per adviser.

relationship summaries in order to communicate updated information. Similar to the other delivery requirements discussed above for proposed rule 204-5, we do not expect investment advisers to incur external costs in delivering amended relationship summaries because we assume that they will make this delivery with other disclosures required to be delivered, such as an interim or annual update to Form ADV.

c. Delivery to New Clients or Prospective New Clients

Data from the IARD system indicate that of the 12,721 advisers registered with the Commission, 7,625 have retail investors, and on average, each has 4,461 clients who are retail investors.[803] Based on IARD system data from 2015 to 2017, we estimate that the client base for investment advisers will grow by approximately 4.5% annually.[804] Based on our experience with Form ADV Part 2, we estimate the annual hour burden for initial delivery of a relationship summary would be the same by paper or electronic format, at 0.02 hours for each relationship summary,[805] or 4 annual hours per adviser.[806] Therefore, we estimate that the aggregate annual hour burden for initial delivery of the relationship summary to new clients would be 30,614 hours,[807] at a monetized cost of $1,836,817, or $241 per adviser.[808] We do not expect that

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803 This average is based on advisers' responses to Item 5 of Part 1A of Form ADV as of December 31, 2017.

804 The number of retail clients reported by RIAs changed by 6.7% between December 2015 and 2016, and by 2.3% between December 2016 and 2017. (6.7% + 2.3%) / 2 = 4.5% average annual rate of change over the past two years.

805 This is the same as the estimate for the burden to deliver the brochure required by Form ADV Part 2. *See* Brochure Adopting Release, *supra* note 157.

806 4,461 clients per adviser with retail clients x 4.5% = 201 new clients per adviser. 201 new clients per adviser x .02 hours per delivery = 4.0 hours per adviser for delivery of a relationship summary to new or prospective new clients.

807 4.0 hours per adviser for delivery obligation to new or prospective clients x 7,625 advisers = 30,614 hours.

808 Based on data from the SIFMA Office Salaries Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, we expect that delivery requirements of rule 204-5 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 7,625 hours x $60 = $1,836,817. We estimate that advisers will not incur any incremental postage costs to deliver the relationship summary to new or prospective clients because we assume that

advisers will incur external costs to deliver the relationship summary to new or prospective clients because we assume that advisers will make the delivery along with other documentation normally provided in such circumstances, such as Form ADV Part 2, or will deliver the relationship summary electronically.

d. Total New Initial and Annual Burdens

Altogether, we estimate the total collection of information burden for proposed new rule 204-5 to be 967,044 annual aggregate hours per year,[809] or 126.8 hours per respondent,[810] for a total annual aggregate monetized cost of $58,022,611,[811] or $7,610[812] per adviser. We request comment on the estimated hourly and cost burdens for the new collection of information under proposed rule 204-5.

D. Form CRS and Rule 17a-14 under the Exchange Act

New proposed rule 17a-14 under the Exchange Act [17 CFR 240.17a-14] and Form CRS [17 CFR 249.640] would require a broker-dealer that offer services to retail investors to prepare, file with the Commission, post to the broker-dealer's website (if it has one), and deliver to retail investors a relationship summary, as discussed in greater detail in Section II above. Broker-

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advisers will make the delivery along with other documentation normally provided in such circumstances, such as Form ADV Part 2. $1,835,371 / 7,625 investment advisers = $241 per adviser.

809 1,230 annual hours for posting initial relationship summaries to adviser websites + 240,953 annual hours for initial delivery to existing clients + 72,286 hours for delivery to existing clients based on material changes to accounts or scope of relationship + 6,286 annual hours to post amended relationship summary to website + 615,674 hours for delivery to existing clients to communicate updated information in amended relationship summaries + 30,614 hours for delivery to new or prospective clients = 967,044 annual total hours for investment advisers to post and deliver the relationship summary under proposed rule 204-5.

810 967,044 hours (initial and other deliveries) / 7,625 advisers = 126.8 hours per adviser.

811 $73,809 for posting initial relationship summaries to adviser websites + $14,457,209 for initial delivery to existing clients + $4,337,162 for delivery to existing clients based on material changes to accounts or scope of relationship + $377,188 to post amended relationship summary to website + $36,940,426 for delivery to existing clients to communicate updated information in amended relationship summaries + $1,836,817 for delivery to new or prospective clients = $58,022,611 in total annual aggregate monetized cost for investment advisers to post and deliver the relationship summary under proposed rule 204-5.

812 $58,022,611 / 7,625 advisers = $7,610 per adviser.

dealers would file the relationship summary with EDGAR and deliver the relationship summary to both existing customers and new or prospective new customers who are retail investors. New proposed rule 17a-14 under the Exchange Act [17 CFR 240.17a-14] and Form CRS [17 CFR 249.640] contain a collection of information requirement. We will use the information to manage our regulatory and examination programs. Clients can use the information required in Form CRS to determine whether to hire or retain a broker-dealer, as well as what types of accounts and services are appropriate for their needs. The collection of information is necessary to provide broker-dealer customers, prospective customers, and the Commission with information about the broker-dealer and its business, conflicts of interest and personnel. This collection of information would be found at 17 CFR 249.640 and would be mandatory. Responses would not be kept confidential.

1. Respondents: Broker-Dealers

The respondents to this information collection would be the broker-dealers registered with the Commission that would be required to deliver a relationship summary in accordance with proposed new rule 17a-14 under the Exchange Act [17 CFR 240.17a-14]. As of December 31, 2017, there were 2,857 broker-dealers registered with the Commission that reported sales to retail customer investors,[813] and therefore likely would be required to prepare and deliver the relationship summary.[814] We also note that these include 366 broker-dealers that are dually

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813 *See supra* note 461 and accompanying text. Retail sales activity is identified from Form BR (*see supra note* 280, which categorizes retail activity broadly (by marking the "sales" box) or narrowly (by marking the "retail" or "institutional" boxes as types of sales activity). We use the broad definition of sales as we preliminarily believe that many firms will just mark "sales" if they have both retail and institutional activity. However, we note that this may capture some broker-dealers that do not have retail activity, although we are unable to estimate that frequency.

814 For purposes of Form CRS, a "retail investor" would be defined as: a prospective or existing client or customer who is a natural person (an individual) and would include a trust or other similar entity that represents natural persons, even if another person is a trustee or managing agent of the trust.

registered as investment advisers.[815] To a great extent, the burden for dual registrants to prepare and deliver the relationship summary and post it to a website is already accounted for in the estimated burdens for investment advisers under the proposed amendments to Form ADV and proposed new rule 204-5, discussed in Sections V.A and V.C above. However, dually registered broker-dealers will incur burdens related to their business as an investment adviser that standalone broker-dealers will not incur, such as the requirement to file the relationship summary with IAPD (in addition to EDGAR as a broker-dealer), and to deliver to both investment advisory clients and brokerage customers, to the extent those groups of retail investors do not overlap. Therefore, although treating dually registered broker-dealers in this way may be over-inclusive, we base our burden estimates for proposed rule 17a-14 and Form CRS on 2,857 broker-dealers with relationship summary obligations, including those dually registered as broker-dealers.[816]

2. Initial and Annual Burdens

a. Initial Preparation, Filing, and Posting of Relationship Summary

Unlike investment advisers, broker-dealers currently are not required to disclose in one place all of the information required by the relationship summary or to file a narrative disclosure document with the Commission. We estimate, therefore, that the initial first year burden for preparing and filing the relationship summary would be 15.0 hours per registered broker-dealer. The narrative descriptions required in the relationship summary should be narrowly tailored and brief, and the relationship summary must be limited to four pages (or equivalent limit if in electronic format). The relationship summary would be standardized across broker-dealers given

815 *See supra* note 457 and accompanying text.

816 *See supra* note 457 and accompanying text.

the mandated set and sequence of topic areas, and moreover, a considerable amount of language within each topic area also would be prescribed, thereby limiting the amount of time required to prepare the disclosure. Therefore, we believe that the time needed to prepare the relationship summary should not vary significantly based on the size of the broker-dealer. However, unlike investment advisers, which already prepare Form ADV Part 2 brochures and have information readily available to prepare the relationship summary, broker-dealers would be required for the first time to prepare disclosure that contains all the information proposed to be required by the relationship summary. In addition, investment advisers already file their brochures on IARD, while broker-dealers may incur new burdens to file their relationship summaries on EDGAR. Therefore, we believe that each broker-dealer respondent would incur 15 hours on a one-time basis, instead of five hours for investment advisers, for the initial preparation and filing of the relationship summary. However, we believe that the amount of time needed to post the relationship summary on the broker-dealer's website, if it has one, would not vary significantly from the time needed by investment advisers because the time required to prepare and post disclosure that is standardized in length and content should not vary significantly across firms. As with investment advisers, we estimate that each broker-dealer would incur 0.5 hours to prepare the relationship summary for posting to its website, if it has one, such as to ensure proper electronic formatting, and to perform the actual posting.[817]

Given these assumptions, we estimate the total one-time initial hourly burden for broker-dealers to prepare the relationship summary and file it with the Commission would be 42,855 hours,[818] for a monetized value of $11,292,293.[819] We estimate that the initial burden of posting

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817 *See supra* note 780.

818 15.0 hours x 2,857 broker-dealers with retail accounts = 42,855 total hours.

the relationship summary to their websites, if they have one, would be 1,428 hours,[820] for a monetized value of $85,710.[821] To arrive at an annual burden for preparing, filing, and posting the relationship summary, as for advisers, the initial burden would be amortized over a three-year period. Therefore, the total annual aggregate hour burden for registered broker-dealers to prepare, file, and post a relationship summary to their website, if they have one, would be 14,761 hours, or 5.17 hours per broker-dealer,[822] for an annual monetized cost of $3,792,668, or $1,328 per broker-dealer.[823]

b. Estimated External Costs for Initial Preparation of Relationship Summary

Under proposed new rule 17a-14, broker-dealers would be required to prepare and file a relationship summary, as well as post it to their website if they have one. We do not anticipate external costs in the form of website set-up, maintenance, or licensing fees because broker-dealers would not be required to establish a website for the sole purpose of posting their relationship summary if they do not already have a website. We do anticipate that some broker-dealers may incur a one-time initial cost for outside legal and consulting fees in connection with

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819 42,855 total aggregate initial hour burden for preparing and filing a relationship summary. We expect that performance of this function will most likely be equally allocated between a senior compliance examiner and a compliance manager. Data from the SIFMA Management and Professional Earnings Report suggest that costs for these positions are $229 and $298 per hour, respectively. (21,427.5 hours x $229 + (21,427.5 hours x $298 = $11,292,293).

820 0.5 hours x 2,857 broker-dealers = 1,248 hours to prepare and post relationship summary to the website.

821 Based on data from the SIFMA Office Salaries Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, we expect that performance of this function will most likely be performed by a general clerk at an estimated cost of $60 per hour. 1,429 hours x $60 = $85,710 total aggregate monetized cost.

822 42,855 hours / 3 years = 14,761 total aggregate annual hour burden to prepare and file relationship summary. 14,761 hours / 2,857 broker-dealers with retail accounts = 5.17 hours annually per broker-dealer.

823 ($11,292,293 total initial aggregate monetized cost for preparation and filing + $85,710 for posting to the website) / 3 = $3,792,668 total annual monetized cost for preparation, filing and posting the relationship summary. $3,792,668 / 2,857 broker-dealers subject to relationship summary obligations = $1,328 per broker-dealer.

the initial preparation of the relationship summary. Although broker-dealers subject to the relationship summary requirement may vary widely in terms of the size, complexity and nature of their businesses, the amount of disclosure required would not vary substantially among broker-dealers. Accordingly, the amount of time, and thus cost, required for outside legal and compliance review is unlikely to vary substantially among those broker-dealers who elect to obtain outside assistance.[824] The relationship summary is short, standardized, and contains largely prescribed language. Because the information required in the relationship summary pertains largely to the broker-dealer's own business practices, the information is likely more readily available to the broker-dealer than to an external legal or compliance consultant. As a result, we anticipate that only a quarter of broker-dealers will seek the help of outside legal services and half will seek the help of compliance consulting services in connection with the initial preparation of the relationship summary. We estimate that the initial per broker-dealer cost for legal services related to the preparation of the relationship summary would be $1,416.[825] We estimate that the initial per broker-dealer cost for compliance consulting services related to the preparation of the relationship summary would be $2,109.[826] Accordingly, we estimate that 715 broker-dealers will use outside legal services, for a total initial aggregate cost burden of

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824 We estimate that an external service provider would spend 3 hours helping a broker-dealer prepare an initial relationship summary.

825 External legal fees are in addition to the projected hour per broker-dealer burden discussed above. $472 per hour for legal services x 3 hours per broker-dealer = $1,416. The hourly cost estimate of $472 is adjusted for inflation and based on our consultation with broker-dealers and law firms who regularly assist them in compliance matters.

826 External compliance consulting fees are in addition to the projected hour per broker-dealer burden discussed above. Data from the SIFMA Management and Professional Earnings Report suggest that outside management consulting services cost approximately $703 per hour. $703 per hour for outside consulting services x 3 hours per adviser = $2,109.

$1,011,378,[827] and 1,429 broker-dealers will use outside compliance consulting services, for a total initial aggregate cost burden of $3,012,707,[828] resulting in a total initial aggregate cost burden among all respondents of $4,024,085, or $1,409 per broker-dealer, for outside legal and compliance consulting fees related to preparation of the relationship summary.[829] Annually, this represents $1,341,362, or $470 per broker-dealer, when amortized over a three-year period.[830]

We do not expect ongoing external legal or compliance consulting costs for the relationship summary. Although broker-dealers would be required to amend the relationship summary within 30 days whenever any information becomes materially inaccurate, given the standardized nature and prescribed language of the relationship summary, we expect that amendments would be factual and require relatively minimal wording changes. We believe that broker-dealers would be more knowledgeable about these facts than outside legal or compliance consultants and would be able to make these revisions in-house. Therefore, we do not expect that broker-dealers will need to incur ongoing external costs for the preparation and review of relationship summary amendments.

c. Amendments to the Relationship Summary and Filing and Posting of Amendments

As with our estimates above for investment advisers, we do not expect broker-dealers to amend their relationship summaries frequently. Based on staff experience, we believe that many broker-dealers, as a matter of best practices, would update their relationship summary at a

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827 25% x 2,857 SEC registered broker-dealers = 715 broker-dealers. $1,416 for legal services x 715 broker-dealers = $1,011,378.

828 50% x 2,857 SEC registered broker-dealers = 1,429 broker-dealers. $2,109 for compliance consulting services x 1,429 broker-dealers = $3,012,707.

829 $1,011,378 + $3,012,707 = $4,024,085. $4,024,085 / 2,857 broker-dealers = $1,409 per broker-dealer.

830 $4,024,085 initial aggregate hours / 3 years = $1,341,362 annually. $1,409 initial hours per broker-dealer / 3 years = $469.50.

minimum once a year, after conducting an annual supervisory review, for example.[831] We also estimate that on average, each broker-dealer preparing a relationship summary may amend the disclosure once more during the year, due to emerging issues. Therefore, we assume that broker-dealers would update their relationship summary, on average, twice a year, and as with investment advisers, we estimate that broker-dealers would require 0.5 hours to amend and file the updated relationship summary, and 0.5 hours to post it to their website. Thus, we estimate that broker-dealers would incur a total annual aggregate hourly burden of 5,714 hours per year, to prepare and file, and post to their websites an estimated total of 5,714 amendments per year.[832]

d. Delivery of the Relationship Summary

Proposed rule 17a-14 under the Exchange Act would require a broker-dealer to deliver the relationship summary, with respect to a retail investor that is a new or prospective customer, before or at the time the retail investor first engages the broker-dealer's services. Broker-dealers also would make a one-time, initial delivery of the relationship summary to all existing customers within a specified time period after the effective date of the proposal. Also with respect to existing customers, broker-dealers would deliver the relationship summary before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's account(s) existing account(s) that would materially change the nature and scope of the broker-dealer's relationship with the retail investor, as further discussed in II.C.2 above.

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831 FINRA rules set an annual supervisory review as a minimum threshold for broker-dealers, for example in FINRA Rules 3110 (requiring an annual review of the businesses in which the broker-dealer engages), 3120 (requiring an annual report detailing a broker-dealer's system of supervisory controls, including compliance efforts in the areas of antifraud and sales practices); and 3130 (requiring each broker-dealer's CEO or equivalent officer to certify annually to the reasonable design of the policies and procedures for compliance with relevant regulatory requirements).

832 2,857 broker-dealers amending relationship summaries x 2 amendments per year = 5,714 amendments per year. 5,714 amendments x (0.5 hours to amend and file + 0.5 hours to post to website) = 5,714 hours.

i. One-Time Initial Delivery to Existing Customers

We estimate the burden for broker-dealers to make a one-time initial delivery of the relationship summary to existing customers based on an estimate of the number of accounts held by these broker-dealers. Based on FOCUS data, we estimate that the 2,857 broker-dealers that report retail activity have approximately 128 million customer accounts, and that approximately 79%, or 101.248 million, of those accounts belong to retail customers.[833] We estimate that, under the proposed rule, broker-dealers would send their relationship summary along with other required disclosures, such as periodic account statements, in order to comply with initial delivery requirement for the relationship summary. As with investment advisers, we estimate that a broker-dealer will require no more than 0.02 hours to send the relationship summary to each customer, or an aggregate initial burden of 2,024,960 hours, or approximately 709 hours per broker-dealer for the first year after the rule is in effect.[834] We would therefore expect the aggregate monetized cost for broker-dealers to make a one-time initial delivery of relationship summaries to existing customers to be $121,497,600.[835] Amortized over three years, the total annual hourly burden is estimated to be 674,987 hours, or approximately 236.3 hours per broker-

833 *See supra* notes 428 – 437 and accompanying text. 2,857 broker-dealers (including dual registrants) report 128 million customer accounts. We are aware that, based on data from IARD, investment advisers reporting retail activity have approximately 79.1% retail clients and 21.9% non-retail clients. While acknowledging the differences between the investment adviser and broker-dealer models, we apply the 79.1% in estimating the proportion of broker-dealer accounts that belong to retail customers. Therefore, 79.1% x 128 million accounts = 101.248 million accounts. This number likely overstates the number of deliveries to be made due to the double-counting of deliveries to be made by dual registrants to a certain extent, and the fact that one customer may own more than one account.

834 (0.02 hours per customer account x 101.248 million customer accounts) = 2,024,960 hours. We note that the burden for preparing updated relationship summaries is already incorporated into the burden estimate for Form CRS discussed above. 2,024,960 hours / 2,857 broker-dealers = approximately 709 hours per broker-dealer.

835 Based on data from SIFMA's Office Salaries Report, we expect that initial delivery requirement to existing clients of rule 17a-14 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 2,024,960 hours x $60 = $121,497,600. We estimate that broker-dealers will not incur any incremental postage costs because we assume that they will make such deliveries with another mailing the broker-dealer was already delivering to clients, such as periodic account statements.

dealer,[836] with annual monetized costs of $40,499,200 and $14,175, respectively.[837] We do not expect that broker-dealers will incur external costs for the initial delivery of the relationship summary to existing clients because we assume that they will make such deliveries along with another required delivery, such as periodic account statements.

ii. Delivery for New Account Types or Material Changes in the Nature or Scope of the Brokerage Relationship

Broker-dealers would be required to deliver the relationship summary to existing customers before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's existing account(s) that would materially change the nature and scope of the adviser's relationship with the retail investor, as further discussed in Section II.C.2. With respect to delivery of the relationship summary in the event of material changes in the nature or scope of the brokerage relationship, as with investment advisers, we estimate that this would take place among 10% of a broker-dealer's retail investors annually. We would therefore estimate broker-dealers to incur a total annual aggregate burden of 202,496 hours, or 71 hours per broker-dealer,[838] at an annual aggregate monetized cost of $12,149,760, or approximately $4,253 per broker-dealer.[839] We do not expect

836 2,024,960 initial aggregate hours / 3 = 674,987 total annual aggregate hours. 709 initial hours per broker-dealer / 3 = 236.3 total annual hours per broker-dealer.

837 $121,497,600 initial aggregate monetized cost / 3 = $40,499,200 annual aggregate monetized cost. $40,499,200 / 2,857 broker-dealers = $14,175 annual monetized cost per broker-dealer.

838 10% of 101.248 million customers x .02 hours = 202,496 hours. 202,496 hours / 2,857 broker-dealers = 71 hours per broker-dealer.

839 Based on data from the SIFMA Office Salaries Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, we expect that delivery requirements of rule 17a-14 will most likely be performed by a general clerk at an estimated cost of $60 per hour. 202,496 hours x $60 = $12,149,760. $12,149,760 / 2,857 broker-dealers = $4,253 per broker-dealer. We estimate that broker-dealers will not incur any incremental postage costs in these deliveries of the relationship summary to existing customers, because we assume that broker-dealers will make such deliveries with another mailing the broker-dealer was already delivering to clients, such as periodic account statements, or new account agreements and other similar documentation.

broker-dealers to incur external costs related to deliveries of the relationship summary due to new account type openings, or material changes to the nature or scope of the relationship, because we assume that broker-dealers will deliver the relationship summary along with new account agreements and other documentation normally required in such circumstances, or with periodic account statements.

iii. Communicating Changes to Amended Relationship Summaries, Including by Delivery

As discussed above, broker-dealers must communicate any changes in an updated relationship summary to retail investors who are existing customers of the firm within 30 days after the updates are required to be made and without charge. The communication can be made by delivering the relationship summary or by communicating the information in another way to the retail investor. Consistent with our discussion on broker-dealers' amendments to the relationship summary we are assuming that the 2,857 broker-dealers with relationship summaries will amend them twice each year. We also assume that 50% will choose to deliver the relationship summary to communicate the update information. As with investment advisers, we estimate that broker-dealers would require 0.02 hours to make a delivery to each customer. Therefore, the estimated burden for those broker-dealers choosing to deliver an amended relationship summary to meet this communication requirement would be approximately 2,024,960 hours, or 709 hours per broker-dealer,[840] translating into a monetized cost of $121,497,600 in aggregate, or $42,526 per broker-dealer.[841] Similar to the other delivery

[840] 2 amendments per year x 101.248 million customer accounts x 50% delivering the amended relationship summary to communicate updated information x 0.02 hours per delivery = 2,024,960 hours to deliver amended relationship summaries. 2,024,960 hours / 2,857 broker-dealers = 709 hours per broker-dealer.

[841] Based on data from the SIFMA Office Salaries Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, we expect that delivery requirements of rule 17a-14 will most likely be performed by a general clerk at an estimated cost

requirements relating to proposed rule 17a-14, we do not expect broker-dealers to incur external costs in delivering amended relationship summaries because we assume that they will make this delivery with other documents required to be delivered, such as periodic account statements.

e. Delivery to New Clients or Prospective New Customers

To estimate the delivery burden for broker-dealers' new or prospective new customers, as discussed above, we estimate that the 2,857 standalone broker-dealers with retail activity have approximately 101.248 million retail customer accounts.[842] Based on FOCUS data over the past five years, we estimate that broker-dealers grow their customer base and enter into new agreements with, on average, 8% more new retail investors each year.[843] We estimate the hour burden for initial delivery of a relationship summary would be the same by paper or electronic format, at 0.02 hours for each relationship summary, as we have estimated above. Therefore, the aggregate annual hour burden for initial delivery of the relationship summary by broker-dealers to new or prospective new customers would be 161,917 hours, or 56.7 hours per broker-dealer.[844] at a monetized cost of $9,715,001 at an aggregate level, or $3,400 per broker-dealer.[845]

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of $60 per hour. 2,024,960 hours x $60 = $121,497,600. $121,497,600 / 2,857 broker-dealers = $42,526 per broker-dealer. We estimate that broker-dealers will not incur any incremental postage costs to deliver these relationship summaries, because we assume that advisers will make the delivery along with other documentation they normally would provide, such as account opening documents.

842 *See supra* notes 429 – 439 and accompanying text.

843 This represents the average annual rate of growth from 2012-2016 in the number of accounts for all broker-dealers reporting retail activity.

844 101.248 million customer accounts x 8% increase = 8,095,834 new customers. 8,095,834 new customers x 0.02 hours per delivery = 161,917 total annual aggregate hours. 161,917 / 2,857 broker-dealers = 56.7 hours per broker-dealer for delivery to new customers.

845 Based on data from the SIFMA Office Salaries Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, we expect that these functions will most likely be performed by a general clerk at an estimated cost of $60 per hour. 161,917 hours x $60 = $9,715,001. $9,715,001 / 2,857 broker-dealers = $3,400 per broker-dealer for delivery to new customers. We estimate that broker-dealers will not incur any incremental postage costs to deliver the relationship summary to new or prospective clients because we assume that broker-dealers will make the delivery along with other documentation, such as periodic account statements.

f. Total New Initial and Annual Burdens

As discussed above, we estimate the total annual collection of information burden for proposed new rule 17a-14 in connection with obligations relating to the relationship summary, including (i) initial preparation, filing, and posting to a website; (ii) amendments to the relationship summary for material updates and related filing and website posting burdens; (iii) one-time initial delivery to existing customers; (iv) delivery to existing customers who are opening new accounts or materially changing the nature or scope of their relationship with the broker-dealer; (v) delivery of amended relationship summaries; and (vi) delivery to new and prospective customers. Given these proposed requirements, we estimate the total annual aggregate hourly burden to be approximately 3,084,835 hours per year, or 1,080 hours on a per broker-dealer basis.[846] This translates into an aggregate annual monetized cost of $188,578,462, or $66,066 on a broker-dealer basis per year.[847] In addition, we estimate that broker-dealers would incur external legal and compliance costs in the initial preparation of the relationship summary of approximately $4,024,085 in aggregate, or $1,409 per broker-dealer, translating into $1,341,362 annually, or $470 per broker-dealer, when amortized over a three year period.

[846] 14,761 hours per year for initial preparation, filing, and posting of relationship summary + 5,714 hours per year for amendments, filing, and posting of amendments + 674,987 hours for one-time initial delivery to existing customers + 202,496 hours for delivery to existing customers making material changes to their accounts + 2,024,960 hours for delivery of amendments + 161,917 hours for delivery to new customers = 3,084,835 total annual aggregate hours. 3,084,835 hours / 2,857 broker-dealers = 1,080 hours per broker-dealer.

[847] $3,792,668 per year for initial preparation, filing, and posting of relationship summary + $924,240 per year for amendments, filing, and posting of amendments + $40,499,200 for one-time initial delivery to existing customers (amortized over three years) + $12,149,760 for delivery to existing customers making material changes to their accounts + $121,497,600 for delivery of amendments + $9,715,001 for delivery to new customers = $188,578,468 in total annual aggregate monetized cost. $188,578,468 / 2,857 broker-dealers = $66,066 per broker-dealer.

E. Recordkeeping Obligations under Rule 17a-3 of the Exchange Act[848]

The proposed requirement to make a record indicating the date that a relationship summary was provided to each customer and to each prospective customer who subsequently becomes a customer would contain a collection of information that would be found at 17 CFR 240.17a-3(a)(24) and would be mandatory. The Commission staff would use this collection of information in its examination and oversight program, and the information generally is kept confidential.[849] The likely respondents to this collection of information requirement are the approximately 2,857 broker-dealers currently registered with the Commission that offer services to retail investors, as defined above.[850]

Exchange Act section 17(a)(1) requires registered broker-dealers to make and keep for prescribed periods such records as the Commission deems "necessary or appropriate in the public interest, for the protection of investors or otherwise in furtherance of the purposes of" the Exchange Act."[851] Exchange Act rules 17a-3 and 17a-4 specify minimum requirements with respect to the records that broker-dealers must make, and how long those records and other documents must be kept, respectively.

The amendments to rule 17a-3 that we are proposing today would require SEC-registered broker-dealers to make a record indicating the date that a relationship summary was provided to each customer and to each prospective customer who subsequently becomes a customer. Commission staff has estimated that the proposed amendments to rule 17a-3(a)(24) would result in an incremental burden increase of 0.1 hours annually for each of the estimated SEC-registered

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848 In a concurrent release, we are proposing additional burden adjustments to rules 17a-3 and 17a-4 of the Exchange Act. *See* Regulation Best Interest Proposal, *supra* note 24.

849 *See* section 24(b) of the Exchange Act (15 U.S.C. 78x-24(b)).

850 *See supra* note 29 and accompanying text.

851 *See* section 17(a) of the Exchange Act.

broker-dealers that would be required to prepare and preserve the initial relationship summary and any amendments.[852]

The incremental hour burden for broker-dealers to maintain the relationship summary would therefore be 286 hours,[853] for a monetized cost of 17,481 in aggregate, or $6.00 per broker-dealer.[854]

F. Record Retention Obligations under Rule 17a-4 of the Exchange Act

Exchange Act section 17(a)(1) requires registered broker-dealers to make and keep for prescribed periods such records as the Commission deems "necessary or appropriate in the public interest, for the protection of investors or otherwise in furtherance of the purposes of" the Exchange Act."[855] Exchange Act rule 17a-4 specifies minimum requirements with respect to how long records created under Exchange Act rule 17a-3 and other documents must be kept. We are proposing amendments to rule 17a-4 that would require broker-dealers to retain copies of each relationship summary, including amendments, and to preserve the record of dates that each relationship summary and each amendment thereto was delivered to any existing customer or to any new or prospective customer, pursuant to the proposed new requirements under amended rule 17a-3, discussed above. These records would be required to be maintained in an easily accessible place for at least six years after such record or relationship summary is created. This

852 We apply the same 0.2 hour estimate as with investment advisers, but divided equally between creating a record of the relationship summary and its deliveries and the maintenance of those records.

853 2,857 broker-dealers x 0.1 hours annually = 286 annual hours for recordkeeping.

854 As with our estimates relating to the proposed amendments to rule 204-2 under the Advisers Act (*see, e.g., supra* note 771 and accompanying text), we expect that performance of this function will most likely be allocated between compliance clerks and general clerks, with compliance clerks performing 17% of the function and general clerks performing 83% of the function. Data from the SIFMA Office Salaries Report suggest that costs for these position are $67 and $60, respectively. (17% x 286 hours x $67) + (83% x 286 hours x $60) = $17,481. $17,481 / 2,857 broker-dealers = $6.00 per broker-dealer.

855 *See* section 17(a) of the Exchange Act.

collection of information would be found at 17 CFR 240.17a-4 and would be mandatory. The Commission staff would use the collection of information in its examination and oversight program. Requiring maintenance of these disclosures as part of the broker-dealer's books and records would facilitate the Commission's ability to inspect for and enforce compliance with firms' obligations with respect to Form CRS. The information generally is kept confidential.[856]

The likely respondents to this collection of information requirement are the approximately 2,857 broker-dealers that report retail activity, as described above.

1. Changes in Burden Estimates and New Burden Estimates

The approved annual aggregate burden for rule 17a-4 is currently 1,042,416 hours, with a total annual aggregate monetized cost burden of approximately $67.8 million, based on an estimate of 4,104 broker-dealers and 150 broker-dealers maintaining an internal broker-dealer system.[857] The currently approved external cost estimate to respondents is $20,520,000.[858] We estimate that the proposed amendments would result in an increase in the collection of information burden estimate by 0.10 hours[859] for each of the estimated 2,857 currently registered broker-dealers that report retail sales activity and would have relationship summary obligations.[860] This would yield an annual estimated aggregate burden of 754,964 hours for all

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856 *See* section 24(b) of the Exchange Act (15 U.S.C. 78x-24(b)).

857 (4,104 broker-dealers x 254 hours per broker-dealer) + (150 broker-dealers maintaining internal broker-dealer systems x 3 hours) = (1,042,416 hours + 450 hours) = 1,042,866 hours each year. The monetized cost was based on these functions being performed by a compliance clerk earning an average of $65 per hour, resulting in a total internal cost of compliance of (1,042,416 x $65) + (450 x $65) = $67,786. *See* 17a-4 Supporting Statement, *available at* https://www.reginfo.gov/public/do/PRAViewDocument?ref_nbr=201607-3235-007.

858 4,104 broker-dealers x $5,000 annual recordkeeping cost per broker-dealer = $20,520,000. *See id*.

859 We apply the same 0.2 hour estimate as with investment advisers, but divided equally between creating a record of the relationship summary and its deliveries and the maintenance of those records.

860 *See supra* note 616.

broker-dealers with relationship summary obligations to comply with rule 17a-4,[861] for a monetized cost of approximately $48.6 million.[862] In addition, the 984 broker-dealers[863] not subject to the proposed amendments would continue to be subject to an unchanged burden of 254 hours per broker-dealer, or 249,936 hours for these broker-dealers.[864] In addition, those maintaining an internal broker-dealer system would continue to be subject to an unchanged burden of 450 hours annually, under rule 17a-4. In summary, taking into account the estimated annual burden of broker-dealers that would be required to maintain records of the relationship summary, as well the estimated annual burden of broker-dealers that do not have relationship summary obligations and whose information collection burden is unchanged, the revised annual aggregate burden for all broker-dealer respondents to the recordkeeping requirements under rule 17a-4 is estimated to be 976,350 total annual aggregate hours,[865] for a monetized cost of approximately $65.4 million.[866]

2. Revised Annual Burden Estimates

As noted above, the approved annual aggregate burden for rule 17a-4 is currently 1,042,416 hours, with a total annual aggregate monetized cost burden of approximately $67.8 million, based on an estimate of 4,104 broker-dealers and 150 broker-dealers maintaining an internal broker-dealer system. The revised annual aggregate hourly burden for rule 17a-4 would

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861 2,857 broker-dealers required to prepare relationship summary x (254 hours + 0.1 hour) = 725,964 hours.

862 Consistent with our prior paperwork reduction analyses for rule 17a-4, we expect that performance of this function will most likely be performed by compliance clerks. Data from the SIFMA Office Salaries Report suggest that costs for these positions are $67 per hour. 725,964 hours x $67 = $48,639,568.

863 *See supra* note 618.

864 984 broker-dealers x 254 hours = 249,936 hours for broker-dealers not preparing a relationship summary.

865 725,964 + 249,936 + 450 = 976,350 total aggregate hours.

866 Consistent with our prior paperwork reduction analyses for rule 17a-4, we expect that performance of this function will most likely be performed by compliance clerks. Data from the SIFMA Office Salaries Report suggest that costs for these positions are $67 per hour. 976,650 hours x $67 = $65,415,430.

be 976,350[867] hours, represented by a monetized cost of approximately $65.4 million,[868] based on an estimate of 2,857 broker-dealers with the relationship summary obligation and 984 broker-dealers without, as noted above. This represents a decrease of 66,516[869] annual aggregate hours in the hour burden and an annual decrease of approximately $2.37 million from the currently approved total aggregate monetized cost for rule 17a-4.[870] These changes are attributable to the proposed amendments to rule 17a-4 relating to the relationship summary as discussed in this proposing release and the decline in the number of registered broker-dealer respondents. The revised external cost to respondents is estimated at approximately $19.2 million, or a reduction of $1.3 million from the currently approved external cost burden of $20,520,000.[871]

G. Rule 151-3 under the Exchange Act

Proposed new rule 151-3 would require broker-dealers and their associated natural persons to prominently disclose that it is, or in the case of a natural person that such person is associated with a broker-dealer that is, registered with the Commission as a broker-dealer in print or electronic retail investor communications. For print communications, we propose to require that such registration status be displayed in a type size at least as large as and of a font style different from, but at least as prominent as, that used in the majority of the communication. In addition, such disclosure must be presented in the body of the communication and not in a footnote. For electronic communications, or in any publication by radio or television, we

867 *See supra* note 865.

868 *See supra* note 739.

869 1,042,866 hours – 976,350 hours = 66,516 hours.

870 $67,786,290 – $65,415,430 = $2,370,860.

871 3,841 registered broker-dealers as of December 31, 2017 x $5,000 per broker-dealer in record maintenance costs = $19,205,000. $20,520,000 - $19,205,000 = $1,315,000.

propose to require that such disclosure be presented in a manner reasonably calculated to draw retail investor attention to it.

Rule 151-3 contains a collection of information requirement. This collection of information would be found at [17 CFR 240.15l-3] and would be mandatory. The likely respondents to this information collection would be all broker-dealers and their associated natural persons that distribute print or electronic retail investor communications.

The Commission believes that the collection of information is necessary to provide retail investors and the Commission with information to better determine whether a communication is from a broker-dealer or investment adviser, and, for retail investors specifically, to allow them to better identify which type of firm is more appropriate for their specific investment needs. Additionally, by requiring an affirmative identification, retail investors would also be better informed whether a financial professional is an associated person of a broker-dealer rather than a supervised person of an investment adviser, allowing them to make a more informed choice as to which type of professional is appropriate for their financial goals.

1. Respondents: Broker-Dealers and Associated Natural Persons

Currently, there are 3,841 registered broker-dealers and 435,071 associated natural persons licensed with FINRA.[872] Of these registered broker-dealers, we estimate that approximately 74% or 2,857 distribute print or electronic retail investor communications[873] while 435,071 associated natural persons distribute print or electronic retail investor communications at

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872 The number of broker-dealers is as of Dec. 31, 2017. Such associated natural persons are registered as registered representatives with FINRA through Form U4 as of Dec. 31, 2017. We took the total 494,399 registered representatives across standalone broker-dealers, dually registered firms, and standalone investment advisers and isolated those registered representatives that act on behalf of standalone broker-dealers and dually registered firms (*i.e.* 88%). *See supra* Section IV.A.1.e, Economic Analysis: Registered Representatives of Broker-Dealers, Investment Advisers and Dually Registered Firms.

873 *See* Section IV.A, *supra* note 460 and accompanying text. As noted above, as of December 2017, 3,841 broker-dealers filed Form BD. Retail sales by broker-dealers were obtained from Form BR.

standalone broker-dealers or dually registered firms.[874] Of these broker-dealers that distribute print or electronic retail investor communications, 1,388 are large broker-dealers and 1,469 are small broker-dealers.[875] Accordingly, the Commission estimates that 2,857 broker-dealers and 435,071 associated natural persons would be required to comply with proposed rule 15l-3. For the purposes of this analysis of the paperwork burden associated with the proposed rules, the Commission preliminarily estimates that there would be approximately 2,857 broker-dealer respondents and 435,071 associated natural person respondents.[876]

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874 *See supra* Section IV.A.1.e, at Table 5. For the purposes of the Paperwork Reduction Act analysis applicable to proposed rules 15l-3 and 211h-1, we are defining a "dually registered firm" in the same manner as "dual registrant" is defined in the baseline of the Economic Analysis. *See supra* Section IV, note 453.

We assume for the purposes of this rule that all 435,071 registered representatives engage retail investors. This estimate is based on the following calculation: (494,399 total licensed registered representatives) x (12% (the percentage of pure investment adviser representatives)) = 59,328 representatives at standalone investment advisers. Then, to isolate the number of representatives at standalone broker-dealers and dually registered firms, subtract 59,328 from 494,399 = 435,071 retail-facing, licensed registered representatives at standalone broker-dealers or dually registered firms.

875 For the purposes of this proposed rule, we define large broker-dealers as those with total assets greater than 1 million and small broker-dealers as those with less than 1 million in total assets. *See* Table 1, Panel B *supra* Section IV.A.1.a. We note that this distinction differs from the distinction used for proposed rule 211h-1 below because historically we have used the number of employees rather than total assets to distinguish small and large investment advisers. *See cf.* Rules Implementing Amendments to the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3221 (Jun. 22, 2011), at n.727 ("Release 3221"). Additionally, we believe that because broker-dealer services encompass a small set of large broker-dealers and thousands of smaller broker-dealers competing for niche or regional segments of the market, the number of employees would not provide the best estimate for how firms would be impacted by our proposed rule based on the number of communications produced. Instead, we believe that total assets properly account for the varying sizes of these smaller broker-dealers and are a better indicator as to how many communications would be impacted in proportion to a firm's size. More specifically, we assume that the greater the total assets, the larger the firm and associated number of customer accounts which in turn would lead to a greater number of communications with retail investors.

876 We note that we are not analyzing new broker-dealers or associated natural persons because there has been a downward trend in broker-dealer registration and the number of associated natural persons has not shown signs of a noticeable increase over the past few years. From 2016 through 2018 the number of broker-dealers registered with the Commission decreased by 160. (4064 – 3904) = 160. *See also* FINRA Statistics, *available at* https://www.finra.org/newsroom/statistics#reps.

2. Initial and Annual Burdens

We estimate that the initial one time burden for complying with the disclosure requirements would be 72 hours per large broker-dealer[877] and 15 hours per small broker-dealer.[878] We note that we are staging the compliance date to ensure that firms can phase out certain older communications from circulation through the regular business lifecycle rather than having to retroactively change them.[879] As a result of this staged compliance, our burden estimates do not reflect the burdens that would have been imposed had these firms had to replace all outstanding communications.

Aside from certain anticipated outside legal costs, as discussed below, we preliminary estimate that to comply with our proposed rule with respect to print communications,[880] broker-dealers would need to review their communications, identify which would need to be amended, make the changes, and verify that all firm communications comply with the rule's requirements including its technical specifications such as the type size, font, and prominence. Therefore, for existing print communications for large broker-dealers, we preliminarily estimate that the total burden for broker-dealers would be 8 hours for compliance and business operations personnel to review, identify, and make changes across all print communications.[881] For smaller broker-

877 (8 hours for print communications per large broker-dealer + 64 hours for electronic communications per large broker-dealer).

878 (5 hours for print communications per small broker-dealer + 10 hours for electronic communications per small broker-dealer).

879 Similarly, we are not requiring firms to send new communications to replace all older print communications as this would be overly burdensome and costly for firms.

880 Such communications could include business cards, letterheads, newspaper advertisements, and article reprints from an unaffiliated magazine or newspaper.

881 This estimate is based upon staff experience and industry sources more generally. *See e.g*. Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Amend FINRA Rule 2210, Exchange Act Release No. 34-75377 (Jul. 7, 2015), at Economic Impact Assessment ("FINRA 2015-22 Notice") (stating with reference to adding BrokerCheck links to mid-size and smaller firm communications, which we believe is analogous to the manual changes made to print

dealers, we preliminarily estimate that the total burden for broker-dealers would be 5 hours for compliance and business operations personnel to review, identify, and make changes across all print communications.[882] We note that there is a difference between large broker-dealers and smaller broker-dealers. We assume that large broker-dealers will have to review, identify and change more print communications and in turn have their compliance staff verify more print communications as being compliant with our proposed rule as compared to small broker-dealers which will have fewer print communications.

With respect to electronic communications,[883] we preliminarily anticipate that it would take large broker-dealers approximately 64 hours[884] to review, identify and make the required updates coupled with verifying that such communications (present and future) would be compliant with the proposed rule. Our estimates take into account that larger firms likely have

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communications, that "mid-size and small members typically have less complex websites, which they manage and maintain with nontechnical staff. These members would use personnel in non-technical roles to accomplish the required updates to their websites…. [I]t would take mid-size or small members approximately eight hours of non-technical staffs' time to make the required updates….").

To compute the 8 hours internal initial burden we assume 2 hours by compliance personnel and 6 hours by business operations personnel of the broker-dealer.

882 This estimate is based upon staff experience and industry sources more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881. To compute the 5 hours internal initial burden we assume 1 hour by compliance personnel and 4 hours by business operations personnel of the broker-dealer.

883 We believe such communications could include websites, smart phone apps, social media, emails, and blogs.

884 This estimate is based upon staff experience and industry sources more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881. ("These estimates are based on FINRA's assumption that large members typically have full-featured websites that dynamically generate webpages based on data and logic. The technology personnel at these members would be required to update the underlying information in order to automate the implementation of references and hyperlinks to BrokerCheck across all applicable webpages. FINRA estimates that on average it would take large members approximately 60 hours of technology staffs' time to make the required updates…."). To compute the 64 hours internal initial burden we assume 4 hours by compliance personnel and 60 hours by business operations and information technology personnel of the broker-dealer.

full-featured websites that generate other webpages based on complex system code and logic.[885] In order to make changes to comply with our proposed rule, we assume that business operations and information technology personnel would likely be required to update the underlying code and logic to automate the implementation of the required language to populate across all associated electronic media. Additionally, we assume that these teams would need to test to ensure that such changes were implemented correctly.

With respect to smaller broker-dealers, we preliminarily anticipate that it would take approximately 10 hours[886] to review, identify and make the required updates coupled with verifying that such communications (present and future) would be compliant with the proposed rule. Our estimate for smaller broker-dealers assumes that smaller broker-dealers have fewer electronic communications that would be subject to our proposed rule as compared to larger firms, resulting in a lower burden preliminary estimate.

We preliminarily estimate that the total initial burden for broker-dealers is 121,971 hours.[887] We preliminarily estimate a cost of approximately $33,179,514 for broker-dealers.[888]

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885 This is based upon staff experience and industry sources more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note (discussing the burdens associated with the inclusion of a BrokerCheck reference and hyperlink across all firm communications for certain firms).

886 This estimate is based upon staff experience and industry sources more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881 (stating with reference to adding BrokerCheck links to firm communications that "mid-size and small members typically have less complex websites, which they manage and maintain with nontechnical staff. These members would use personnel in non-technical roles to accomplish the required updates to their websites…. [I]t would take mid-size or small members approximately eight hours of non-technical staffs' time to make the required updates….").

To compute the 10 hours internal initial burden, we assume 2 hours by compliance personnel and 8 hours by business operations and information technology personnel of the broker-dealer.

887 (8 hours for print communications per large broker-dealer + 64 hours for electronic communications per large broker-dealers) = 72 hours per large broker-dealer. (72 hours x 1,388 large broker-dealers) = 99,936 total initial burden for large broker-dealers.

(5 hours for print communications per small broker-dealer + 10 hours for electronic communications per small broker-dealer) = 15 hours per small broker-dealer. (15 hours x 1,469 small broker-dealers) = 22,035 total initial burden for small broker-dealers.

This would be an annual average burden of 43 hours per broker-dealer[889] (as monetized, is an average annual burden per broker-dealer of $11,613).[890]

We further preliminarily anticipate that associated natural persons would have an initial one-time burden of 0.5 hours for each associated natural person respondent to review, identify,

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(99,936 total initial burden large broker-dealers + 22,035 total initial burden small broker-dealers) = 121,971 total broker-dealer initial burden.

888 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270. The average technology and business rate is ($268 business rate + $270 technology rate) / 2 = $269 average rate.

This figure was calculated as follows: (6 compliance hours x $298 compliance rate) + (66 technology/business hours x $269 averaged technology/business rate) x 1,388 large broker-dealers = $27,124,296 total initial costs for large broker-dealers.

(3 compliance hours x $298 compliance rate) + (12 technology/business hours x $269 averaged technology/business rate) x 1,469 small broker-dealers = $6,055,218 total initial costs for small broker-dealers.

$27,124,296 total initial cost for large broker-dealers + $6,055,218 total initial cost for small broker-dealers = $33,179,514 total initial costs for all broker-dealers.

889 (8 hours for print communications per large broker-dealer + 64 hours for electronic communications per large broker-dealers) = 72 hours per large broker-dealer. (72 hours x 1,388 large broker-dealers) = 99,936 total initial burden for large broker-dealers.

(5 hours for print communications per small broker-dealer + 10 hours for electronic communications per small broker-dealer) = 15 hours per small broker-dealer. (15 hours x 1,469 small broker-dealers) = 22,035 total initial burden for small broker-dealers.

99,936 total initial burden large broker-dealers + 22,035 total initial burden small broker-dealers = 121,971 total broker-dealer initial burden / 2,857 total broker-dealers = 43 total initial burden per broker-dealer.

890 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270. The average technology and business rate is ($268 business rate + $270 technology rate) / 2 = $269 average rate.

This figure was calculated as follows: (6 compliance hours x $298 compliance rate) + (66 technology/business hours x $269 averaged technology/business rate) x 1,388 large broker-dealers = $27,124,296 total initial costs for large broker-dealers.

(3 compliance hours x $298 compliance rate) + (12 technology/business hours x $269 averaged technology/business rate) x 1,469 small broker-dealers = $6,055,218 total initial costs for small broker-dealers.

$27,124,296 total initial cost for large broker-dealers + $6,055,218 total initial cost for small broker-dealers = $33,179,514 total initial costs for all broker-dealers / 2,857 total number of broker-dealers=$11,613 total initial cost per broker-dealer.

and make changes to their individual communications, both print and electronic.[891] Based on staff experience, we anticipate that many firms will make many communication changes for their associated natural persons, including their business cards and letterheads, leaving only certain responsibilities to the individual such as changes to their individual social media profile(s) and email signatures. Therefore, we preliminarily estimate that the total initial one-time burden for associated natural persons is 217,536 hours.[892] We preliminarily estimate a monetized cost of approximately $31,107,576.50 for associated natural persons.[893] This would be an annual average burden of 0.5 hours per associated natural person[894] (as monetized, is an average annual

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891 This estimate is based upon staff experience. *See e.g.* Custody of Funds or Securities of Clients by Investment Advisers, Investment Advisers Act Release No. 2968 (Dec. 30, 2009) ("Release 2968") ("We further estimate that the adviser will spend 10 minutes per client drafting and sending the notice."); Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47 ("we estimate, as we did in the proposing release, that rule 498 will impose a ½ hour burden per portfolio annually associated with the compilation of the additional information required on a cover page or at the beginning of the Summary Prospectus. Rule 498 also imposes annual hour burdens associated with the posting of a fund's Summary Prospectus, statutory prospectus, SAI, and most recent report to shareholders on an Internet website. We estimate that the average hour burden for one portfolio to comply with the Internet website posting requirements will be approximately one hour annually.").

892 (0.5 hours x 435,071 associated natural persons) = 217,536 total initial burden for associated natural persons.

893 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per associated natural person.

(0.5 x $143 total cost per associated natural person x 435,071 associated natural persons) = $31,107,576.50 total initial cost for associated natural persons.

894 (0.5 hours x 435,071 associated natural persons) = 217,536 total initial burden for associated natural persons.

(217,536 total initial burden / 435,071 total associated natural persons) = 0.5 total initial burden per associated natural person.

burden per associated natural person of $71.50).[895]

Aside from the internal initial burden, we anticipate that there will be certain associated outside costs as well. We believe that broker-dealers and their associated natural persons may engage outside counsel to assist them in understanding our proposed rule should it be adopted.[896] We assume that the amount of outsourced legal assistance would vary among various sizes of broker-dealers and their number of associated natural persons. As a result, we preliminarily estimate that large broker-dealers together with their associated natural persons may initially outsource approximately 8 hours of legal time in order to understand the implications of our proposed rule, including which communications are subject to the proposed rule and how best to comply with the technical specifications.[897] For small broker-dealers, we anticipate that such

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895 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per associated natural person.

(0.5 x $143 total cost per associated natural person x 435,071 associated natural persons) = $31,107,576.50 total initial cost for associated natural persons.

($31,107,576.50 total initial cost for associated natural persons / 435,071 total number of associated natural persons) = $71.50 total initial cost per associated natural person.

896 We are assuming that associated natural persons would not independently seek outside counsel and would instead rely on the advice received from outside counsel to the firm. Therefore, we are not including a separate estimate for associated natural persons.

897 This estimate is based upon staff experience. *See e.g*. Disclosure of Order Handling Information Proposed Rule, Securities Exchange Act Release No. 34-78309 (July 13, 2016) ("Release 34-78309") (estimating 4 hours for legal burden "to assign each order routing strategy for institutional orders into passive, neutral, and aggressive categories and establish and document its specific methodologies for assigning order routing strategies as required by Rule 606(b)(3)(v)"); Regulation of NMS Stock Alternative Trading Systems Proposed Rule, Securities Exchange Act Release No. 34-76474 (Nov. 18, 2015) ("Release 34-76474") (estimating 7 legal hours "to put in writing its safeguards and procedures to protect subscribers' confidential trading information and the oversight procedures to ensure such safeguards and procedures are followed….").

firms will outsource 4 hours of legal time.[898] Our preliminary estimates take into account that large firms have more communications affected by our proposed rule and more associated natural persons to supervise than smaller firms. We estimate initial outside legal costs associated with the proposed rule of $8,014,560 for broker-dealers[899] or $2,805 per broker-dealer.[900]

Additionally, we anticipate that firms will also have one-time outside cost associated with the cost of printing new communications including new business cards, envelopes, pitch books, and letterheads. As part of these costs, we anticipate that both large and small broker-dealers will have to work with printers to set the disclosure on, for example, business cards. We estimate initial costs to amend certain communications associated with the proposed rule of $617,848,307 for broker-dealers[901] (or $216,258 per broker-dealer).[902] We assume that because small broker-dealers have fewer associated natural persons there will be less communications that will require printing.

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898 This estimate is based upon staff experience. *See supra* note 897.

899 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for legal services is $472/hour.

($472 x 8 legal hours = $3,776 x 1,388 large broker-dealers = $5,241,088) + ($472 x 4 legal hours = $1,888 x 1,469 small broker-dealers = $2,773,472).

($5,241,088 large broker-dealers + $2,773,472 small broker-dealers) = $8,014,560 total cost.

900 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for legal services is $472/hour.

($472 x 8 legal hours = $3,776 x 1,388 large broker-dealers = $5,241,088) + ($472 x 4 legal hours = $1,888 x 1,469 small broker-dealers = $2,773,472).

$5,241,088 large broker-dealers + $2,773,472 small broker-dealers = $8,014,560 total cost/ 2,857 broker-dealers = $2,805 total cost per broker-dealer.

901 Our estimates are based on staff experience and industry sources. In particular, staff factored in its cost estimate the costs associated with printing envelopes, pitch books, letterheads, and business cards. For large broker-dealers, the staff assumes a printing cost of $445,121. For small broker-dealers, the staff assumes a printing cost of $20,359.

($445,121 x 1,388 large broker-dealers = $617,827,948) + ($20,359 x 1,469 small broker-dealers = $29,907,371) = $617,848,307 total broker-dealer outside costs.

902 ($445,121 x 1,388 large broker-dealers = $617,827,948) + ($20,359 x 1,469 small broker-dealers = $29,907,371) = $617,848,307 total broker-dealer outside costs / 2,857 broker-dealers = $216,258 total cost per broker-dealer.

For the ongoing burden of new communications for broker-dealers, we preliminarily estimate that the burden for legal, compliance, business operations, and technology services for adding a registration status statement would be 0.5 hours annual hours per broker-dealer.[903] We anticipate that broker-dealers will need to add the registration disclosure to each new communication which they create, however we anticipate the burdens associated with this task to be minimal and therefore we do not believe there is a material difference between large and small broker-dealers.[904] We preliminarily estimate that the total ongoing annual aggregate burden for broker-dealers is 1,429 hours.[905] We preliminarily estimate a total ongoing monetized cost of approximately $204,275.50 for broker-dealers.[906] This would be an annual average

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903 This estimate is based upon staff experience. *See e.g*. Release 2968, *supra* note 891; Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47.

In this estimate we are not calculating the print and technological associated burdens of updating communications which we analyzed earlier as we are assuming those burdens to be a one-time initial burden for a firm seeking compliance with the proposed rule.

904 Our assumption of no material difference between large and small rests on the fact that all major systems changes would already have been implemented as part of the initial one-time burden. Therefore, any new electronic communications would have the disclosure statement required by our proposed rule built in at the outset which should take minimal time rather than having to retroactively insert it into the systems logic which is a more onerous task. We note that such communications will need to be reviewed by compliance staff for compliance with applicable securities laws and associated self-regulatory agency rules, including FINRA Rule 2210. We anticipate that compliance with proposed rule 151-3's requirements will be reviewed as part of this larger compliance check.

905 (0.5 hours x 2,857 broker-dealers) = 1,429 total ongoing burden for broker-dealers.

906 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per broker-dealer.

(0.5 hours x $143 total cost per broker-dealer x 2,857 broker-dealers) = $204,275.50 total ongoing cost for broker-dealers.

burden of 0.5 hours per broker-dealer[907] (as monetized, is an average annual burden per broker-dealer of $71.50).[908]

For the ongoing burden of new communications for associated natural persons of a broker-dealer, we preliminarily estimate that the burden for compliance, business operations, and technology services for adding a registration status statement would be 0.5 hours.[909] Therefore, we preliminarily estimate that the total ongoing annual aggregate burden for associated natural persons is 217,536 hours.[910] We preliminarily estimate a total ongoing monetized cost of approximately $31,107,576.50 for associated natural persons.[911] This would be an ongoing

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907 (0.5 hours x 2,857 broker-dealers) = 1,429 total ongoing burden for broker-dealers.

(1,429 total ongoing burden for broker-dealers / 2,857 total broker-dealers) = 0.5 total initial burden per broker-dealer.

908 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per broker-dealer.

(0.5 hours x $143 total cost per broker-dealer x 2,857 broker-dealers) = $204,275.50 total ongoing cost for broker-dealers / 2,857 total number of broker-dealers = $71.50 total ongoing cost per broker-dealer.

909 This estimate is based upon staff experience. *See e.g.* Release 2968, *supra* note 891; Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47.

In this estimate we are not calculating the print and technological associated burdens of updating communications which we analyzed earlier as we are assuming those burdens to be a one-time initial burden for an associated natural person of a broker-dealer seeking compliance with the proposed rule.

910 (0.5 hours x 435,071 associated natural persons) = 217,536 total ongoing burden for associated natural persons.

911 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

annual average burden of 0.5 hours per associated natural person[912] (as monetized, is an average ongoing annual burden per associated natural person of $71.50).[913]

H. Rule 211h-1 under the Advisers Act

Proposed rule 211h-1 would require investment advisers registered under section 203 and their supervised persons to prominently disclose that it is, or in the case of supervised persons that such persons are supervised by an investment adviser that is, registered with the Commission as an investment adviser in print or electronic retail investor communications. For print communications, we propose to require that such registration status be displayed in a type size at least as large as and of a font style different from, but at least as prominent as, that used in the majority of the communication. In addition, such disclosure must be presented in the body of the communication and not in a footnote. For electronic communications, or in any publication

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($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per associated natural person.

(0.5 hours x $143 total cost per associated natural person x 435,071 associated natural person) = $31,107,576.50 total ongoing cost for associated natural persons.

912 (0.5 hours x 435,071 associated natural persons) = 217,536 total ongoing annual burden for associated natural persons.

(217,536 total ongoing burden / 435,071 total associated natural persons) = 0.5 total ongoing annual burden per associated natural person.

913 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per associated natural person.

(0.5 hours x $143 total cost per associated natural person x 435,071 associated natural person) = $31,107,576.50 total ongoing cost for associated natural persons / 435,071 total number of associated natural persons) = $71.50 total ongoing annual cost per associated natural person.

by radio or television, we propose to require that such disclosure be presented in a manner reasonably calculated to draw retail investor attention to it. This collection of information would be found at [17 CFR 240.15l-3] and would be mandatory. The likely respondents to this information collection would be all investment advisers and their supervised persons that distribute print or electronic retail investor communications.

The Commission believes that the collection of information is necessary to provide retail investors and the Commission with information to better determine whether a communication is from a broker-dealer or investment adviser, and, for retail investors specifically, to allow them to better identify which type of firm is more appropriate for their specific investment needs. Additionally, by requiring an affirmative identification, retail investors would also be better informed whether a financial professional is a supervised person of an investment adviser rather than an associated person of a broker-dealer. For similar reasons, we believe that because retail investors interact with a firm primarily through financial professionals, it is important that financial professionals disclose the firm type with which they are associated.

1. Respondents: Investment Advisers and Supervised Persons

Currently, there are 12,721 registered investment advisers and approximately 942,215 supervised persons.[914] Of these, 7,625 investment advisers distribute print or electronic retail investor communications while 245,408 supervised persons distribute print or electronic retail investor communications at standalone investment advisers or dually registered firms.[915]

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914 The investment adviser and supervised person numbers are as of December 31, 2017. *See supra* Section IV.A.1.b, at Table 3, Panel A. We note that our estimate of supervised persons is based on those supervised persons identified in the baseline in the Economic Analysis. *See* Section IV.A.1.e, at Table 6.

915 We estimate the number of supervised persons who distribute print or electronic retail investor communications using several data points. First, we analyzed those supervised persons who only hold a series 65 at a dual registrant or an investment adviser firm, totaling 27,879. Next we analyzed those supervised persons at dual registrants or investment advisers holding a combination of either a series 6 and

Additionally, of these investment advisers 2,738 are large advisers and 4,887 are small advisers.[916] Accordingly, the Commission estimates that 7,625 investment advisers and 245,408 supervised persons would be required to comply with proposed rule 211h-1. There are also 477 new SEC registered investment advisers per year on average and 3,000 new supervised persons per year.[917]

2. Initial and Annual Burdens

We estimate that the initial one-time burden for complying with the disclosure requirements would be 72 hours per large investment adviser[918] and 15 hours per small investment adviser.[919] We note that we are staging the compliance date to ensure that firms can phase out certain older communications from circulation through the regular business lifecycle rather than having to retroactively change them.[920] As a result of this staged compliance, our

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65 or a series 7 and 65, totaling 15,381 and 172,304 respectively. Finally, we analyzed those supervised persons at dual registrants or investment advisers holding a series 6, 7, and 65, totaling 29,944. (27,879 + 15,281 + 172,304 + 29,944) = 245,408 total supervised persons who engage retail investors through print or electronic communications. We note that our estimate does not reflect supervised persons who hold various designations (*e.g.* Chartered Financial Analyst) in lieu of the licenses we used to identify supervised persons of investment advisers who distribute print or electronic retail investor communications. Finally, our estimate does not employ rounding as compared to Table 6 in the Economic Analysis Baseline. *See* Table 6: Number of Employees at Retail Facing Firms who are Registered Representatives, Investment Adviser Representatives, or Both, Section I.V.A.1.e. These numbers are as of December 31, 2017.

916 For purposes of this estimate, we categorize small advisers as advisers with 10 or fewer employees and large advisers as those with 10 or more employees. *See cf.* Release 3221, *supra* note 875, at n.727.

917 The number of new investment advisers is calculated by looking at the number of new advisers in 2016 and 2017 and then isolating the number each year that services retail investors. (455 for 2016 + 499 for 2017) / 2) = 477.

The number of new supervised persons is calculated by looking at the difference in the number of supervised persons in 2017 as compared to 2016 at firms which service retail investors.

918 (8 hours for print communications per broker-dealer + 64 hours for electronic communications per broker-dealer).

919 (5 hours for print communications per broker-dealer + 10 hours for electronic communications per broker-dealer).

920 Similarly, we are not requiring firms to send new communications to replace all older print communications as this would be overly burdensome and costly for firms.

burden estimates do not reflect the burdens that would have been imposed had these firms had to replace all outstanding communications.

Aside from certain anticipated outside legal costs, as discussed below, we preliminary estimate that to comply with our proposed rule with respect to print communications,[921] investment advisers would need to review their communications, identify which would need to be amended, make the changes, and verify that all firm communications comply with the rule's requirements including its technical specifications such as the type size, font, and prominence. Our preliminary estimates differ for large and small investment advisers. We drew these distinctions because we assume that the larger an adviser is the more communications it would need to review, identify and change and in turn have its compliance staff verify that such communications are compliant with our proposed rule.

For existing print communications for large investment advisers we preliminarily estimate that the total burden for investment advisers would be 8 hours for compliance and business operations personnel to review, identify, and make changes across all print communications.[922] For small investment advisers, we preliminarily estimate that the total burden for investment advisers would be 5 hours for compliance and business operations personnel to review, identify, and make changes across all print communications.[923]

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921 Such communications could include business cards, letterheads, newspaper advertisements, and article reprints from an unaffiliated magazines or newspaper.

922 This estimate is based upon staff experience and industry sources more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881.

To compute the 8 hours internal initial burden we assume 2 hours by compliance personnel and 6 hours by business operations personnel of the broker-dealer.

923 This estimate is based upon staff experience and industry materials more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881. To compute the 5 hours internal initial burden we assume 1 hour by compliance personnel and 4 hours by business operations personnel of the investment adviser.

With respect to electronic communications[924] we preliminarily anticipate that it would take large investment advisers approximately 64 hours[925] to review, identify and make the required updates coupled with verifying that such communications (present and future) would be compliant with the proposed rule. Our estimates take into account that larger firms likely have full-featured websites that generate other webpages based on complex system code and logic.[926] In order to make changes to comply with our proposed rule, we assume that business operations and information technology personnel would likely be required to update the underlying code and logic to automate the implementation of the required language to populate across all associated electronic media. Additionally, we assume that these teams would need to test to ensure that such changes were implemented correctly.

With respect to small investment advisers, we preliminarily anticipate that it would take approximately 10 hours[927] to review, identify and make the required updates coupled with verifying that such communications (present and future) would be compliant with the proposed rule. Our estimate for small investment advisers assumes that small investment advisers have fewer electronic communications that would be subject to our proposed rule as compared to larger firms, resulting in a lower burden preliminary estimate.

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924 We believe such communications could include websites, smart phone apps, social media, emails, and blogs.

925 This estimate is based upon staff experience and industry materials more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881. To compute the 64 hours internal initial burden we assume 4 hours by compliance personnel and 60 hours by business operations and information technology personnel of the investment adviser.

926 This is based upon staff experience and industry materials more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881 (discussing the burdens associated with the inclusion of a BrokerCheck reference and hyperlink across all firm communications for certain firms).

927 This estimate is based upon staff experience and industry materials more generally. *See e.g*. FINRA 2015-22 Notice, *supra* note 881.

To compute the 10 hours internal initial burden, we assume 2 hours by compliance personnel and 8 hours by business operations and information technology personnel of the investment adviser.

We preliminarily estimate that the total initial burden for investment advisers is 270,441 hours.[928] We preliminarily estimate a cost of approximately $73,650,210 for investment advisers.[929] This would be an annual average burden of 35 hours per investment adviser[930] (as monetized, an annual average cost of $9,659 per investment adviser).[931]

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928 (8 hours for print communications per large investment adviser + 64 hours for electronic communications per large investment adviser) = 72 hours per large investment adviser.

(72 hours x 2,738 large investment advisers) = 197,136 total initial burden for large investment advisers.

(5 hours for print communications per small investment adviser + 10 hours for electronic communications per small investment adviser) = 15 hours per small investment adviser. (15 hours x 4887 small investment advisers) = 73,305 total initial burden for small investment advisers.

(197,136 total burden large investment advisers + 73,305 total burden small investment advisers) = 270,441 hours.

929 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services in the securities industry is $298, for business services is $268, and for technology services is $270. The average technology and business rate is ($270 technology rate + $268 business rate) / 2 = $269 average rate.

This figure was calculated as follows: (6 compliance hours x $298 compliance rate) + (66 technology/business hours x $269 averaged technology/business rate) x 2,738 large investment advisers = $53,505,996 total initial costs for large investment advisers.

(3 compliance hours x $298 compliance rate) + (12 technology/business hours x $269 averaged technology/business rate) x 4,887 small investment advisers = $20,144,214 total initial costs for small investment advisers.

($53,505,996 total initial costs for large investment advisers + $20,144,214 total initial costs for small investment advisers) = $73,650,210 total initial costs for investment advisers.

930 (8 hours for print communications per large investment adviser + 64 hours for electronic communications per large investment adviser) = 72 hours per large investment adviser.

(72 hours x 2,738 large investment advisers) = 197,136 total initial burden for large investment advisers.

(5 hours for print communications per small investment advisers + 10 hours for electronic communications per small investment adviser) = 15 hours per small investment adviser. (15 hours x 4887 small investment advisers) = 73,305 total initial burden for small investment advisers.

197,136 total burden large investment advisers + 73,305 total burden small investment advisers = 270,441 hours / 7,625 total investment advisers = 35 hours average initial burden per investment adviser.

931 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270. The average technology and business rate is ($268 business rate + $270 technology rate) / 2 = $269 average rate.

This figure was calculated as follows: (6 compliance hours x $298 compliance rate) + (66 technology/business hours x $269 averaged technology/business rate) x 2,738 large investment advisers = $53,505,996 total initial costs for large investment advisers.

We further preliminarily anticipate that supervised persons would have an initial burden of 0.5 hours for each supervised person respondent to review, identify, and make changes to their individual communications, both print and electronic.[932] Based on staff experience, we anticipate that many firms will make many communication changes for their supervised persons, including their business cards and letterheads, leaving only certain responsibilities to the individual such as changes to their individual social media profile(s) and email signatures. Therefore, we preliminarily estimate that the total initial one-time burden for supervised persons is 122,704 hours.[933] We preliminarily estimate a monetized cost of approximately $17,546,672 for supervised persons.[934] This would be an annual average burden of 0.5 hours per supervised person[935] (as monetized, is an annual average cost of $71.50 per supervised person).[936]

(3 compliance hours x $298 compliance rate) + (12 technology/business hours x $269 averaged technology/business rate) x 4,887 small investment advisers = $20,144,214 total initial costs for small investment advisers.

$53,505,996 total initial cost large investment advisers + $20,144,214 total initial costs small investment advisers = $73,650,210 total initial cost investment advisers / 7,625 total number of investment advisers = $9,659 average initial cost per investment adviser.

932 This estimate is based upon staff experience. *See e.g*. Release 2968, *supra* note 891; Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47.

933 (0.5 hours x 245,408 supervised persons) = 122,704 total initial burden for supervised persons.

934 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per supervised person.

(0.5 hours x $143 total cost per supervised person x 245,408 supervised persons) = $17,546,672 total initial cost for supervised persons.

935 (0.5 hours x 245,408 supervised persons) = 122,704 total initial burden for supervised persons.

(122,704 total initial burden for supervised persons / 245,408 total supervised persons) = 0.5 hours average initial burden per investment adviser.

Aside from the internal initial burden, we anticipate that there would be certain associated outside costs as well. We believe that investment advisers and their supervised persons may engage outside counsel to assist them in understanding our proposed rule should it be adopted.[937] We assume that the amount of outsourced legal assistance would vary among various sizes of investment advisers and their number of supervised persons. As a result, we preliminarily estimate that large investment advisers together with their supervised persons may initially outsource approximately 8 hours of legal time in order to understand the implications of our proposed rule and how best to comply with the technical specifications.[938] For small investment advisers, we anticipate that such firms will outsource 4 hours of legal time.[939] The hour differences in our preliminary estimates take into account that larger firms have more communications affected by our proposed rule and more supervised persons to supervise than small firms. We estimate initial outside legal costs associated with the proposed rule of

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936 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per supervised person.

(0.5 hours x $143 total cost per supervised person x 245,408 supervised persons) = $17,546,672 total initial cost for supervised persons / 245,408 total number of supervised persons) = $71.50 average initial cost per supervised person.

937 We are assuming that supervised persons would not independently seek outside counsel and would instead rely on the advice received from outside counsel to the firm. Therefore, we are not including a separate estimate for supervised persons.

938 This estimate is based upon staff experience. *See e.g*. Release 34-78309, *supra* note 897; Release 34-76474, *supra* note 897.

939 This estimate is based upon staff experience. *See supra* note 938.

$19,565,344 for investment advisers[940] (or $2,566 on average per investment adviser.)[941]

Additionally, we anticipate that firms will also have one-time outside costs associated with the cost of printing new communications including new business cards, envelopes, pitch books, and letterheads. As part of these costs, we anticipate that both large and small investment advisers will have to work with printers to set the disclosure on, for example, business cards. We estimate initial costs to amend certain communications associated with the proposed rule of $346,787,187 for investment advisers[942] (or $45,480 per investment adviser.)[943] We assume that because small investment advisers have fewer supervised persons there will be less communications that will require printing.

For the ongoing burden of new communications for investment advisers, we preliminarily estimate that the burden for compliance, business operations, and technology services for adding

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940 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for legal services is $472/hour.

($472 x 8 legal hours) = $3,776 x 2,738 large investment advisers = $10,338,688.

($472 x 4 legal hours) = $1,888 x 4,887 small investment advisers = $9,226,656.

($10,338,688 total large investment advisers costs + $9,226,656 total small investment advisers costs) = $19,565,344.

941 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for legal services is $472/hour.

($472 x 8 legal hours) = $3,776 x 2,738 large investment advisers = $10,338,688.

($472 x 4 legal hours) = $1,888 x 4,887 small investment advisers = $9,226,656.

$10,338,688 total large investment advisers costs + $9,226,656 total small investment advisers costs = $19,565,344 /7625 total investment advisers = $2,566 total cost per investment adviser.

942 Our estimates are based on staff experience and industry materials. In particular, staff factored in its cost estimate the costs associated with printing envelopes, pitch books, letter heads, and business cards. For large investment advisers, we assume printing costs of $65,973. For small investment advisers, we assume printing costs of $33,999.

($65,973 x 2,738 large investment advisers = $180,634,074) + ($33,999 x 4,887 small investment advisers = $166,153,113) = $346,787,187 total investment adviser outside costs.

943 ($65,973 x 2,738 large investment advisers = $180,634,074) + ($33,999 x 4,887 small investment advisers = $166,153,113) = $346,787,187 total investment adviser outside costs / 7,625 investment advisers =$45,480 total cost per investment adviser.

a registration status statement would be 0.5 hours annual hours per investment adviser.[944] We anticipate that investment advisers will need to add the registration disclosure to each new communication which they create, however we anticipate the burdens associated with this task to be minimal and therefore we do not believe there is a material difference between large and small investment advisers.[945] We preliminarily estimate that the total ongoing annual aggregate burden for investment advisers is 3,812.50 hours.[946] We preliminarily estimate a total ongoing monetized cost of approximately $545,187.50 for investment advisers.[947] This would be an annual average burden of 0.5 hours per investment advisers[948] (as monetized, is an annual

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944 This estimate is based upon staff experience. *See e.g*. Release 2968, *supra* note 891; Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47.

In this estimate we are not calculating the print and technological associated burdens of updating communications which we analyzed earlier as we are assuming those burdens to be a one-time initial burden for a firm seeking compliance with the proposed rule.

945 Our assumption of no material difference between large and small investment advisers rests on the fact that all major systems changes would already have been implemented as part of the initial burden. Therefore, any new electronic communications would have the disclosure statement required by our proposed rule built in at the outset which should take minimal time rather than having to retroactively insert it into the systems logic which is a more onerous task. We note that such communications would likely be reviewed by compliance staff for compliance with applicable securities laws including rule 206(4)-1 of the Advisers Act. We anticipate that compliance with proposed rule 211h-1's requirements would be reviewed as part of this larger compliance check.

946 (0.5 hours x 7,625 investment advisers) = 3,812.50 total ongoing burden for investment advisers.

947 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per investment adviser.

(0.5 hours x $143 total cost per investment adviser x 7,625 investment advisers) = $545,187.50 total ongoing cost for investment advisers.

948 (0.5 hours x 7,625 investment advisers) = 3,812.50 total ongoing burden for investment advisers.

(3,812.5 / 7,625 total investment advisers) = 0.5 hours average initial burden per investment adviser.

average cost of $71.50 per investment adviser).[949]

For the ongoing burden of new communications for supervised persons of an investment adviser, we preliminarily estimate that the burden for compliance, business operations, and technology services for adding a registration status statement would be 0.5 hours.[950] Therefore, we preliminarily estimate that the total ongoing annual aggregate burden for supervised persons is 122,704 hours.[951] We preliminarily estimate a total ongoing monetized cost of approximately $17,546,672 for supervised persons.[952] This would be an annual average burden of 0.5 hours per supervised person[953] (as monetized, is an annual average cost of $71.50 per supervised person).[954]

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949 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per investment adviser.

(0.5 hours x $143 total cost per investment adviser x 7,625 investment advisers) = $545,187.50 total ongoing cost for investment advisers / 7,625 total number of investment advisers = $71.50 average annual ongoing cost per investment adviser.

950 This estimate is based upon staff experience. *See e.g*. Release 2968, *supra* note 891; Enhanced Mutual Fund Disclosure Adopting Release, *supra* note 47.

In this estimate we are not calculating the print and technological associated burdens of updating communications which we analyzed earlier as we are assuming those burdens to be a one-time initial burden for a supervised person of an investment adviser seeking compliance with the proposed rule.

951 (0.5 hours x 245,408 supervised persons) = 122,704 total ongoing burden for supervised persons.

952 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

Additionally, we believe that any new investment advisers and their supervised persons would likely only incur the same ongoing annual burden estimate rather than the initial burden because they would incorporate the proposed registration status in all communications at their inception and not have to conduct a review and identification of outstanding communications nor make changes to their already existing communications. We do anticipate that such persons would also incur similar outside legal costs, depending on their size, as discussed above. We do not believe that such new investment advisers would incur outside printing costs as a result of our proposed rule because these new firms would have their print communications produced with the appropriate disclosure initially as part of other materials they seek to have printed. Therefore, we preliminarily estimate that the total burden for new investment advisers is 238.50 hours.[955] Additionally, we preliminarily estimate a cost of approximately $34,105.50 for new

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$51 + $46 + $46 = $143 total cost per supervised person.

(0.5 hours x $143 total cost per supervised person x 245,408 supervised persons) = $17,546,672 total ongoing cost for supervised persons.

953 (0.5 hours x 245,408 supervised persons) = 122,704 total ongoing annual burden for supervised persons.

(122,704 total initial burden for supervised persons / 245,408 total supervised persons) = 0.5 hours average ongoing annual burden per supervised person.

954 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per supervised person.

(0.5 hours x $143 total cost per supervised person x 245,408 supervised persons) = $17,546,672 total ongoing cost for supervised persons / 245,408 total number of supervised persons = $71.50 average ongoing annual cost per supervised person.

955 (0.5 hours x 477 new investment advisers) = 238.50 total burden for new investment advisers.

investment advisers.[956] This would be an initial average burden of 0.5 hours per new investment adviser[957] (as monetized, is an initial average cost of $71.50 per new investment adviser).[958] Additionally, we anticipate 1,500 hours[959] for new supervised persons of an investment adviser and costs of approximately $214,500 for new supervised persons[960] of an investment adviser

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956 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

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($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per investment adviser.

(0.5 hours x $143 total cost per investment adviser x 477 new investment advisers) = $34,105.50 total initial cost for new investment advisers.

957 (0.5 hours x 477 new investment advisers) = 238.50 total initial burden for new investment advisers.

(238.50 total initial burden for new investment advisers/ 477 total new investment advisers) = 0.5 hours average initial burden per investment adviser.

958 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per investment adviser.

(0.5 hours x $143 total cost per investment adviser x 477 new investment advisers) = $34,105.50 total cost for new investment advisers / 477 total number of new investment advisers = $71.50 average initial cost per new investment adviser.

959 (0.5 hours x 3,000 new supervised persons) = 1,500 total burden for new supervised persons.

960 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

resulting from these requirements. This would be an initial average burden of 0.5 hours per new supervised person[961] (as monetized, is an initial average cost of $71.50 per supervised person).[962]

I. Request for Comment

We request comment on our estimates for the new estimated burden hours and change in current burden hours, and their associated costs described above. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments in order to: (i) evaluate whether the proposed collections of information are necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (ii) evaluate the accuracy of the Commission's estimate of the burden of the proposed collections of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) determine whether there are ways to minimize the burden of

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($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per supervised person.

(0.5 hours x $143 total cost per supervised person x 3,000 new supervised persons) = $214,500 total cost for new supervised persons.

961 (0.5 hours x 3,000 new supervised persons) = 1,500 total initial burden for new supervised persons.

(1,500 total initial burden for new supervised persons / 3000 total new supervised persons) = 0.5 hours average initial burden per new supervised person.

962 Based on the SIFMA Management and Professional Earnings Report, Commission staff preliminarily estimates that the average hourly rate for compliance services is $298, for business operation services is $268, and for information technology services is $270.

This figure was calculated as follows: 0.5 hours / 3 firm staff categories (*i.e.* compliance, business operations, and information technology) = 0.17 hours per staff category

($298 compliance/hour x 0.17) = $51 per 0.17 of an hour.

($268 business operations rate/hour x 0.17) = $46 per 0.17 of an hour.

($270 information technology rate/hour x 0.17) = $46 per 0.17 of an hour.

$51 + $46 + $46 = $143 total cost per supervised person.

(0.5 hours x $143 total cost per supervised person x 3,000 new supervised persons) = $214,500 total cost for new supervised persons / 3,000 total number of new supervised persons = $71.50 average initial cost per new supervised person.

the collections of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

The agency has submitted the proposed collections of information to OMB for approval. Persons wishing to submit comments on the collection of information requirements of the proposed amendments should direct them to the Office of Management and Budget, Attention Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should send a copy to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549, with reference to File No. S7-08-18. As OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of the proposal, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication. Requests for materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7-08-18, and be submitted to the Securities and Exchange Commission, Office of FOIA Services, 100 F Street, NE, Washington, DC 20549.

VI. INITIAL REGULATORY FLEXIBILITY ANALYSIS

The Commission has prepared the following Initial Regulatory Flexibility Analysis ("IRFA") in accordance with section 3(a) of the Regulatory Flexibility Act ("RFA").[963] It relates to: (i) proposed new rule 204-5 under the Advisers Act and proposed amendment to, Form ADV (17 CFR 279.1), to add a new Part 3: Form CRS; (ii) proposed amendments to rule 203-1 under the Advisers Act; (iii) proposed amendments to rule 204-1 under the Advisers Act; (iv) proposed amendments to rule 204-2 under the Advisers Act; (v) proposed new rule 17a-14 under the Exchange Act and new Form CRS (17 CFR 249.640); (vi) proposed amendments to rules 17a-3

963 5 U.S.C. 603(a).

and 17a-4 under the Exchange Act; (vii) proposed new rules 15l-2 and 15l-3 under the Exchange Act; and (viii) proposed new rule 211h-1 under the Advisers Act.

A. Reason for and Objectives of the Proposed Action

Individual investors rely on the services of broker-dealers and investment advisers when making and implementing investment decisions. Such "retail investors" can receive investment advice from a broker-dealer, an investment adviser, or both, or decide to make their own investment decisions. Broker-dealers, investment advisers and dually registered firms all provide important services for individuals who invest in the markets. Studies show that retail investors are confused about the differences among them.[964] These differences include the scope and nature of the services they provide, the fees and costs associated with those services, conflicts of interest, and the applicable legal standards and duties owed to investors. Studies also indicate that retail investors are confused about whether their firm and financial professional are broker-dealers or investment advisers, or both.[965] Based on these studies, it appears that certain names or titles used by broker-dealers, including "financial advisor," contribute to this confusion and could mislead retail investors into believing that they are engaging with an investment adviser – and are receiving services commonly provided by an investment adviser and subject to an adviser's fiduciary duty, which applies to the retail investors' entire relationship –when they are not.[966]

We recognize the benefits of retail investors having access to diverse business models and of preserving investor choice among brokerage services, advisory services, or both. However, we believe that retail investors need clear information in order to understand the

964 *See* Siegel & Gale Study, *supra* note 5; Rand Study, *supra* note 5; and CFA Survey, *supra* note 5.

965 *See* Siegel & Gale Study, *supra* note 5; Rand Study, *supra* note 5; and 913 Study, *supra* note 3.

966 *See supra* note 375.

differences and key characteristics of each type of service. Providing this clarity is intended to assist investors in making an informed choice when choosing an investment firm and professional and type of account to help to ensure they receive services that meet their needs and expectations. We also believe it is important to mitigate the risk that certain names or titles could result in retail investors being misled, including believing that the financial professional is a fiduciary, leading to uninformed decisions regarding which firm or financial professional to engage, which may in turn result in investors being harmed.

The Commission considered ways to address investor confusion and preserve investor choice, including reviewing studies, comment letters, and committee recommendations.[967] We believe it is important to ensure that retail investors receive the information they need to clearly understand the services, standard of conduct, fees, conflicts, and disciplinary history of firms and financial professionals they are considering. We also believe it is important for retail investors to better understand the distinction between investment advisers and broker-dealers and to have access to the information necessary to make an informed decision about which firm type and financial professional they are engaging or seeking to engage and avoid potential harm.

1. Proposed Form CRS Relationship Summary

We are proposing new rules and rule amendments to require broker-dealers and investment advisers to deliver a Form CRS (or relationship summary) to retail investors that would include general information about each of these topics, including where to find additional information. We preliminarily believe that providing this information before or at the time a

967 *See supra* notes 6 – 22 and accompanying text, referring to the Siegel & Gale Study, the RAND Study, the 913 Study, commenters responding to the 2013 Request for Data, the 917 Financial Literacy Study, comment letters of commenters providing input for these studies, the recommendation of the Commission's Investor Advisory Committee, and comment letters of commenters responding to Chairman Clayton's Request for Comment.

retail investor enters into an investment advisory agreement or first engages a brokerage firm's services, as well as at certain points during the relationship (*e.g.*, switching or adding account types), as further discussed above, is appropriate and in the public interest and will improve investor protection, and will deter potentially misleading sales practices by helping retail investors to make a more informed choice among the types of firms and services available to them.[968]

As discussed above in Section II.A, the relationship summary would be short, with a mix of tabular and narrative information, and contain sections covering: (i) introduction; (ii) the principal relationships and services the firm offers to retail investors; (iii) the standard of conduct applicable to those services; (iv) the fees and costs that retail investors will pay; (v) comparisons of brokerage and investment advisory services (for standalone broker-dealers and investment advisers); (vi) conflicts of interest; (vii) where to find additional information, including whether the firm or its financial professionals currently have reportable legal or disciplinary events and who to contact about complaints; and (viii) key questions for retail investors to ask the firm's financial professional.

The proposed rules and rule amendments would require advisers and broker-dealers to deliver their relationship summaries to retail investors, to file them electronically with the Commission, and to post them electronically on their public websites (if they have a public website). If they do not have a public website, they would be required to include in their relationship summary a toll-free number that retail investors may call to request documents. We are also proposing to require firms to update their relationship summaries within 30 days whenever any information in the relationship summary becomes materially inaccurate. Firms

968 *See supra* note 36 and accompanying text.

would be required to file the updated version electronically with the Commission, and post them on their firms' websites (if they have a public website). Firms would be required to communicate any changes in an updated relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge. The communication could be made by delivering the relationship summary or by communicating the information in another way to the retail investor. The proposal would require a firm to maintain a copy of the relationship summary and each amendment or revision as part of its books and records and make them available to Commission staff upon request, as discussed in Section II.E above. All of these requirements are discussed in detail above in Sections I through IV. The burdens of these requirements on small advisers and broker-dealers are discussed below as well as above in our Economic Analysis and Paperwork Reduction Act Analysis, which discuss the burdens on all advisers and broker-dealers.[969]

As discussed in Section II above, the relationship summary would be in addition to, and not in lieu of, current disclosure and reporting requirements for broker-dealers and investment advisers.[970] The relationship summary would alert retail investors to important information for them to consider when choosing a firm and a financial professional and prompt retail investors to ask informed questions. In addition, the content of the relationship summary would facilitate comparisons across firms. As discussed in Section II above, while the information required by the relationship summary is generally already provided in greater detail for investment advisers

969 *See, e.g.*, Sections IV.B.2.b and V.

970 *See, e.g., supra* note 33 and accompanying text.

by Form ADV Part 2, the relationship summary would provide in one place information about the services, fees, conflicts, and disciplinary history for broker-dealers.[971]

2. Proposed Rules Relating to Restrictions on the Use of Certain Terms and Required Disclosure of Regulatory Status and a Financial Professional's Firm Association

We are also proposing a rule under the Exchange Act that would restrict broker-dealers and their associated natural persons, when communicating with a retail investor, from using as part of a name or title the term "adviser" or "advisor" unless any such (1) broker or dealer is an investment adviser registered under section 203 of the Advisers Act or with a state, or (2) natural person who is an associated person of a broker or dealer is a supervised person of an investment adviser registered under section 203 of the Advisers Act or with a state, and such person provides investment advice on behalf of such investment adviser. We are also proposing rules under the Exchange Act and Advisers Act that would require broker-dealers and investment advisers and their associated natural persons and supervised persons, respectively, to prominently disclose the firm's registration status with the Commission and the financial professional's association with such firm in print and electronic retail investor communications. As discussed above in Section III, the proposed restriction is designed to address the risk that retail investors could be misled by the term "adviser" or "advisor" and, as a result, make an uninformed decision regarding which firm or financial professional they are engaging or seeking to engage, resulting in investors being harmed. Additionally, as discussed above in Section III, we believe that requiring firms and their associated natural persons or supervised persons,

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971 *See supra* text accompanying note 316. In addition, under Regulation Best Interest, broker-dealers would be required to disclose, in writing, the material facts relating to the scope and terms of the relationship with the retail customer and all material conflicts of interest that are associated with the recommendation. *See supra* note 296.

respectively, to disclose whether a firm is a broker-dealer or investment adviser and requiring a financial professional to disclose his or her association with such firm would assist retail investors in determining which type of firm is more appropriate for their specific investment needs. Similarly, our proposed rules to require a firm to disclose whether it is a broker-dealer or an investment adviser in print or electronic communications to retail investors would help to facilitate investor understanding, even if investors currently may not understand the differences between investment advisers and broker-dealers. For similar reasons, we preliminarily believe that because retail investors interact with a firm primarily through financial professionals, it is important that financial professionals disclose the firm type with which they are associated.

B. Legal Basis

The Commission is proposing the following new rule and rule amendments under the authority set forth in section 19(a) of the Securities Act of 1933 [15 U.S.C. 77s(a)], sections 23(a) and 28(e)(2) of the Securities Exchange Act of 1934 [15 U.S.C. 78w(a) and 78bb(e)(2)], section 319(a) of the Trust Indenture Act of 1939 [15 U.S.C. 7sss(a)], section 38(a) of the Investment Company Act of 1940 [15 U.S.C. 80a-37(a)], and sections 203(c)(1), 204, 206A, 206(4), 211(a) and 211(h), and of the Investment Advisers Act of 1940 [15 U.S.C. 80b-3(c)(1), 80b-4, 80b-6a, 80b-6(4), 80b-11(a) and 80b-11(h)], and section 913(f) of Title IX of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"): (i) proposed new rule 204-5 under the Advisers Act ; (ii) amendments to rule 279.1, Form ADV, to create Form CRS for investment advisers; (iii) amendments to rule 203-1 under the Advisers Act; (iv) amendments to rule 204-1 under the Advisers Act; and (v) amendments to rule 204-2 under the Advisers Act. The Commission is proposing the following rule amendments under the authority set forth in section 913(f) of Title IX of the Dodd-Frank Act, sections 3, 10, 15, 23 and

36 of the Exchange Act [15 U.S.C. 78c, 78j, 78o, 78q, 78w and 78mm]: (i) proposed new rule 17a-14 under the Exchange Act; (ii) proposed Form CRS (17 CFR 249.640) under the Exchange Act; and (iii) amendments to rule 17a-3 and 17a-4 under the Exchange Act. The Commission is also proposing the following new rules under the authority set forth in sections 15(l), 23(a), and 36 of the Securities Exchange Act of 1934 (78o(l), 78w(a), and 78mm), sections 211(h), 206A, 211(a) of the Investment Advisers Act of 1940, 15 U.S.C. 80b-1 et seq., (80b-11(h), 80b-6a, 80b-11(a), sections 913(f) and 913(g)(2) of Title IX of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010; (i) proposed new rule 15l-2 under the Exchange Act; (ii) proposed new rule 15l-3 under the Exchange Act; and (iii) proposed new rule 211h-1 under the Advisers Act.

C. Small Entities Subject to the Rule and Rule Amendments

In developing these proposals, we have considered their potential impact on small entities that would be subject to the proposed amendments. The proposed amendments would affect many, but not all, broker-dealers and investment advisers registered with the Commission, including some small entities.

1. Investment Advisers

Under Commission rules, for the purposes of the Advisers Act and the RFA, an investment adviser generally is a small entity if it: (1) has assets under management having a total value of less than $25 million; (2) did not have total assets of $5 million or more on the last day of the most recent fiscal year; and (3) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of $25 million or more, or any person (other than a natural person) that had total assets of $5 million or

more on the last day of its most recent fiscal year.[972] As discussed in Section V, above, the Commission estimates that based on IARD data as of December 31, 2017, approximately 7,625 investment advisers would be subject to the proposed new rule 204-5 under the Advisers Act, Form CRS (required by a new Part 3 of Form ADV), the proposed amendments to rules 203-1, 204-1, and rule 204-2 under the Advisers Act, and the proposed new rule 211h-1 under the Advisers Act.[973] Our proposed new rules and amendments would not affect most investment advisers that are small entities ("small advisers") because they are generally registered with one or more state securities authorities and not with the Commission. Under section 203A of the Advisers Act, most small advisers are prohibited from registering with the Commission and are regulated by state regulators. Based on IARD data, we estimate that as of December 31, 2017, approximately 618 SEC-registered advisers are small entities under the RFA.[974] Of these, 179 provide advice to individual high net worth and individual non-high net worth clients, and would therefore be subject to the proposed Form CRS requirements and the related new and amended rules under the Advisers Act, and proposed new rule 211h-1 under the Advisers Act requiring disclosure of Commission registration status and a financial professional's association in certain communications with retail investors.[975]

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972 Advisers Act rule 0-7(a).

973 *See supra* Section V, at note 712 and accompanying text. Based on responses to Item 5.D. of Form ADV. These advisers indicated that they advise either high net worth individuals or individuals (other than high net worth individuals), which includes trusts, estates, and 401(k) plans and IRAs of individuals and their family members, but does not include businesses organized as sole proprietorships. The proposed definition of retail investor would include a trust or other entity similar entity that represents of natural persons, even if another person is a trustee or managing agent of the trust. We are not able to determine, based on responses to Form ADV, exactly how many advisers provide investment advice to these types of trusts or other entities; however, we believe that these advisers most likely also advise individuals and are therefore included in our estimate.

974 Based on SEC-registered investment adviser responses to Items 5.F. and 12 of Form ADV.

975 Based on SEC-registered investment adviser responses to, Items 5.D.(a), 5.D.(b), 5.F. and 12 of Form ADV, which indicate that the adviser has clients that are high net worth individuals and/or individuals

2. Broker-Dealers

For purposes of a Commission rulemaking in connection with the RFA, a broker-dealer will be deemed a small entity if it: (1) had total capital (net worth plus subordinated liabilities) of less than $500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to rule 17a-5(d) under the Exchange Act,[976] or, if not required to file such statements, had total capital (net worth plus subordinated liabilities) of less than $500,000 on the last day of the preceding fiscal year (or in the time that it has been in business, if shorter); and (2) is not affiliated with any person (other than a natural person) that is not a small business or small organization.

As discussed in Sections IV and V, above, the Commission estimates that as of December 31, 2017, approximately 2,857 retail broker-dealers would be subject to the proposed Form CRS requirements and new rule 17a-14 under the Exchange Act, and proposed amendments to rule 17a-3 and 17a-4 under the Exchange Act, and proposed new rules 15l-2 and 15l-3 under the Exchange Act.[977] Further, based on FOCUS Report data, the Commission estimates that as of December 31, 2017, approximately 1,040 broker-dealers may be deemed small entities under the

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(other than high net worth individuals) and that the adviser is a small entity. Of these, 3 firms are dually registered as a broker-dealer and an investment adviser and may offer services to retail investors as both a broker-dealer and investment adviser (*e.g.*, "dual registrants" for purposes of the relationship summary). *See supra* note 25. Dual registrants would file Form CRS on both IARD and EDGAR describing their retail advisory and retail brokerage businesses. In this RFA, dual registrants are counted in both the total number of small entity investment advisers and broker-dealers that would be subject to Form CRS and the proposed related rules and rule amendments. We believe that counting these firms twice is appropriate because of their additional burdens of complying with the rules with respect to both their advisory and brokerage businesses and filing Form CRS with IARD and EDGAR.

976 *See* 17 CFR 240.0-10(c).

977 *See supra* note 461 and accompanying text. Retail sales activity is identified from Form BD, which categorizes retail activity broadly (by marking the "sales" box) or narrowly (by marking the "retail" or "institutional" boxes as types of sales activity). We use the broad definition of sales as we preliminarily believe that many firms will just mark "sales" if they have both retail and institutional activity. However, we note that this may capture some broker-dealers that do not have retail activity, although we are unable to estimate that frequency.

RFA.[978] Of these, approximately 802 have retail business, and would be subject to the proposed Form CRS requirements and related proposed new and amended rules, the proposed rule requiring disclosure of Commission registration status in certain communications with retail investors, and the proposed rule regarding the prohibition of certain terms in names or titles in certain communications with retail investors.[979]

D. Projected Reporting, Recordkeeping and Other Compliance Requirements

1. Initial Preparation of Form CRS Relationship Summary

Proposed Form CRS and the proposed rules and rule amendments would impose certain reporting and compliance requirements on certain advisers and broker-dealers, including those that are small entities, requiring them to create and update relationship summaries containing specified information regarding their advisory and brokerage businesses, as applicable. The proposed rules and rule amendments, including new recordkeeping requirements, are summarized in this RFA (Section VI.A., above). All of these proposed requirements are also discussed in detail, above, in Sections II.A-E., and these requirements and the burdens on advisers and broker-dealers, including those that are small entities, are discussed above in Sections IV and V (the Economic Analysis and Paperwork Reduction Act Analysis) and below.

The proposed amendments to Form ADV that would require each registered investment adviser that offers advisory services to retail investors to prepare, file and deliver Form CRS would impose additional costs on many registered advisers, including some small advisers. Our

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978 The Commission's estimate is obtained from Form BD filings. Although Form BD filings are updated on a more frequent basis than annually, FOCUS data, which also informs this baseline with respect to broker-dealers, is only sparsely updated throughout the year. Moreover, instead, broker-dealers tend to make their most complete updates in the fourth calendar quarter of each year. Therefore, in order to minimize discrepancies in the broker-dealer data between Form BD and FOCUS data, we have normalized all of the data to the most recently complete FOCUS data, which is for December 2017.

979 *Id.*

Economic Analysis, discussed in Section IV, above, discusses these costs and burdens for investment advisers, which include small advisers.[980] In addition, as discussed in our Paperwork Reduction Analysis, above, we anticipate that some advisers may incur a one-time initial cost for outside legal and consulting fees in connection with the initial preparation of the relationship summary.[981] Generally, all advisers, including small advisers that advise retail investors are currently required to prepare and distribute Part 2 of Form ADV (the firm brochure). Because advisers already provide disclosures about their services, fees, conflicts and disciplinary history in their firm brochures,[982] they would be able to use some of this information to respond to the disclosure requirements of the relationship summary. They would, however, have to draft completely new disclosure to comply with the proposed new format of Form CRS. As discussed above, approximately 179 small advisers currently registered with us would be subject to the proposed new Form ADV Part 3.[983] As discussed above in our Paperwork Reduction Act Analysis, we expect these 179 small advisers to spend, on average, an additional total of 23,152 annual hours, or approximately 129.34 hours per adviser,[984] which translates into an approximate monetized cost of $1,478,055, or $8,257 per adviser, attributable to the initial preparation, filing,

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980 *See supra* notes 621 – 637 and accompanying text (discussing the direct costs of Form CRS and related requirements on broker-dealers and investment advisers, including costs associated with delivery, preparation, and firm-wide implementation of the relationship summary, as well as training and monitoring for compliance).

981 *See supra* notes 729 – 730 and accompanying text (stating, however, that we do not anticipate external costs to investment advisers in the form of website set-up, maintenance, or licensing fees because they would not be required to establish a website for the sole purpose of posting their relationship summary if they do not already have a website, and we also do not expect other ongoing external costs for the relationship summary).

982 Much of the disclosure in Part 2A addresses an investment adviser's conflicts of interest with its clients, and is disclosure that the adviser, as a fiduciary, must make to clients in some manner regardless of the form requirements. *See supra* note 314.

983 *See supra* note 975 and accompanying text.

984 *See supra* Sections V.A.2, V.B, and V.C. 2.52 hours for preparing and filing of the relationship summary + 126.8 hours for posting to the website and delivery = 129.3 hours per adviser.

posting, and delivery related to Form CRS.[985] We expect the incremental external legal and compliance cost for small entity investment advisers to be estimated at $525 per adviser, or $93,936 in aggregate for small advisers.[986]

Similarly, requiring each broker-dealer that offers brokerage services to retail investors to prepare, file and deliver Form CRS would impose additional costs on many broker-dealers, including some small broker-dealers. Our Economic Analysis, discussed in Section IV, above, discusses these costs and burdens for broker-dealers, which include small broker-dealers.[987] In addition, as discussed in our Paperwork Reduction Analysis, above, we anticipate that some broker-dealers may incur a one-time initial cost for outside legal and consulting fees in connection with the initial preparation of the relationship summary.[988] As discussed above,[989] unlike investment advisers, broker-dealers are not currently required to deliver to their retail investors written disclosures covering their services, fees, conflicts, and disciplinary history in one place such as the investment advisory firm brochure.[990] Under existing provisions of the Exchange Act and self-regulatory organization rules, however, a broker-dealer is required to

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985 *See supra* Sections V.A.2, V.B, and V.C. 129.3 hours x 179 small advisers = $23,152 in total annual aggregate hours for small advisers. $8,257 x 179 small advisers = $1,478,055 in total annual aggregate monetized cost for small advisers.

986 *See supra* Section V.A.2.b.

987 *See supra* notes 621 – 637 and accompanying text (discussing the direct costs of Form CRS and related requirements on broker-dealers and investment advisers, including costs associated with delivery, preparation, and firm-wide implementation of the relationship summary, as well as training and monitoring for compliance).

988 *See supra* Section V.D.1. (stating, however, that we do not expect ongoing external legal or compliance consulting costs for the relationship summary).

989 *See supra* Section IV, at note 629 and accompanying text;

990 Broker-dealers are required under certain circumstances, such as when effecting certain types of transactions, to disclose certain conflicts of interest to their customers in writing, in some cases at or before the time of the completion of the transaction. *See* 913 Study, *supra* note 3, at nn.256-259 and accompanying text. *See supra* note 311 and accompanying text. Under Regulation Best Interest, broker-dealers would also be required to disclose the material facts relating to the scope and terms of the relationship. Regulation Best Interest Proposal, *supra* note 24.

disclose certain information to its customers.[991] To the extent that some of the new Form CRS disclosure burdens would apply to small broker-dealers, these broker-dealers are therefore already obligated to make certain of these disclosures to retail investors, although the disclosure is not currently required to be included in one comprehensive document such as Form ADV. As discussed above,[992] approximately 802 broker-dealers that are small entities would be subject to the proposed Form CRS requirements and proposed new and amended rules. As discussed above, we expect these 802 small broker-dealers to spend, on average, 1,080 hours per broker-dealer,[993] for a monetized value of $66,006 per broker-dealer,[994] or 865,956 aggregate annual hours to respond to the proposed new Form CRS requirements,[995] for an annual monetized burden of approximately $52,936,812. We expect the aggregate annual external third-party cost to small broker-dealers associated with this process would be $376,940.[996]

The costs associated with preparing the new relationship summaries will be limited for investment advisers and broker-dealers, including small entities, for several reasons. First, the disclosure document is concise (no more than four pages in length or equivalent limit if in electronic format), and much of the information is already provided by the broker-dealers and investment advisers as part of current disclosure practices. Second, the disclosure will be uniform across retail investors and would not be customized or personalized to potential

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991 *See supra* Section II, at notes 309 – 312 and accompanying text. *See also* Regulation Best Interest Proposal, *supra* note 24.

992 *See supra* note 979.

993 *See supra* note 846.

994 *See supra* note 847.

995 *See supra* note 823 and accompanying text. 802 small broker-dealers x 1,080 hours per broker-dealer = 865,956 annual aggregate hours. 802 small broker-dealers x $66,006 in monetized cost per broker-dealer = 52,936,812 annual aggregate hours.

996 *See supra* note 829 and accompanying text. 802 small broker-dealers x $470 in external legal and compliance costs on average per broker-dealer = $376,940.

investors. Third, the disclosure would involve a certain degree of standardization across firms. In particular, firms would be required to use the same headings, prescribed wording, and present the information under the headings in the same order. Additionally, firms would be prohibited from adding any items to those prescribed by the Commission and any information other than what the Instructions require or permit. These standardized elements allow for potential economies of scale for entities that may have subsidiaries that would also be required to produce the disclosure. The compliance costs could, however, be different across firms with relatively smaller or larger numbers of retail investors as customers or clients.[997]

Filing, Delivery, and Updating Requirements Related to Form CRS. As discussed above, a firm would be required to give a relationship summary to each retail investor, if the firm is an investment adviser, before or at the time the firm enters into an investment advisory agreement with the retail investor, or if the firm is a broker-dealer, before or at the time the retail investor first engages the services of the broker-dealer.[998] A firm would be required to deliver the relationship summary even if the firm's agreement with the retail investor is oral. A dual registrant would deliver the relationship summary at the earlier of entering into an investment advisory agreement with the retail investor or the retail investor engaging the firm's services. In order to ensure that existing retail investors receive the disclosures in the relationship summary, the Commission proposes that firms would deliver the relationship summary to retail investors who are existing clients and customers on an initial one-time basis within 30 days after the date

997 *See supra* note 628 and accompanying text (discussing the Commission's preliminary belief that compliance costs could be different across firms with relatively smaller or larger numbers of retail investors as customers or clients).

998 *See supra* Section II.C for a discussion of the delivery requirements.

the firm is first required to file its relationship summary with the Commission.[999] In addition, firms would be required to deliver the relationship summary to a retail investor who is an existing client or customer before or at the time a new account is opened or changes are made to the retail investor's account(s) that would materially change the nature and scope of the firm's relationship with the retail investor. This would include, for example, before or at the time the firm recommends that the retail investor transfers from an investment advisory account to a brokerage account or from a brokerage account to an investment advisory account, or moves assets from one type of account to another in a transaction not in the normal, customary or already agreed course of dealing.

As discussed above, firms would be required to update the relationship summary within 30 days whenever any information in the relationship summary becomes materially inaccurate.[1000] Firms also would be required to post the latest version on its website (if it has one), and electronically file the relationship summary with the Commission. Firms would be required to communicate any changes in the updated relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge. The firm could communicate the information by delivering the amended relationship summary or by communicating the information in another way to the retail investor. We believe that this flexibility would minimize the burden of the communication requirement for all firms, including small advisers and broker-dealers. Firms also would also be required to deliver the relationship summary to a retail investor upon the retail investor's request.

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999 *See supra* Section II.D for a discussion of the delivery requirements during the proposed transition period following the effectiveness of the proposed new rule.

1000 *See supra* Section II.C.3 for a discussion of updating requirements.

In addition, firms would be permitted to deliver the relationship summary, as well as updates, electronically consistent with the Commission's prior guidance regarding electronic delivery. We believe that this would further minimize the burden of delivery for all firms, including small advisers and broker-dealers. To the extent that small advisers and broker-dealers are more likely to have fewer retail investors than larger advisers and broker-dealers, the proposed delivery requirements should impose lower variable costs on small advisers and broker-dealers than on larger firms. The additional hours per adviser and broker-dealer, the monetized cost per adviser and broker-dealer, and the incremental external legal and compliance cost for small entity investment advisers and broker-dealers, attributable to the initial preparation, filing, posting, delivery, and recordkeeping related to Form CRS, are estimated above and in the Paperwork Reduction Analysis.[1001]

Recordkeeping Requirements Related to Form CRS. The proposed amendments would impose new recordkeeping requirements on many investment advisers and broker-dealers, including some small advisers and broker-dealers. We are proposing amendments to Advisers Act rule 204-2 and Exchange Act rules 17a-3 and 17a-4, which set forth requirements for maintaining, making and preserving specified books and records, to require SEC-registered investment advisers and broker-dealers to retain copies of each relationship summary. Firms would also be required to maintain each amendment and revision to the relationship summary and a record of dates that each relationship summary and each amendment was delivered.

These proposed changes are designed to update the books and records rules in light of proposed Form CRS, and they mirror the current recordkeeping requirements for the Form ADV brochure and brochure supplement. The records for investment advisers would be required to be

[1001] *See supra* Sections V.A. – F.

maintained in the same manner, and for the same period of time, as other books and records required to be maintained under rule 204-2(a) under the Advisers Act, and the records for broker-dealers would be required to maintained for six years after the record was created in accordance with rule 17a-4(e)(10) under the Exchange Act.[1002] As discussed in the Paperwork Reduction Act Analysis in Section IV above, the proposed amendments to rule 204-2 under the Advisers Act would increase the annual burden by approximately 0.2 hours per adviser, or 35.80 hours in aggregate for small advisers.[1003] We therefore expect the annual monetized aggregate cost to small advisers associated with our proposed amendments would be $2,148.[1004] Also as discussed in the Paperwork Reduction Act Analysis in Section IV above, the proposed amendments to rules 17a-3 and 17a-4 under the Exchange Act would increase the burden by approximately 0.2 annual hours per broker-dealer, or 160.4 annual hours in the aggregate.[1005] We expect the aggregate cost to small broker-dealers associated with our proposed amendments would be $9,624.[1006]

2. Rule 15l-2 Relating to Restrictions on the Use of Certain Terms in Names and Titles

As discussed above in Section III, we are proposing to restrict broker-dealers and associated natural persons of broker-dealers, when communicating with a retail investor, from using as part of a name or title the term "adviser" or "advisor" unless any such (1) broker or dealer is an investment adviser registered under section 203 of the Advisers Act or with a state, or (2) natural

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1002 *See supra* note 371 (referencing Advisers Act rule 204-2(e)(1) and Exchange Act rule 17a-4(e)(10), and stating that pursuant to Advisers Act rule 204-2(e)(1), investment advisers will be required to maintain the relationship summary for a period of five years, while Exchange Act rule 17a-4(e)(5) will require broker-dealers to maintain the relationship summary for a period of six years).

1003 *See supra* note 765. 0.2 hours x 179 small entity retail investment advisers = 35.8.

1004 *See supra* note 768.

1005 0.2 hours x 802 small broker-dealers = 160.4 hours.

1006 *See supra* note 854 and accompanying text. $12 per broker-dealer x 802 small broker-dealers = $9,624.

person who is an associated person of a broker or dealer is a supervised person of an investment adviser registered under section 203 of the Advisers Act or with a state, and such person provides investment advice on behalf of such investment adviser.

This would include such names or titles as, for example, financial advisor (or adviser), wealth advisor (or adviser), and trusted advisor (or adviser), and advisory (*e.g.*, "Sample Firm Advisory") when communicating with any retail investor.

The proposed rule would permit firms that are registered both as investment advisers and broker-dealers to use the term "adviser" or "advisor" in their name or title. The proposed rule would, however, only permit an associated natural person of a dually registered firm[1007] to use these terms where such person is also a supervised person of an investment adviser registered with the Commission or with a state and provides investment advice on behalf of such investment adviser. This would limit the ability of natural persons associated with a broker-dealer that do not typically provide investment advisory services to retail investors from continuing to use the term "adviser" or "advisor" by virtue of the fact that they are affiliated with a dually registered firm.

Proposed rule 15l-2 would impose certain compliance requirements on broker-dealers, including small broker-dealers, but would not impose reporting or recordkeeping requirements on broker-dealers. The compliance burdens on broker-dealers, including small broker-dealers, are described above in our Economic Analysis in Section IV. They would need to change their names or titles where their names or titles include "adviser" or "advisor" in violation of the proposed rule. As discussed in Section IV above, the Commission estimates that as of December

[1007] For purposes of rules 15l-2, 15l-3 and 211h-1, we are defining a "dually registered firm" in the same manner as a "dual registrant" is defined in the baseline of the Economic Analysis. *See supra* Section IV, note 453. *See also supra* note 411. We use the more narrowly defined "dual registrant" for purposes of the relationship summary discussion only.

31, 2017, approximately 2,857 broker-dealers would be subject to the proposed rule 151-2 under the Exchange Act.[1008] As discussed in Section IV, above, approximately 103 broker-dealers that are not dually registered as investment advisers use the term "adviser," "advisor," or "advisory" as part of their current company name. To the extent these broker-dealers, some of which may be small entities, advise retail investors and would be subject to proposed rule 151-2, they would be subject to potentially substantial, one-time costs associated with the proposed rule. Broker-dealer firms subject to the restriction on the use of certain names or titles would be required to change current company names (if the company name contains "adviser/advisor"), marketing materials, advertisements (*e.g.*, print ads or television commercials), website and social media appearance, among other items, resulting in direct compliance costs.

In addition, as discussed in Section IV, as a result of the proposed rule 151-2, broker-dealers would need to assess whether their associated natural persons use as part of a name or title the term "adviser" or "advisor." As discussed in Section IV, financial professionals providing brokerage services use a large variety of names or titles to describe their business and the services that they offer, including "financial advisor," "financial consultant," "banker," and "broker."[1009] To the extent their associated natural persons use the terms adviser" or "advisor" when communicating with a retail investor, firms would need to assess whether to require their associated natural persons to change their names or title to comply with the proposed rule and modify their retail investor communications. We request comment on how many associated

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1008 *See supra* Section IV.A.1.a.

1009 As discussed in Section IV, approximately 39 percent of the 103 broker-dealers described above used a proper name coupled with the term "advisor" alone, and an additional 31 percent used a proper name coupled with the term "capital advisor." Additionally, as discussed in the RAND Study, professionals providing advisory services or both brokerage and advisory services similarly also use a wide variety of titles, but the proportion of professionals who use titles containing the terms "adviser" or "advisor" are somewhat larger at 35%. *See supra* Section IV, Table 8: Replication of Table 6.3 of the RAND Study – Professional Titles Most Commonly Reported by Respondents, and accompanying text.

natural persons of broker-dealers, including small entity broker-dealers, are currently using the terms "adviser" or "advisor" in their names or titles, and how many of these associated natural persons are supervised persons of an investment adviser registered with the Commission or with a state and who provide investment advice on behalf of such investment adviser.

The proposed restriction on the use of the term "adviser" and "advisor" in a name or title does not apply to registered investment advisers, whether they are solely registered as investment advisers or whether they are dually registered as broker-dealers. Consequently, there would be no compliance costs for registered investment advisers associated with the restriction on certain terms in names or titles. However, as discussed in Sections III and IV, supervised persons of dually registered investment advisers who do not provide investment advice on behalf of such investment adviser would be restricted from using these terms when communicating with a retail investor, which could lead to costs for those financial professionals or their firms.

3. Rules 15l-3 and 211h-1 Relating to Disclosure of Commission Registration Status and Financial Professional Association

As discussed above, we are proposing rule 15l-3 under Exchange Act and rule 211h-1 under the Advisers Act that would require broker-dealers and investment advisers and their associated natural persons and supervised persons, respectively, to disclose the firm's registration status with the Commission and such financial professional's relationship with the firm in print or electronic retail investor communications. These rules would impose certain compliance requirements on many broker-dealers and investment advisers but would not impose separate reporting or recordkeeping requirements on investment advisers and broker-dealers. The compliance burdens on broker-dealers and investment advisers, including small broker-dealers and investment advisers, are described above in our Economic Analysis in Section IV and the Paperwork Reduction Act discussion in Section V. These include the requirement for

investment advisers and broker-dealers that would be subject to the proposed rule to prominently disclose their registration status in print or electronic retail investor communications. In addition, associated natural persons would need to prominently disclose that they are associated persons of a broker-dealer registered with the Commission, and supervised persons would need to prominently disclose that they are supervised persons of an investment adviser registered with the Commission.

As discussed in Sections IV and V above, the Commission estimates that as of December 31, 2017, approximately 2,857 broker-dealers would be subject to the proposed rule 151-3 under the Exchange Act. As discussed above, of these, approximately 802 are small entities. These broker-dealers would be subject to the rule's requirements described in the previous paragraph. As discussed above, the Commission estimates that as of December 31, 2017, approximately 7,625 investment advisers would be subject to the proposed rule 211h-1 under the Advisers Act. Based on IARD data, we estimate that as of December 31, 2017, approximately 618 advisers are small entities under the RFA. Of these, approximately 179 advise retail investors, and would therefore be subject to the proposed rule 211h-1 under the Advisers Act.

Compliance with these proposed rules would require changes to retail investor communications, which would have to be modified to incorporate the registration status in the manner the rule prescribes. As discussed above in Sections IV and V, to comply with our proposed rule with respect to print communications, broker-dealers and investment advisers would need to review their print and electronic retail investor communications, identify which would need to be amended, make the changes, and verify that all firm retail investor communications comply with the rule's requirements including its technical specifications such as the type size, font, and prominence. As discussed above in Section V, we preliminarily

anticipate that the costs associated with complying with the proposed rule with respect to print communications would be larger for large broker-dealers than for small broker-dealers, because we assume large broker-dealers will have to review, identify and change more print communications and in turn have their compliance staff verify more print communications as being compliant with our proposed rule as compared to small broker-dealers which will have fewer print communications. With respect to electronic communications, broker-dealers would need to review, identify and make the required updates coupled with verifying that such retail investor communications (present and future) would be compliant with the proposed rule.[1010] We preliminarily estimate that the costs associated with complying with the proposed rule regarding electronic communications would similarly be lower for small broker-dealers than for large broker-dealers, because we assume that small broker-dealers have fewer electronic communications that are subject to our proposed rule as compared to large firms. For investment advisers, as discussed above in Section V, we preliminarily estimate that large firms would require larger costs than small firms to comply with the proposed rule (*e.g.*, large firms have a greater amount of retail investor communications subject to our proposed rule that would need to be reviewed, changed, and verified).

The Commission also preliminarily estimates that the costs associated with complying with the proposed rules' disclosure requirements for broker-dealers, investment advisers, and their associated natural persons and supervised persons, respectively, would also be smaller for small firms than for large firms. With respect to broker-dealers, we estimate that the costs would increase with the size of the broker-dealer, such as costs associated with revisions to each

[1010] As stated in Section III.D above, we are not requiring firms to send new communications to replace all older print communications as this would be overly burdensome and costly for firms. Instead, we are staging the compliance date to ensure that firms can phase out certain older communications from circulation through the regular business lifecycle rather than having to retroactively change them.

individual representative's communication and advertising materials.[1011] Specifically, large broker-dealers would have to review, identify and change more print and electronic communications and in turn have their compliance staff verify more communications as being compliant with our proposed rules as compared to small broker-dealers which would have fewer communications. Similarly, with respect to investment advisers, we estimate that small investment advisers would have fewer print and electronic communications that would be subject to our proposed rule as compared to large firms, resulting in a lower burden preliminary estimate. In addition, the Commission estimates that small entity advisers have fewer employees performing investment advisory functions than large advisers.[1012] Therefore, we anticipate that small entity retail investment advisers would require fewer resources to oversee their employees' compliance with the proposed rule.

E. Duplicative, Overlapping, or Conflicting Federal Rules

As noted above, broker-dealers and investment advisers have other disclosure obligations under the federal securities laws and other federal laws.[1013] For example, the information required by the relationship summary is generally already provided in greater detail for investment advisers by Form ADV Part 2. The current disclosure requirements and obligations result in varying degrees and kinds of information to investors, but we believe that all retail investors would benefit from a short summary that focuses on certain key aspects of the firm and its services. By requiring both investment advisers and broker-dealers to deliver a relationship

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1011 *See* Section IV.

1012 Based on adviser responses to Item 5.B.(1) of Form ADV, we estimate that as of September 30, 2017, the median small entity retail investment adviser employed 1 person performing investment advisory functions, and the median non-small entity retail investment advisers employed 5 persons performing investment advisory functions.

1013 *See supra* notes 308 – 316.

summary that discusses both types of services and their differences, the relationship summary would help all retail investors, whether they are considering an investment adviser or a broker-dealer. A relationship summary would help retail investors to understand their relationship with a particular firm, to compare different types of accounts, and to compare that firm with other firms. The relationship summary would provide in one place, for the first time, summary information about the services, fees, conflicts, and disciplinary history for broker-dealers.

Under our proposed rules, firms would be required to file their relationship summary with the Commission, and the relationship summary will be available on the Commission's public disclosure website. Dual registrants would be required to file Form CRS on both IARD and EDGAR. We are proposing IARD and EDGAR because they are familiar filing systems for investment advisers and broker-dealers.[1014] By having firms file the relationship summaries with the Commission, the Commission can more easily monitor the filings for compliance with Form CRS. We believe that requiring dual registrants to file on both EDGAR and IARD is appropriate and in the public interest and will improve investor protection. This is because retail investors seeking brokerage services (but not investment advisory services) would be likely to search EDGAR, and retail investors seeking investment advisory services (but not brokerage services) would be likely to search IARD.

F. Significant Alternatives

The RFA directs the Commission to consider significant alternatives that would accomplish our stated objectives, while minimizing any significant adverse impact on small entities. We considered the following alternatives for small entities in relation to the proposed Form CRS required by Part 3 of Form ADV, the proposed amendments to Form ADV (17 CFR

[1014] *See supra* Section II.C.1.

279.1) and rules 203-1, 204-1, and 204-2 under the Advisers Act, the proposed new rule 204-5 under the Advisers Act, the proposed amendments to rules 17a-3 and 17a-4 under the Exchange Act, the proposed new rule 17a-14 and new Form CRS (17 CFR 249.640) under the Exchange Act, the proposed new rules 15l-2 and 15l-3 under the Exchange Act, and the proposed new rule 211h-1 under the Advisers Act: (i) the establishment of differing compliance or reporting requirements that take into account the resources available to small entities; (ii) the clarification, consolidation, or simplification of compliance and reporting requirements under the proposed Form CRS, and proposed new rules and rule amendments for such small entities; (iii) the use of performance rather than design standards; and (iv) an exemption from coverage of the proposed Form CRS, and proposed rules and rule amendments, or any part thereof, for such small entities.

1. Form CRS Relationship Summary

Regarding the first alternative, the Commission believes that establishing different compliance or reporting requirements for small advisers and broker-dealers would be inappropriate under these circumstances. Because the protections of the Advisers Act and Exchange Act are intended to apply equally to retail investor clients and customers of both large and small firms, it would be inconsistent with the purposes of the Advisers Act and the Exchange Act to specify differences for small entities under the proposed rules and rule amendments. As discussed above, we believe that the proposed new Form CRS, and the proposed rules and rule amendments would result in multiple benefits to all retail investors, including alerting retail investors to certain information to consider when choosing a firm and a financial professional and prompting retail investors to ask informed questions. In addition, the content of the relationship summary would facilitate comparisons across firms. We believe that these benefits

should apply to retail investors of smaller firms as well as retail investors of larger firms.[1015] To establish different disclosure requirements for small entities would diminish this investor protection for clients of small advisers.

It would also be inappropriate to establish different recordkeeping requirements for small entities, because requiring maintenance of Form CRS and related records as part of the firm's books and records would facilitate the Commission's ability to inspect for and enforce compliance with firms' obligations with respect to Form CRS, which is important for retail investors clients of both large and small firms.

In addition, as discussed above in Section II, we are proposing to require that investment advisers and dual registrants file their relationship summaries with the Commission electronically through IARD in the same manner as they currently file Form ADV Parts 1 and 2. We are proposing to require that broker-dealers file their relationship summaries with the Commission electronically on EDGAR. As discussed above, there are several reasons we propose having the relationship summaries filed with the Commission, including that the public would benefit by being able to use a central location to find any firm's relationship summary, and that easy access to various relationship summaries through one source may facilitate simpler comparison across firms.[1016] In addition, as also discussed below, some firms may not maintain a website, and therefore their relationship summaries would not otherwise be accessible to the public.[1017] We do not believe that proposing different filing requirements for large and small firms would be appropriate given our belief that the benefits of electronic filing are important for

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1015 *See supra* Section 0 (discussing the benefits of retail investors having access to diverse business models and of preserving investor choice among brokerage services, advisory services, or both).

1016 *See supra* note 320 and accompanying text.

1017 *Id.*

retail investors clients and customers of both large and small firms. Furthermore, almost all advisers, including small advisers, have Internet access and use the Internet for various purposes.[1018]

Finally, the proposal to require investment advisers and broker-dealers post their relationship summary on their public websites, if they have a public website, in a way that is easy for retail investors to find, already incorporates the flexibility to permit different compliance and reporting requirements for small entities, if applicable. To the extent that broker-dealers and investment advisers that are small entities are less likely to have public websites and do not have them, they would not be required under our proposal to post the relationship summary on their websites.[1019] In other ways, as well, the proposal incorporates flexibility for smaller broker-dealers and investment advisers to comply with the proposed requirements. For instance, we are proposing to require firms to communicate the information in an amended relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge.[1020] This requirement provides firms the ability to disclose changes without requiring them to duplicate disclosures and incur additional costs.

Regarding the second alternative, we believe the current proposal is clear and that further clarification, consolidation, or simplification of the compliance requirements is not necessary.

1018 *See* 2000 Brochure Proposing Release, *supra* note 271, at n.304 and accompanying text. However, an adviser that is a small business may be eligible for a continuing hardship exemption for Form ADV filings, which would include proposed Form CRS, if it can demonstrate that filing electronically would impose an undue hardship. *See* Instruction 17 of General Instructions to Form ADV.

1019 *See supra* note 320 (we are proposing that firms without a website include a toll-free telephone number in their relationship summaries that retail investors can call to obtain up-to-date information).

1020 Advisers Act proposed rule 204-5(b)(4) and Exchange Act proposed rule 17a-14(c)(2)(iv4); proposed General Instruction 6.(b) to Form CRS. *See supra* Section II.C.3. Firms could communicate this information by delivering the amended relationship summary or by communicating the information another way to the retail investor. *Id*.

The proposed Instructions are designed to present requirements for advisers' and broker-dealers' relationship summaries clearly and simply to all such firms, including small entities. In addition, to aid firms in understanding the type of disclosures we propose to require, we have created mock-ups of a relationship summary for an investment advisory firm, a brokerage firm, and a dual registrant, and have included them as appendices to this release. These mock-ups examples are designed to illustrate the application of the proposed requirements. We also believe that the delivery and filing requirements are clear. As further discussed above, our proposal would require: delivery of the relationship summary to each retail investor before or at the time of beginning a relationship with a firm,[1021] updating the relationship summary within 30 days whenever any information in the relationship summary becomes materially inaccurate,[1022] and delivery of the relationship summary to an existing retail investor client or customer at certain points during the relationship.[1023] Firms would also be required to file their relationship summaries with the Commission and post them on their firm websites, if they have a public website.

Regarding the third alternative, the Commission believes that proposed Form CRS and the related new rules and amendments appropriately use a combination of performance and design standards. We are proposing to standardize the relationship summaries among firms by specifying the headings, sequence, and content of the topics; prescribing language for firms to

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1021 *See supra* Section II.C.2. We are proposing different triggers for initial delivery of the relationship summary by investment advisers (before or at the time the firm enters into an investment advisory agreement with the retail investor) and by broker-dealers (before or at the time the retail investor first engages the firm's services). These proposed requirements are intended to make the relationship summary readily accessible to retail investors at the time when they are choosing investment services and are generally consistent with the approach many commenters recommended. *Id*.

1022 *See supra* Section II.C.3.

1023 *See supra* Section II.C.2. For example, our proposal would require firms to communicate the information in an amended relationship summary to retail investors who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge.

use as applicable; and limiting the length of the relationship summary. We believe that the standardization will provide comparative information in a user-friendly format that helps retail investors with informed decision making. For example, we are prescribing the use of graphical formats in specified circumstances, based on studies that indicate the effectiveness of graphical presentation for retail investors.[1024] Also, as discussed above, we are requiring firms to use prescribed wording in many items, and we are proposing that firms may not include disclosure in the relationship summary other than disclosure that is required or permitted by the Instructions.[1025] We believe that allowing only the proposed mandatory or permissible information would promote consistency of information presented to investors, and allow investors to focus on information that we believe is particularly helpful in deciding among firms.[1026]

Within the framework of standardization, we are proposing that for certain disclosure Items in Form CRS, firms would have some flexibility in how they include the required information.[1027] In addition, we have proposed permitting, but not requiring, the use of graphical formats where doing so does not unduly constrain effective description of a range of information. With respect to the prescribed wording, we are proposing that if a prescribed statement is inapplicable to a firm's business or would be misleading to a reasonable retail investor, the firm

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1024 For example we are proposing to require dual registrants to present all of the information required by Items 2 through 4 and Item 6 in a tabular format, comparing advisory services and brokerage services side-by-side, with prescribed headings. *See* proposed General Instruction 1.(e) to Form CRS. Similarly, standalone broker-dealers and investment advisers would be required to provide general information about fee types in tabular format, in a separate comparison section. *See* proposed Item 5 of Form CRS.

1025 *See* supra notes 54 – 55 and accompanying text.

1026 It would also encourage impartial information by preventing firms from adding information commonly used in marketing materials, such as performance.

1027 *See supra* note 56.

would be permitted to omit or modify that statement.[1028]

We believe that this approach of using both performance and design standards balances the need to provide firms flexibility in making the presentation of information consistent with their particular business model while ensuring that all investors receive certain information regardless of the firm in a manner that promotes comparability. In the sections above, we request comment on whether the proposed mix of design and performance standards would work for investment advisers and broker-dealers, including small entities, and what the impact of such standards would be on firms.[1029]

Regarding the fourth alternative, we believe that, similar to the first alternative, it would be inconsistent with the purposes of the Advisers Act and the Exchange Act to exempt small advisers and broker-dealers from the proposed rule and form amendments, or any part thereof. Because the protections of the Advisers Act and Exchange Act are intended to apply equally to retail investors that are clients and customers of both large and small advisers and broker-dealers, it would be inconsistent with the purposes of the Advisers Act and Exchange Act to specify differences for small entities under the proposed amendments. As discussed above, the information in the relationship summary would alert retail investors to important information for them to consider when choosing a firm and a financial professional, and would prompt retail investors to ask informed questions. In addition, the content of the relationship summary would facilitate comparisons across firms that offer the same or substantially similar services. We preliminarily believe that providing this information before or at the time a retail investor enters

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1028 *See* proposed General Instruction 3 to Form CRS. Firms may omit or modify prescribed wording or other statements required to be part of the relationship summary if such statements are inapplicable to a firm's business or would be misleading to a reasonable retail investor.

1029 *See* requests for comment in Sections II.A and II.B with respect to the proposed prescribed wording in places throughout the relationship summary, and the proposed prescribed headings, order and format.

into an investment advisory agreement or first engages a brokerage firm's services, as well as at certain points during the relationship (*e.g.*, switching account types) is appropriate and in the public interest and will improve investor protection, and will deter potentially misleading sales practices by helping retail investors to make a more informed choice among the types of firms and services available to them. Since we view investor confusion about brokerage and advisory services as an issue for many retail investors who are clients and customers of advisers and broker-dealers, it would be inconsistent with the purpose of the relationship summary to specify different requirements for small entities.[1030]

2. Rule 15l-2 Relating to Restrictions on the Use of Certain Terms in Names and Titles

Regarding the first alternative, the Commission preliminarily believes that establishing different compliance or reporting requirements for small broker-dealers would be inappropriate under these circumstances. We believe it is important to address the risk that retail investors are confused and potentially misled based on the names or titles of their firms and financial professionals and as a result, make uninformed decisions regarding which firm or financial professional they are engaging or seeking to engage. Because the protections of the Exchange Act are intended to apply equally to retail investor clients of both large and small firms, the Commission preliminarily believes it would be inconsistent with the purposes of the Exchange Act to specify differences for small entities under the proposed rule.

Regarding the second alternative, we believe that the current proposal is clear and that further clarification, consolidation, or simplification is not necessary. As discussed in Section III above, the restriction is limited to use of the terms "adviser" and "advisor." As discussed above

[1030] *See supra* note 3, citing studies that show retail investor confusion about the differences among broker-dealers and investment advisers.

in Section III, we considered whether we should restrict broker-dealers from using additional terms, such as, for example, "financial consultant." We believe, however, that the term "adviser" or "advisor" is more closely related to the statutory term "investment adviser," which makes it more likely than these other terms that retail investors would associate such terms with an investment adviser and its advisory activities than with a broker-dealer and its brokerage activities. We preliminarily believe that the use of the terms "adviser" and "advisor" by broker-dealers and their associated natural persons has particularly contributed to investor confusion about the typical services, fee structures, conflicts of broker-dealers and investment advisers, and legal standards of conduct to which broker-dealers and investment advisers are subject. Therefore, we believe that the current proposal is clear in its limited scope of restricted terms.

Regarding the third alternative, we believe that using performance rather than our proposed design standards would be less effective in addressing the issue of investor confusion based on the names or titles of their firms and financial professionals. As discussed in Section III, the proposed rule would restrict broker-dealers' or its associated natural persons' use of the term "adviser" or "advisor" as part of a name or title when communicating with a retail investor. We believe that the use of the terms "adviser" and "advisor" has particularly contributed to investor confusion about the typical services, fee structures, conflicts of interest, and legal standards of conduct to which broker-dealers and investment advisers are subject and as a result has potentially misled retail investors as to the type of firm or financial professional they are engaging or seeking to engage. Accordingly, we believe that restricting these terms appropriately addresses these issues based on a broker-dealer's or its associated natural persons' use of the term "adviser" or "advisor" as part of a name or title. As discussed above in Section III, we preliminarily believe that without restricting a broker-dealer or its associated natural

person(s) from using "adviser" or "advisor" in a name or title, a retail investor may be misled into believing and expecting that their "financial advisor," who may, for example, solely provide brokerage services at a broker-dealer, is an investment adviser (*i.e.* a fiduciary) on the basis of his name or title.

Additionally, we considered two performance-based standards, as discussed above in Section III.C.[1031] However, we believe that either performance standard would be less effective than our proposed design standard in addressing investor confusion stemming from their association with the statutory term investment adviser. In the first alternative approach, we considered proposing a rule which would have stated that a broker-dealer that uses the term "adviser" or "advisor" as part of a name or title would not be considered to provide investment advice solely incidental to the conduct of its brokerage business and therefore would not be excluded from the definition of investment adviser under section 202(a)(11)(C) of the Advisers Act.. For the second alternative approach, we considered precluding a broker-dealer from relying on the solely incidental exclusion of section 202(a)(11)(C) if it "held itself out" as an investment adviser to retail investors such as by representing or implying through any communication or other sales practice (including through the use of names or titles) that they are offering investment advice subject to a fiduciary relationship with an investment adviser. Under this second approach, there would be a prohibition on certain broker-dealer and its associated natural person communications that suggest, or could reasonably be understood as suggesting, that such broker-dealer or its associated natural persons are performing investment advisory services in a manner that would subject them to the Advisers Act rather than as solely incidental to their business as a broker-dealer. For the reasons we set out in Section III above, we believe

[1031] *See supra* Section III.C.

that our proposed restriction on the use of "adviser" and "advisor" in combination with the requirement to deliver a relationship summary is a simpler, more administrable approach to address the confusion about the difference between investment advisers and broker-dealers, and to prevent investors from being potentially misled. As a result, we believe that our proposed approach is more tailored toward creating greater clarity than our alternative approaches.

Regarding the fourth alternative, we preliminarily believe that, similar to the first alternative, it would be inconsistent with the purposes of the Exchange Act to exempt small broker-dealers from the proposed rule, or any part thereof.

3. Rule 15l-3 Relating to Disclosure of Commission Registration Status and Financial Professional Association

Regarding the first alternative, the Commission believes that establishing different compliance or reporting requirements for small advisers and broker-dealers would be inappropriate under these circumstances. We believe it is important to assist retail investors in determining which type of firm is more appropriate for their specific investment needs and promote better informed decisions regarding which firm or financial professional they are engaging or seeking to engage. Because the protections of the Advisers Act and Exchange Act are intended to apply equally to retail investor clients of both large and small firms, we preliminarily believe it would be inconsistent with the purposes of the Exchange Act and the Advisers Act to specify differences for small entities under the proposed rule.

Regarding the second alternative, we believe that the current proposal is clear and that further clarification, consolidation, or simplification of the compliance requirements is not necessary. As discussed in Section III.D, we are proposing rules under the Exchange Act and Advisers Act that would require broker-dealers and investment advisers and their associated natural persons and supervised persons, respectively, to prominently disclose the firm's

registration status with the Commission and the associated natural persons and supervised person's relationship with the firm in print and electronic retail investor communications. As discussed above in Section III, our proposal would subject broker-dealers and investment advisers to the same requirements, adding to the clarity and consolidation of the compliance requirements. Finally, we note that our proposed rules contain specific presentation and prominence requirements, as discussed above in Section III, for both print and electronic communications.

Regarding the third alternative, we believe that using performance rather than design standards would be less effective in assisting retail investors in determining which type of firm is more appropriate for their specific investment needs. Specifically, we are concerned that in the absence of the specific prominence and formatting requirements, firms and financial professionals may disclose their registration status in a footnote or at the bottom of a website and in small print as they do today with other regulatory mandated disclosures (*e.g.*, member of Securities Investor Protection Corporation). In such cases, retail investors would be unable to readily discern whether a firm is a broker-dealer or investment adviser and thus avoid making an uniformed choice of which firm or financial professional to engage or seek to engage, undermining a key purpose of our proposed rules. Therefore, we believe that our proposed design standards would facilitate the presentation of required information to retail investors. Specifically, as we noted above, disclosures as important as a firm's registration status or a financial professional's association with such firm should not be disclosed inconspicuously or placed in fine print. Accordingly, we are proposing to require a firm and its financial professionals to disclose their registration statuses in print communications in a type size at least as large as and of a font style different from, but at least as prominent as, that used in the

majority of the communication. In addition, we are proposing to require the disclosure to be presented in the body of the communication and not in a footnote. Finally, we are also proposing that if a communication is delivered through an electronic communication or in any publication by radio or television, the disclosure must be presented in a manner reasonably calculated to draw retail investors' attention to it. We believe that through these design standards retail investors would have the information necessary to facilitate an informed choice of financial firm and its professionals.

Regarding the fourth alternative, we preliminarily believe that, similar to the first alternative, it would be inconsistent with the purposes of the Advisers Act and the Exchange Act to exempt small advisers and broker-dealers from the proposed rule, or any part thereof.

G. Solicitation of Comments

We encourage written comments on the matters discussed in this IRFA. We solicit comment on the number of small entities subject to the proposed Form CRS, and the proposed rules and rule amendments as well as the potential impacts discussed in this analysis; and whether the proposal could have an effect on small entities that has not been considered. We request that commenters describe the nature of any impact on small entities and provide empirical data to support the extent of such impact.

VII. CONSIDERATION OF THE IMPACT ON THE ECONOMY

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA,"[1032] we must advise OMB whether a proposed regulation constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results in or is likely to result

[1032] Public Law 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

in (1) an annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers or individual industries; or (3) significant adverse effects on competition, investment or innovation.

We request comment on the potential effect of the proposed amendments on the U.S. economy on an annual basis; any potential increase in costs or prices for consumers or individual industries; and any potential effect on competition, investment or innovation. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

VIII. STATUTORY AUTHORITY

The Commission is proposing amendments to rule 203-1 under the Advisers Act pursuant to authority set forth in sections 203(c)(1), 204, and 211(a) of the Investment Advisers Act of 1940 [15 U.S.C. 80b-3(c)(1), 80b-4, and 80b-11(a)].

The Commission is proposing amendments to rule 204-1 under the Advisers Act pursuant to authority set forth in sections 203(c)(1) and 204 of the Investment Advisers Act of 1940 [15 U.S.C. 80b-3(c)(1) and 80b-4].

The Commission is proposing new rule 204-5 under the Advisers Act pursuant to authority set forth in sections 204, 206A, 206(4), 211(a), and 211(h) of the Investment Advisers Act of 1940 [15 U.S.C. 80b-4, 80b-6a, 80b-6(4), 80b-11(a), 80b-11(h)], and section 913(f) of Title IX of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act").

The Commission is proposing amendments to rule 279.1, Form ADV, under section 19(a) of the Securities Act of 1933 [15 U.S.C. 77s(a)], sections 23(a) and 28(e)(2) of the Securities Exchange Act of 1934 [15 U.S.C. 78w(a) and 78bb(e)(2)], section 319(a) of the Trust Indenture

Act of 1939 [15 U.S.C. 7sss(a)], section 38(a) of the Investment Company Act of 1940 [15 U.S.C. 80a-37(a)], and sections 203(c)(1), 204, 206A, 211(a) and 211(h), and of the Investment Advisers Act of 1940 [15 U.S.C. 80b-3(c)(1), 80b-4, 80b-6a, 80b-11(a) and 80b-11(h)], and section 913(f) of Title IX of the Dodd-Frank Act.

The Commission is proposing to amend rule 204-2 under the Advisers Act pursuant to authority set forth in sections 204 and 211 of the Advisers Act [15 U.S.C. 80b-4 and 80b-11].

The Commission is proposing new rule 17a-14 under the Exchange Act, Form CRS, and amendments to rules 17a-3 and 17a-4 under the Exchange Act pursuant to the authority set forth in the Exchange Act and particularly sections 3, 10, 15, 17, 23 and 36 thereof 15 U.S.C. 78c, 78j, 78o, 78q, 78w and 78mm, and section 913(f) of Title IX of the Dodd-Frank Act.

The Commission is proposing new rules 15*l*-2 and 15*l*-3 under the authority set forth in sections 10, 15, 23, and 36 of the Securities Exchange Act of 1934 [15 U.S.C. 78j, 78o, 78w, and 78mm] and new rule 211h-1 under the authority set forth in sections 211(h), 206A, 211(a) of the Investment Advisers Act of 1940 [15 U.S.C. 80b-11(h), 80b-6a, 80b-11(a)].

IX. TEXT OF RULE AND FORM

List of Subjects in 17 CFR Parts 240 and 249

Brokers, Reporting and recordkeeping requirements, Sales practice and disclosure requirements, Securities.

List of Subjects in 17 CFR Parts 275 and 279

Investment advisers, Reporting and recordkeeping requirements, Securities.

TEXT OF PROPOSED RULES

For the reasons set out in the preamble, title 17, chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 240 – GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The general authority citation for part 240 continues to read as follows and sectional authorities for 240.15*l*-2, 240.15*l*-3, and 240.17a-14 are added to read as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78c-3, 78c-5, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78*l*, 78m, 78n, 78n-1, 78*o*, 78*o*-4, 78*o*-10, 78p, 78q, 78q-1, 78s, 78u-5, 78w, 78x, 78*ll*, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, 7201 *et seq.;* and 8302; 7 U.S.C. 2(c)(2)(E); 12 U.S.C. 5221(e)(3); 18 U.S.C. 1350; and Pub. L. 111-203, 939A, 124 Stat. 1887 (2010); and secs. 503 and 602, Pub. L. 112-106, 126 Stat. 326 (2012), unless otherwise noted.

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Section 240.15*l*-2 is also issued under Pub. L. 111-203, sec. 913, 124 Stat. 1376 (2010).

Section 240.15*l*-3 is also issued under Pub. L. 111-203, sec. 913, 124 Stat. 1376 (2010).

Section 240.17a-14 is also issued under Pub. L. 111-203, sec. 913, 124 Stat. 1376 (2010).

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2. Section 240.15*l*-2 is added to read as follows:

§240.15*l*-2 Use of the Term "Adviser" or "Advisor".

(a) A broker or dealer, or a natural person who is an associated person of a broker or dealer shall be restricted, when communicating with a retail investor, from using as part of a name or title the term "adviser" or "advisor" unless any such:

(1) Broker or dealer is an investment adviser registered under Section 203 of the Investment Advisers Act of 1940 or with a State, or

(2) Natural person who is an associated person of a broker or dealer is a supervised person of an investment adviser registered under Section 203 of the Investment Advisers Act of

1940 or with a State, and such person provides investment advice on behalf of such investment adviser.

(b) The term *retail investor* has the meaning set forth in §240.17a-14.

3. Section 240.15*l*-3 is added to read as follows:

§240.15*l*-3 Disclosure of Registration Status.

(a) A broker or dealer shall prominently disclose that it is registered with the Commission as a broker-dealer in print or electronic retail investor communications.

(b) A natural person who is an associated person of a broker or dealer shall prominently disclose that he or she is an associated person of a broker-dealer registered with the Commission in print or electronic retail investor communications.

(c) Such disclosures in paragraphs (a) and (b) shall be provided in the following manner:

(1) For print communications, such status must be displayed in a type size at least as large as and of a font style different from, but at least as prominent as, that used in the majority of the communication. In addition, such disclosure must be presented in the body of the communication and not in a footnote.

(2) For electronic communications, or in any publication by radio or television, such disclosure must be presented in a manner reasonably calculated to draw retail investor attention to it.

(d) The term *retail investor* has the meaning set forth in §240.17a-14.

4. Section 240.17a-3 is amended by adding paragraph (a)(24) to read as follows:

§240.17a-3 Records to be made by certain exchange members, brokers and dealers.

(a) * * *

(24) A record of the date that each Form CRS was provided to each retail investor, including any Form CRS provided before such retail investor opens an account.

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5. Section 240.17a-4 is amended by adding paragraph (e)(10) to read as follows:

§240.17a-4 Records to be preserved by certain exchange members, brokers and dealers.

* * * * *

(e) * * *

(10) All records required pursuant to §240.17a-3(a)(24), as well as a copy of each Form CRS, until at least six years after such record or Form CRS is created.

* * * * *

6. Section 240.17a-14 is added to read as follows:

§240.17a-14 Form CRS, for preparation, filing and delivery of Form CRS.

(a) *Scope of Section.* This section shall apply to every broker or dealer registered with the Commission pursuant to section 15 of the Act that offers services to a retail investor.

(b) *Form CRS.* You must:

(1) Prepare Form CRS 17 CFR 249.640, by following the instructions in the form.

(2) File your current Form CRS electronically with the Commission through the Commission's EDGAR system, and thereafter, file an amended Form CRS in accordance with the instructions in the form.

(3) Amend your Form CRS as required by the instructions in the form.

(c) *Delivery of Form CRS.* You must:

(1) Deliver to each retail investor your current Form CRS before or at the time the retail investor first engages your services.

(2) Deliver to each retail investor who is an existing customer your current Form CRS before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's existing account(s) that would materially change the nature and scope of the relationship with the retail investor, including before or at the time you recommend that the retail investor transfers from an advisory account to a brokerage account, transfers from a brokerage account to an advisory account, or moves assets from one type of account to another in a transaction not in the normal, customary or already agreed course of dealing. Whether a change would require delivery of the Form CRS would depend on the specific facts and circumstances.

(3) Post the current Form CRS prominently on your Web site, if you have one, in a location and format that is easily accessible for retail investors.

(4) Communicate any changes made to Form CRS to each retail investor who is an existing customer within 30 days after the amendments are required to be made and without charge. The communication can be made by delivering the current Form CRS or by communicating the information in another way to the retail investor.

(5) Deliver a current Form CRS to each retail investor within 30 days upon request.

(d) *Other disclosure obligations*. Delivering a Form CRS in compliance with this section does not relieve you of any other disclosure obligations arising under the federal securities laws and regulations or other laws or regulations (including the rules of a self-regulatory organization).

(e) *Definitions*. For purposes of this section:

(1) *Current Form CRS* means the most recent version of the Form CRS.

(2) *Retail investor* means a customer or prospective customer who is a natural person (an individual). This term includes a trust or other similar entity that represents natural persons, even if another person is a trustee or managing agent of the trust.

(f) *Transition rule.* (1) You must begin to comply with this section by [INSERT DATE SIX MONTHS AFTER EFFECTIVE DATE OF RULES/FORM], including by filing your Form CRS in accordance with paragraph (b)(2) of this section by that date.

(2) Within 30 days after the date by which you are first required by paragraph (f)(1) of this section to electronically file your Form CRS with the Commission, you must deliver to each of your existing customers who is a retail investor your current Form CRS.

(3) After [INSERT DATE SIX MONTHS AFTER EFFECTIVE DATE OF RULES/FORM], if you are a newly registered broker or dealer that is subject to this section, you must begin to comply with this section by the date on which your registration with the Commission becomes effective pursuant to Section 15(b) of the Act, including by filing your Form CRS in accordance with paragraph (b)(2) of this section by that date.

EDITORIAL NOTE: For FEDERAL REGISTER citations affecting Form CRS, see the List of CFR Sections Affected, which appears in the Finding Aids section of the printed volume and at *www.fdsys.gov.*

PART 249 – FORMS, SECURITIES EXCHANGE ACT OF 1934

7. The authority citation for part 249 is amended by adding sectional authorities to read as follows:

Authority: 15 U.S.C. 78a *et seq.* and 7201 *et seq.*; 12 U.S.C. 5461 *et seq.*; 18 U.S.C. 1350; Sec. 953(b), Pub. L. 111-203, 124 Stat. 1904; Sec. 102(a)(3), Pub. L. 112-106, 126 Stat.

309 (2012); Sec. 107, Pub. L. 112-106, 126 Stat. 313, (2012), and Sec. 72001, Pub. L. 114-94, 129 Stat. 1312 (2015), unless otherwise noted.

* * * * *

Section 249.640 is also issued under Pub. L. 111-203, sec. 913, 124 Stat. 1376 (2010).

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8. Section 249.640 is added to read as follows:

§249.640 Form CRS, Relationship Summary for Broker-Dealers Providing Services to Retail Investors, pursuant to §240.17a-14 of this chapter.

This form shall be prepared and filed by broker-dealers registered with the Securities and Exchange Commission pursuant to Section 15 of the Act that offer services to a retail investor pursuant to §240.17a-14 of this chapter.

PART 275 – RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

9. The general authority citation for part 275 continues to read as follows and sectional authorities for 275.204-5 and 275.211h-1 are added to read as follows:

Authority: 15 U.S.C. 80b-2(a)(11)(G), 80b-2(a)(11)(H), 80b-2(a)(17), 80b-3, 80b-4, 80b-4a, 80b-6(4), 80b-6a, and 80b-11, unless otherwise noted.

* * * * *

Section 275.204-5 is also issued under sec. 913, Pub. L. 111-203, sec. 124 Stat. 1827-28 (2010).
Section 275.211h-1 is also issued under sec. 913, Pub. L. 111-203, sec. 124 Stat. 1827-28 (2010).

* * * * *

10. Amend §275.203-1 by revising paragraph(a) to read as follows:

§275.203-1 Application for investment adviser registration.

(a) *Form ADV.* (1) To apply for registration with the Commission as an investment adviser, you must complete Form ADV (17 CFR 279.1) by following the instructions in the form and you must file Part 1A of Form ADV, the firm brochure(s) required by Part 2A of Form ADV and Form CRS required by Part 3 of Form ADV electronically with the Investment Adviser Registration Depository (IARD) unless you have received a hardship exemption under §275.203-3. You are not required to file with the Commission the brochure supplements required by Part 2B of Form ADV.

(2) After [INSERT DATE SIX MONTHS AFTER EFFECTIVE DATE OF RULES/FORM] the Commission will not accept any initial application for registration as an investment adviser that does not include a Form CRS that satisfies the requirements of Part 3 of Form ADV.

NOTE TO PARAGRAPH (a)(1): Information on how to file with the IARD is available on the Commission's Web site at *http://www.sec.gov/iard.* If you are not required to deliver a brochure or Form CRS to any clients, you are not required to prepare or file a brochure or Form CRS, as applicable, with the Commission. If you are not required to deliver a brochure supplement to any clients for any particular supervised person, you are not required to prepare a brochure supplement for that supervised person.

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11. Amend §275.204-1 by revising paragraphs (a) and (b) to read as follows:

§275.204-1 Amendments to Form ADV.

(a) *When amendment is required.* You must amend your Form ADV (17 CFR 279.1):

(1) Parts 1 and 2:

(i) At least annually, within 90 days of the end of your fiscal year; and

(ii) More frequently, if required by the instructions to Form ADV.

(2) Part 3 at the frequency required by the instructions to Form ADV.

(b) *Electronic filing of amendments.* (1) Subject to paragraph (b)(3) of this rule, you must file all amendments to Part 1A, Part 2A and Part 3 of Form ADV electronically with the IARD, unless you have received a continuing hardship exemption under §275.203-3. You are not required to file with the Commission amendments to brochure supplements required by Part 2B of Form ADV.

(2) If you have received a continuing hardship exemption under §275.203-3, you must, when you are required to amend your Form ADV, file a completed Part 1A, Part 2A and Part 3 of Form ADV on paper with the SEC by mailing it to FINRA.

(3) Transition to filing Form CRS. You must amend your Form ADV by electronically filing with the IARD Form CRS that satisfies the requirements of Part 3 of Form ADV (as amended effective [INSERT EFFECTIVE DATE OF RULES/FORM]) as part of the next annual updating amendment you are required to file after [INSERT DATE SIX MONTHS AFTER EFFECTIVE DATE OF RULES/FORM].

NOTE TO PARAGRAPHS (a) AND (b): Information on how to file with the IARD is available on our Web site at *http://www.sec.gov/iard.* For the annual updating amendment: Summaries of material changes that are not included in the adviser's brochure must be filed with the Commission as an exhibit to Part 2A in the same electronic file; and if you are not required to prepare a brochure, a summary of material changes, an annual updating amendment to your brochure, or Form CRS you are not required to file them with the Commission. See the instructions for Part 2A and Part 3 of Form ADV.

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12. Section 275.204-2 is amended by revising paragraph (a)(14)(i) as follows:

§275.204-2 Books and records to be maintained by investment advisers.

(a) * * *

(14)

(i) A copy of each brochure, brochure supplement and Form CRS, and each amendment or revision to the brochure, brochure supplement and Form CRS, that satisfies the requirements of Part 2 or Part 3 of Form ADV, as applicable [17 CFR 279.1]; any summary of material changes that satisfies the requirements of Part 2 of Form ADV but is not contained in the brochure; and a record of the dates that each brochure, brochure supplement and Form CRS, each amendment or revision thereto, and each summary of material changes not contained in a brochure was given to any client or to any prospective client who subsequently becomes a client.

*** * * * ***

13. Section 275.204-5 is added to read as follows:

§275.204-5 Delivery of Form CRS.

(a) *General requirements.* If you are registered under the Act as an investment adviser, you must deliver Form CRS, required by Part 3 of Form ADV [17 CFR 279.1], to each retail investor.

(b) *Delivery requirements.* You (or a supervised person acting on your behalf) must:

(1) Deliver to each retail investor your current Form CRS before or at the time you enter into an investment advisory contract with that retail investor.

(2) Deliver to each retail investor who is an existing client your current Form CRS before or at the time (i) a new account is opened that is different from the retail investor's existing account(s); or (ii) changes are made to the retail investor's existing account(s) that would materially change the nature and scope of the relationship with the retail investor, including

before or at the time you recommend that the retail investor transfers from an advisory account to a brokerage account, transfers from a brokerage account to an advisory account, or moves assets from one type of account to another in a transaction not in the normal, customary or already agreed course of dealing. Whether a change would require delivery of the Form CRS would depend on the specific facts and circumstances.

(3) Post the current Form CRS prominently on your Web site, if you have one, in a location and format that is easily accessible for retail investors.

(4) Communicate any changes made to Form CRS to each retail investor who is an existing client within 30 days after the amendments are required to be made and without charge. The communication can be made by delivering the amended Form CRS or by communicating the information in another way to the retail investor.

(5) Deliver a current Form CRS to each retail investor within 30 days upon request.

(c) *Other disclosure obligations.* Delivering Form CRS in compliance with this section does not relieve you of any other disclosure obligations you have to your retail investors under any federal or state laws or regulations.

(d) *Definitions.* For purposes of this section:

(1) *Current Form CRS* means the most recent version of the Form CRS.

(2) *Retail investor* means a client or prospective client who is a natural person (an individual). This term includes a trust or other similar entity that represents natural persons, even if another person is a trustee or managing agent of the trust.

(3) *Supervised person* means any of your officers, partners or directors (or other persons occupying a similar status or performing similar functions) or employees, or any other person who provides investment advice on your behalf.

(e) *Transition rule*.

(1) Within 30 days after the date by which you are first required by §275.204-1(b)(3) to electronically file your Form CRS with the Commission, you must deliver to each of your existing clients who is a retail investor your current Form CRS as required by Part 3 of Form ADV.

(2) As of the date by which you are first required to electronically file your Form CRS with the Commission, you must begin using your Form CRS as required by Part 3 of Form ADV to comply with the requirements of paragraph (b) of this section.

14. Section 275.211h-1 is added to read as follows:

§275.211h-1 Disclosure of Registration Status.

(a) An investment adviser registered under section 203 of the Act shall prominently disclose that it is registered with the Commission as an investment adviser in print or electronic retail investor communications.

(b) A supervised person of an investment adviser registered under section 203 of the Act shall prominently disclose that he or she is a supervised person of an investment adviser registered with the Commission in print or electronic retail investor communications.

(c) Such disclosures in paragraphs (a) and (b) of this section shall be provided in the following manner:

(1) For print communications, such status must be displayed in a type size at least as large as and of a font style different from, but at least as prominent as, that used in the majority of the communication. In addition, such disclosure must be presented in the body of the communication and not in a footnote.

(2) For electronic communications, or in any publication by radio or television, such disclosure must be presented in a manner reasonably calculated to draw retail investor attention to it.

(d) The term *retail investor* has the meaning set forth in Rule 204-5 (§275.204-5 of this chapter).

PART 279 – FORMS PRESCRIBED UNDER THE INVESTMENT ADVISERS ACT OF 1940

15. The authority citation for part 279 is revised to read as follows:

Authority: The Investment Advisers Act of 1940, 15 U.S.C. 80b-1, et seq., Pub. L. 111-203, 124 Stat. 1376.

16. Form ADV [referenced in §279.1] is amended by:

a. In the instructions to the form, revising the section entitled "Form ADV: General Instructions." The revised version of Form ADV: General Instructions is attached as Appendix A;

b. In the instructions to the form, adding the section entitled "Form ADV, Part 3: Instructions to Form CRS." The new version of Form ADV, Part 3: Instructions to Form CRS is attached as Appendix B.

By the Commission.

Dated: April 18, 2018.
Brent J. Fields,
SECRETARY.

Note: The text of Form ADV does not and the amendments will not appear in the Code of Federal Regulations.

APPENDICES

FORM ADV (Paper Version)

- **UNIFORM APPLICATION FOR INVESTMENT ADVISER REGISTRATION AND**
- **REPORT FORM BY EXEMPT REPORTING ADVISERS**

Form ADV: General Instructions

Read these instructions carefully before filing Form ADV. Failure to follow these instructions, properly complete the form, or pay all required fees may result in your application or report being delayed or rejected.

In these instructions and in Form ADV, "you" means the investment adviser (*i.e.*, the advisory firm).

If you are a "separately identifiable department or division" (SID) of a bank, "you" means the SID, rather than your bank, unless the instructions or the form provide otherwise.

If you are a *private fund* adviser filing an *umbrella registration*, "you" means the *filing adviser* and each *relying adviser*, unless the instructions or the form provide otherwise. The information in Items 1, 2, 3 and 10 (including corresponding schedules) should be provided for the *filing adviser* only.

Terms that appear in *italics* are defined in the Glossary of Terms to Form ADV.

1. Where can I get more information on Form ADV, electronic filing, and the IARD?

The SEC provides information about its rules and the Advisers Act on its website: <http://www.sec.gov/iard>.

NASAA provides information about state investment adviser laws and state rules, and how to contact a *state securities authority*, on its website: <http://www.nasaa.org>.

FINRA provides information about the IARD and electronic filing on the IARD website: <http://www.iard.com>.

2. What is Form ADV used for?

Investment advisers use Form ADV to:

- Register with the Securities and Exchange Commission
- Register with one or more *state securities authorities*
- Amend those registrations;

- Report to the SEC as an *exempt reporting adviser*
- Report to one or more *state securities authorities* as an *exempt reporting adviser*

- Amend those reports; and
- Submit a final report as an *exempt reporting adviser*

3. How is Form ADV organized?

Form ADV contains five parts:

- Part 1A asks a number of questions about you, your business practices, the *persons* who own and *control* you, and the *persons* who provide investment advice on your behalf.
  - All advisers registering with the SEC or any of the *state securities authorities* must complete Part 1A.

  - *Exempt reporting advisers* (that are not also registering with any *state securities authority*) must complete only the following Items of Part 1A: 1, 2, 3, 6, 7, 10, and 11, as well as corresponding schedules. *Exempt reporting advisers* that are registering with any *state securities authority* must complete all of Form ADV.

  Part 1A also contains several supplemental schedules. The items of Part 1A let you know which schedules you must complete.

  - Schedule A asks for information about your direct owners and executive officers.

  - Schedule B asks for information about your indirect owners.

  - Schedule C is used by paper filers to update the information required by Schedules A and B (see Instruction 18).

  - Schedule D asks for additional information for certain items in Part 1A.

  - Schedule R asks for additional information about *relying advisers*.

  - Disclosure Reporting Pages (or DRPs) are schedules that ask for details about disciplinary events involving you or your *advisory affiliates*.

- Part 1B asks additional questions required by *state securities authorities*. Part 1B contains three additional DRPs. If you are applying for SEC registration or are registered only with the SEC, you do not have to complete Part 1B. (If you are filing electronically and you do not have to complete Part 1B, you will not see Part 1B).

- Part 2A requires advisers to create narrative *brochures* containing information about the advisory firm. The requirements in Part 2A apply to all investment advisers registered with or applying for registration with the SEC, but do not apply to *exempt reporting advisers*. Every application for registration must include a narrative brochure prepared in accordance with the requirements of Part 2A of Form ADV. See Advisers Act Rule 203-1.

- Part 2B requires advisers to create *brochure supplements* containing information about certain *supervised persons*. The requirements in Part 2B apply to all investment advisers registered with or applying for registration with the SEC, but do not apply to *exempt reporting advisers*.

- Part 3 requires advisers to create a *relationship summary* (Form CRS) containing information for *retail investors*. The requirements in Part 3 apply to all investment advisers registered or applying for registration with the SEC, but do not apply to *exempt reporting advisers*. Every adviser that has *retail investors* to whom it must deliver a *relationship summary* must include in the application for registration a *relationship summary* prepared in accordance with the requirements of Part 3 of Form ADV. See Advisers Act Rule 203-1.

4. When am I required to update my Form ADV?

- SEC- and State-Registered Advisers:

  - *Annual updating amendments*: You must amend your Form ADV each year by filing an *annual updating amendment* within 90 days after the end of your fiscal year. When you submit your *annual updating amendment*, you must update your responses to all items, including corresponding sections of Schedules A, B, C, and D and all sections of Schedule R for each *relying adviser*. You must submit your summary of material changes required by Item 2 of Part 2A either in the *brochure* (cover page or the page immediately thereafter) or as an exhibit to your *brochure*.

  - Other-than-annual amendments: In addition to your *annual updating amendment*, if you are registered with the SEC or a *state securities authority*, you must amend Part 1 and Part 2 of your Form ADV, including corresponding sections of Schedules A, B, C, D, and R, by filing additional amendments (other-than-annual amendments) promptly, if:

    - you are adding or removing a *relying adviser* as part of your *umbrella registration;*

    - information you provided in response to Items 1 (except 1.O. and Section 1.F. of Schedule D), 3, 9 (except 9.A.(2), 9.B.(2), 9.E., and 9.F.), or 11 of Part 1A or Items 1, 2.A. through 2.F., or 2.I. of Part 1B or Sections 1 or 3 of Schedule R becomes inaccurate in any way;

    - information you provided in response to Items 4, 8, or 10 of Part 1A, or Item 2.G. of Part 1B, or Section 10 of Schedule R becomes materially inaccurate; or

    - information you provided in your *brochure* becomes materially inaccurate (see note below for exceptions).

Notes: Part 1: If you are submitting an other-than-annual amendment, you are not required to update your responses to Items 2, 5, 6, 7, 9.A.(2), 9.B.(2), 9.E., 9.F., or 12 of Part 1A, Items 2.H. or 2.J. of Part 1B, Section 1.F. of Schedule D or Section 2 of Schedule R even if your responses to those items have become inaccurate.

Part 2: You must amend your *brochure supplements* (see Form ADV, Part 2B) promptly if any information in them becomes materially inaccurate. If you are submitting an other-than-annual amendment to your *brochure*, you are not required to update your summary of material changes as required by Item 2. You are not required to update your *brochure* between annual amendments solely because the amount of *client* assets you manage has changed or because your fee schedule has changed. However, if you are updating your *brochure* for a separate reason in between annual amendments, and the amount of *client* assets you manage listed in response to Item 4.E. or your fee schedule listed in response to Item 5.A. has become materially inaccurate, you should update that item(s) as part of the interim amendment.

- If you are an SEC-registered adviser, you are required to file your *brochure* amendments electronically through IARD. You are not required to file amendments to your *brochure supplements* with the SEC, but you must maintain a copy of them in your files.

- If you are a state-registered adviser, you are required to file your *brochure* amendments and *brochure supplement* amendments with the appropriate *state securities authorities* through IARD.

- Part 3 amendments: You must amend your *relationship summary* and file your *relationship summary* amendments in accordance with the Form ADV, Part 3 (Form CRS), General Instructions, 6.

- *Exempt reporting advisers*:

  - *Annual Updating Amendments*: You must amend your Form ADV each year by filing an *annual updating amendment* within 90 days after the end of your fiscal year. When you submit your *annual updating amendment*, you must update your responses to all required items, including corresponding sections of Schedules A, B, C, and D.

  - Other-than-Annual Amendments: In addition to your *annual updating amendment*, you must amend your Form ADV, including corresponding sections of Schedules A, B, C, and D, by filing additional amendments (other-than-annual amendments) promptly if:

    - information you provided in response to Items 1 (except Item 1.O. and Section 1.F. of Schedule D), 3, or 11 becomes inaccurate in any way; or

- information you provided in response to Item 10 becomes materially inaccurate.

Failure to update your Form ADV, as required by this instruction, is a violation of SEC rules or similar state rules and could lead to your registration being revoked.

5. What is SEC *umbrella registration* and how can I satisfy the requirements of filing an *umbrella registration*?

An *umbrella registration* is a single registration by a *filing adviser* and one or more *relying advisers* who advise only *private funds* and certain separately managed account *clients* that are *qualified clients* and collectively conduct a single advisory business. Absent other facts suggesting that the *filing adviser* and *relying adviser*(s) conduct different businesses, *umbrella registration* is available under the following circumstances:

i. The *filing adviser* and each *relying adviser* advise only *private funds* and *clients* in separately managed accounts that are *qualified clients* and are otherwise eligible to invest in the *private funds* advised by the *filing adviser* or a *relying adviser* and whose accounts pursue investment objectives and strategies that are substantially similar or otherwise related to those *private funds*.

ii. The *filing adviser* has its *principal office and place of business* in the United States and, therefore, all of the substantive provisions of the Advisers Act and the rules thereunder apply to the *filing adviser's* and each *relying adviser's* dealings with each of its *clients*, regardless of whether any *client* of the *filing adviser* or *relying adviser* providing the advice is a *United States person*.

iii. Each *relying adviser*, its *employees* and the *persons* acting on its behalf are subject to the *filing adviser's* supervision and *control* and, therefore, each *relying adviser*, its *employees* and the *persons* acting on its behalf are "persons associated with" the *filing adviser* (as defined in section 202(a)(17) of the Advisers Act).

iv. The advisory activities of each *relying adviser* are subject to the Advisers Act and the rules thereunder, and each *relying adviser* is subject to examination by the SEC.

v. The *filing adviser* and each *relying adviser* operate under a single code of ethics adopted in accordance with SEC rule 204A-1 and a single set of written policies and procedures adopted and implemented in accordance with SEC rule 206(4)-7 and administered by a single chief compliance officer in accordance with that rule.

To satisfy the requirements of Form ADV while using *umbrella registration* the *filing adviser* must sign, file, and update as required, a single Form ADV (Parts 1 and 2) that relates to, and includes all information concerning, the *filing adviser* and each *relying adviser* (*e.g.*, disciplinary information and ownership information), and must include this same information in any other reports or filings it must make under the Advisers Act or the rules

thereunder (*e.g.*, Form PF). The *filing adviser* and each *relying adviser* must not be prohibited from registering with the SEC by section 203A of the Advisers Act (*i.e.*, the *filing adviser* and each *relying adviser* must individually qualify for SEC registration).

Unless otherwise specified, references to "you" in Form ADV refer to both the *filing adviser* and each *relying adviser*. The information in Items 1, 2, 3 and 10 (including corresponding schedules) should be provided for the *filing adviser* only. A separate Schedule R should be completed for each *relying adviser*. References to "you" in Schedule R refer to the *relying adviser* only.

A *filing adviser* applying for registration with the SEC should complete a Schedule R for each *relying adviser*. If you are a *filing adviser* registered with the SEC and would like to add or delete *relying advisers* from an *umbrella registration*, you should file an other-than-annual amendment and add or delete Schedule Rs as needed.

Note: *Umbrella registration* is not available to *exempt reporting advisers*.

6. Where do I sign my Form ADV application or amendment?

You must sign the appropriate Execution Page. There are three Execution Pages at the end of the form. Your initial application, your initial report (in the case of an *exempt reporting adviser*), and all amendments to Form ADV must include at least one Execution Page.

- If you are applying for or are amending your SEC registration, or if you are reporting as an *exempt reporting adviser* or amending your report, you must sign and submit either a:
    - Domestic Investment Adviser Execution Page, if you (the advisory firm) are a resident of the United States; or
    - *Non-Resident* Investment Adviser Execution Page, if you (the advisory firm) are not a resident of the United States.

- If you are applying for or are amending your registration with a *state securities authority*, you must sign and submit the State-Registered Investment Adviser Execution Page.

7. Who must sign my Form ADV or amendment?

The individual who signs the form depends upon your form of organization:

- For a sole proprietorship, the sole proprietor.
- For a partnership, a general partner.
- For a corporation, an authorized principal officer.
- For a "separately identifiable department or division" (SID) of a bank, a principal officer of your bank who is directly engaged in the management, direction, or supervision of your investment advisory activities.
- For all others, an authorized individual who participates in managing or directing your affairs.

The signature does not have to be notarized, and in the case of an electronic filing, should be a typed name.

8. How do I file my Form ADV?

Complete Form ADV electronically using the Investment Adviser Registration Depository (IARD) if:

- You are filing with the SEC (and submitting *notice filings* to any of the *state securities authorities*), or

- You are filing with a *state securities authority* that requires or permits advisers to submit Form ADV through the IARD.

  Note: SEC rules require advisers that are registered or applying for registration with the SEC, or that are reporting to the SEC as an *exempt reporting adviser*, to file electronically through the IARD system. See SEC rules 203-1 and 204-4.

To file electronically, go to the IARD website (<www.iard.com>), which contains detailed instructions for advisers to follow when filing through the IARD.

Complete Form ADV (Paper Version) on paper if:

- You are filing with the SEC or a *state securities authority* that requires electronic filing, but you have been granted a continuing hardship exemption. Hardship exemptions are described in Instruction 17.

- You are filing with a *state securities authority* that permits (but does not require) electronic filing and you do not file electronically.

9. How do I get started filing electronically?

First, obtain a copy of the IARD Entitlement Package from the following website: <http://www.iard.com/GetStarted.asp>. Second, request access to the IARD system for your firm by completing and submitting the IARD Entitlement Package. The IARD Entitlement Package explains how the form may be submitted. Mail the forms to: FINRA Entitlement Group, 9509 Key West Avenue, Rockville, MD 20850.

When FINRA receives your Entitlement Package, they will assign a *CRD* number (identification number for your firm) and a user I.D. code and password (identification number and system password for the individual(s) who will submit Form ADV filings for your firm). Your firm may request an I.D. code and password for more than one individual. FINRA also will create a financial account for you from which the IARD will deduct filing fees and any state fees you are required to pay. If you already have a *CRD* account with FINRA, it will also serve as your IARD account; a separate account will not be established.

Once you receive your *CRD* number, user I.D. code and password, and you have funded your account, you are ready to file electronically.

Questions regarding the Entitlement Process should be addressed to FINRA at 240.386.4848.

10. If I am applying for registration with the SEC, or amending my SEC registration, how do I make *notice filings* with the *state securities authorities*?

If you are applying for registration with the SEC or are amending your SEC registration, one or more *state securities authorities* may require you to provide them with copies of your SEC filings. We call these filings "*notice filings*." Your *notice filings* will be sent electronically to the states that you check on Item 2.C. of Part 1A. The *state securities authorities* to which you send *notice filings* may charge fees, which will be deducted from the account you establish with FINRA. To determine which *state securities authorities* require SEC-registered advisers to submit *notice filings* and to pay fees, consult the relevant state investment adviser law or *state securities authority*. See General Instruction 1.

If you are granted a continuing hardship exemption to file Form ADV on paper, FINRA will enter your filing into the IARD and your *notice filings* will be sent electronically to the *state securities authorities* that you check on Item 2.C. of Part 1A.

11. I am registered with a state. When must I switch to SEC registration?

If at the time of your *annual updating amendment* you meet at least one of the requirements for SEC registration in Item 2.A.(1) to (12) of Part 1A, you must apply for registration with the SEC within 90 days after you file the *annual updating amendment*. Once you register with the SEC, you are subject to SEC regulation, regardless of whether you remain registered with one or more states. See SEC rule 203A-1(b)(2). Each of your *investment adviser representatives*, however, may be subject to registration in those states in which the representative has a place of business. See Advisers Act section 203A(b)(1); SEC rule 203A-3(a). For additional information, consult the investment adviser laws or the *state securities authority* for the particular state in which you are "doing business." See General Instruction 1.

12. I am registered with the SEC. When must I switch to registration with a *state securities authority*?

If you check box 13 in Item 2.A. of Part 1A to report on your *annual updating amendment* that you are no longer eligible to register with the SEC, you must withdraw from SEC registration within 180 days after the end of your fiscal year by filing Form ADV-W. See SEC rule 203A-1(b)(2). You should consult state law or the *state securities authority* for the states in which you are "doing business" to determine if you are required to register in these states. See General Instruction 1. Until you file your Form ADV-W with the SEC, you will remain subject to SEC regulation, and you also will be subject to regulation in any states where you register. See SEC rule 203A-1(b)(2).

13. I am an *exempt reporting adviser*. When must I submit my first report on Form ADV?

- All *exempt reporting advisers*:
  You must submit your initial Form ADV filing within 60 days of relying on the exemption from registration under either section 203(l) of the Advisers Act as an adviser solely to one or more venture capital funds or section 203(m) of the Advisers Act because you act solely as an adviser to private funds and have assets under management in the United States of less than $150 million.

- Additional instruction for advisers switching from being registered to being *exempt reporting advisers*:
  If you are currently registered as an investment adviser (or have an application for registration pending) with the SEC or with a *state securities authority*, you must file a Form ADV-W to withdraw from registration in the jurisdictions where you are switching. You must submit the Form ADV-W before submitting your first report as an *exempt reporting adviser*.

14. I am an *exempt reporting adviser*. Is it possible that I might be required to also register with or submit a report to a *state securities authority*?

Yes, you may be required to register with or submit a report to one or more *state securities authorities*. If you are required to register with one or more *state securities authorities*, you must complete all of Form ADV. See General Instruction 3. If you are required to submit a report to one or more *state securities authorities*, check the box(es) in Item 2.C. of Part 1A next to the state(s) you would like to receive the report. Each of your *investment adviser representatives* may also be subject to registration requirements. For additional information about the requirements that may apply to you, consult the investment adviser laws or the *state securities authority* for the particular state in which you are "doing business." See General Instruction 1.

15. What do I do if I no longer meet the definition of "*exempt reporting adviser*"?

- Advisers Switching to SEC Registration:

  - You may no longer be an *exempt reporting adviser* and may be required to register with the SEC if you wish to continue doing business as an investment adviser. For example, you may be relying on section 203(l) and wish to accept a *client* that is not a venture capital fund as defined in SEC rule 203(l)-1, or you may have been relying on SEC rule 203(m)-1 and reported in Section 2.B. of Schedule D to your *annual updating amendment* that you have *private fund* assets of $150 million or more.

    - If you are relying on section 203(l), unless you qualify for another exemption, you would violate the Advisers Act's registration requirement if you accept a *client* that is not a venture capital fund as defined in SEC rule 203(l)-1 before

the SEC approves your application for registration. You must submit your final report as an *exempt reporting adviser* and apply for SEC registration in the same filing.

- If you were relying on SEC rule 203(m)-1 and you reported in Section 2.B. of Schedule D to your *annual updating amendment* that you have *private fund* assets of $150 million or more, you must register with the SEC unless you qualify for another exemption. If you have complied with all SEC reporting requirements applicable to an *exempt reporting adviser* as such, you have up to 90 days after filing your *annual updating amendment* to apply for SEC registration, and you may continue doing business as a *private fund* adviser during this time. You must submit your final report as an *exempt reporting adviser* and apply for SEC registration in the same filing. Unless you qualify for another exemption, you would violate the Advisers Act's registration requirement if you accept a *client* that is not a *private fund* during this transition period before the SEC approves your application for registration, and you must comply with all SEC reporting requirements applicable to an *exempt reporting adviser* as such during this 90-day transition period. If you have not complied with all SEC reporting requirements applicable to an *exempt reporting adviser* as such, this 90-day transition period is not available to you. Therefore, if the transition period is not available to you, and you do not qualify for another exemption, your application for registration must be approved by the SEC before you meet or exceed SEC rule 203(m)-1's $150 million asset threshold.

- You will be deemed in compliance with the Form ADV filing and reporting requirements until the SEC approves or denies your application. If your application is approved, you will be able to continue business as a registered adviser.

- If you register with the SEC, you may be subject to state *notice filing* requirements. To determine these requirements, consult the investment adviser laws or the *state securities authority* for the particular state in which you are "doing business." See General Instruction 1.

Note: If you are relying on SEC rule 203(m)-1 and you accept a *client* that is not a *private fund*, you will lose the exemption provided by SEC rule 203(m)-1 immediately. To avoid this result, you should apply for SEC registration in advance so that the SEC has approved your registration before you accept a *client* that is not a *private fund*.

The 90-day transition period described above also applies to investment advisers with their *principal offices and places of business* outside of the United States with respect to their *clients* who are *United States persons* (*e.g.*, the adviser would not be eligible for the 90-day transition period if it accepted a *client* that is a *United States person* and is not a *private fund*).

- Advisers Not Switching to SEC Registration:

- You may no longer be an *exempt reporting adviser* but may not be required to register with the SEC or may be prohibited from doing so. For example, you may cease to do business as an investment adviser, become eligible for an exemption that does not require reporting, or be ineligible for SEC registration. In this case, you must submit a final report as an *exempt reporting adviser* to update only Item 1 of Part 1A of Form ADV.

- You may be subject to state registration requirements. To determine these requirements, consult the investment adviser laws or the *state securities authority* for the particular state in which you are "doing business." See General Instruction 1.

16. Are there filing fees?

Yes. These fees go to support and maintain the IARD. The IARD filing fees are in addition to any registration or other fee that may be required by state law. You must pay an IARD filing fee for your initial application, your initial report, and each *annual updating amendment*. There is no filing fee for an other-than-annual amendment, a final report as an *exempt reporting adviser*, or Form ADV-W. The IARD filing fee schedule is published at <http://www.sec.gov/iard>; <http://www.nasaa.org>; and <http://www.iard.com>.

If you are submitting a paper filing under a continuing hardship exemption (see Instruction 17), you are required to pay an additional fee. The amount of the additional fee depends on whether you are filing Form ADV or Form ADV-W. (There is no additional fee for filings made on Form ADV-W.) The hardship filing fee schedule is available by contacting FINRA at 240.386.4848.

17. What if I am not able to file electronically?

If you are required to file electronically but cannot do so, you may be eligible for one of two types of hardship exemptions from the electronic filing requirements.

- A **temporary hardship exemption** is available if you file electronically, but you encounter unexpected difficulties that prevent you from making a timely filing with the IARD, such as a computer malfunction or electrical outage. This exemption does <u>not</u> permit you to file on paper; instead it extends the deadline for an electronic filing for seven business days. See SEC rules 203-3(a) and 204-4(e).

- A **continuing hardship exemption** may be granted if you are a small business and you can demonstrate that filing electronically would impose an undue hardship. You are a small business, and may be eligible for a continuing hardship exemption, if you are required to answer Item 12 of Part 1A (because you have assets under management of less than $25 million) <u>and</u> you are able to respond "no" to each question in Item 12. See SEC rule 0-7.

If you have been granted a continuing hardship exemption, you must complete and submit the paper version of Form ADV to FINRA. FINRA will enter your responses into the IARD. As discussed in General Instruction 16, FINRA will charge you a fee to reimburse it for the expense of data entry.

18. I am eligible to file on paper. How do I make a paper filing?

When filing on paper, you must:

- Type all of your responses.
- Include your name (the same name you provide in response to Item 1.A. of Part 1A) and the date on every page.
- If you are amending your Form ADV:
  - complete page 1 and circle the number of any item for which you are changing your response.
  - include your SEC 801-number (if you have one), or your 802-number (if you have one), and your *CRD* number (if you have one) on every page.
  - complete the amended item in full and circle the number of the item for which you are changing your response.
  - to amend Schedule A or Schedule B, complete and submit Schedule C.

Where you submit your paper filing depends on why you are eligible to file on paper:

- If you are filing on paper because you have been granted a continuing hardship exemption, submit one manually signed Form ADV and one copy to: IARD Document Processing, FINRA, P.O. Box 9495, Gaithersburg, MD 20898-9495.

  If you complete Form ADV on paper and submit it to FINRA but you do not have a continuing hardship exemption, the submission will be returned to you.

- If you are filing on paper because a state in which you are registered or in which you are applying for registration allows you to submit paper instead of electronic filings, submit one manually signed Form ADV and one copy to the appropriate *state securities authorities*.

19. Who is required to file Form ADV-NR?

Every *non-resident* general partner and *managing agent* of <u>all</u> SEC-registered advisers and *exempt reporting advisers*, whether or not the adviser is resident in the United States, must file Form ADV-NR in connection with the adviser's initial application or report. A general partner or *managing agent* of an SEC-registered adviser or *exempt reporting adviser* who becomes a *non-resident* after the adviser's initial application or report has been submitted must file Form ADV-NR within 30 days. Form ADV-NR must be filed on paper (it cannot be filed electronically).

Submit Form ADV-NR to the SEC at the following address:

Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549; Attn: OCIE Registrations Branch.

Failure to file Form ADV-NR promptly may delay SEC consideration of your initial application.

Federal Information Law and Requirements

Sections 203 and 204 of the Advisers Act [15 U.S.C. §§ 80b-3 and 80b-4] authorize the SEC to collect the information required by Form ADV. The SEC collects the information for regulatory purposes, such as deciding whether to grant registration. Filing Form ADV is mandatory for advisers who are required to register with the SEC and for *exempt reporting advisers*. The SEC maintains the information submitted on this form and makes it publicly available. The SEC may return forms that do not include required information. Intentional misstatements or omissions constitute federal criminal violations under 18 U.S.C. § 1001 and 15 U.S.C. § 80b-17.

SEC's Collection of Information

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number. The Advisers Act authorizes the SEC to collect the information on Form ADV from investment advisers. See 15 U.S.C. §§ 80b-3 and 80b-4. Filing the form is mandatory.

The form enables the SEC to register investment advisers and to obtain information from and about *exempt reporting advisers*. Every applicant for registration with the SEC as an adviser, and every *exempt reporting adviser*, must file the form. See 17 C.F.R. §§ 275.203-1 and 204-4. By accepting a form, however, the SEC does not make a finding that it has been completed or submitted correctly. The form is filed annually by every adviser, no later than 90 days after the end of its fiscal year, to amend its registration or its report. It is also filed promptly during the year to reflect material changes. See 17 C.F.R. § 275.204-1. The SEC maintains the information on the form and makes it publicly available through the IARD.

Anyone may send the SEC comments on the accuracy of the burden estimate on page 1 of the form, as well as suggestions for reducing the burden. The Office of Management and Budget has reviewed this collection of information under 44 U.S.C. § 3507.

The information contained in the form is part of a system of records subject to the Privacy Act of 1974, as amended. The SEC has published in the Federal Register the Privacy Act System of Records Notice for these records.

[Form ADV, Part 3:][1] Instructions to Form CRS

General Instructions

Under rule 17a-14 under the Securities Exchange Act of 1934 and rule 204-5 under the Investment Advisers Act of 1940, broker-dealers registered under section 15 of the Exchange Act and investment advisers registered under section 203 of the Advisers Act are required to deliver to *retail investors* a *relationship summary* disclosing information about the firm. Read all the General Instructions as well as the particular item requirements before preparing or updating the *relationship summary*.

1. Narrative and Graphical Format.

   a. The *relationship summary* must include the required items enumerated below. The items require you to provide specific information and, in some cases, prescribe the particular wording that you must use.

   b. You must respond to each item and must provide responses in the same order as the items appear in these instructions. Unless otherwise noted, you must also present the required information within each item in the order listed.

   c. Whether in electronic or paper format, the *relationship summary* must not exceed four 8½" x 11" pages if converted to PDF format, using at least an 11 point font size and a minimum 0.75" margins on all sides.

   d. You may not include disclosure in the *relationship summary* other than disclosure that is required or permitted by these Instructions and the applicable item.

   e. If you are a *dual registrant*, present the information in Items 2 through 4 and Item 6 in a tabular format, comparing advisory services and brokerage services side-by-side. In the column discussing brokerage services, include the heading "Broker-Dealer Services" and the sub-heading "Brokerage Accounts." In the column discussing investment advisory services, include the heading "Investment Adviser Services" and the sub-heading "Advisory Accounts." *Dual registrants* should not complete Item 5, which must be completed by *standalone investment advisers and standalone broker-dealers*.

   f. You may use charts, graphs, tables, and other graphics or text features to explain the required information, so long as the information: (i) is responsive to and meets the requirements in these instructions (including space limitations); (ii) is not inaccurate or misleading; and (iii) does not, because of the nature, quantity, or manner of presentation, obscure or impede understanding of the information that must be included. When using interactive graphics or tools, you may include instructions on their use and interpretation.

[1] The bracketed text will be included for Form ADV, Part 3 (17 CFR 279.1) only.

g. In a *relationship summary* that is posted on your website or otherwise provided electronically, you must use hyperlinks for any document that is cross-referenced in the *relationship summary* if the document is available online. See General Instruction 8.a. You may add embedded hyperlinks within the *relationship summary* in order to supplement required disclosures, for example, links to fee schedules, conflicts disclosures, the firm's narrative brochure required by Part 2A of Form ADV, or other regulatory disclosures.

2. Plain Language. The items of the *relationship summary* are designed to promote effective communication between you and *retail investors*. Write your *relationship summary* in plain language, taking into consideration *retail investors'* level of financial experience. The *relationship summary* should be concise and direct. In drafting the *relationship summary*: (i) use short sentences; (ii) use definite, concrete, everyday words; (iii) use active voice; (iv) avoid legal jargon or highly technical business terms unless you clearly explain them or you believe that reasonable *retail investors* will understand them; and (v) avoid multiple negatives. You must write the *relationship summary* as if you are speaking to the *retail investor*, using "you," "us," "our firm," etc.

   Note: The SEC's Office of Investor Education and Advocacy has published A Plain English Handbook. You may find the handbook helpful in writing your relationship summary. For a copy of this handbook, visit the SEC's website at *www.sec.gov/news/extra/handbook.htm* or call 1-800-732-0330.

3. Full and Truthful Disclosure. All information in your *relationship summary* must be true and may not omit any material facts necessary to make the disclosures required by these Instructions and the applicable item not misleading. If a statement is inapplicable to your business or would be misleading to a reasonable *retail investor*, you may omit or modify that statement.

   Broker-dealers and investment advisers have disclosure and reporting obligations under state and federal law, including, but not limited to, obligations under the Exchange Act, the Advisers Act, and the respective rules thereunder. Broker-dealers are also subject to disclosure obligations under the rules of self-regulatory organizations. Delivery of this document will not necessarily satisfy the additional disclosure requirements that you have under the federal securities laws and regulations or other laws.

4. Preserving Records. You must maintain a copy of each version of the *relationship summary* and make it available to the SEC staff upon request. See SEC Advisers Act rule 204-2(a)(14)(i); SEC Exchange Act rule 17a-4.

5. Initial Filing and Delivery; Transition Provisions.

   a. **Initial filing.** If you are a registered investment adviser and are required to give a *relationship summary* to a *retail investor*, you must complete Form ADV, Part 3 (Form

CRS) and file it electronically in a text-searchable format with the Investment Adviser Registration Depository (IARD). If you are a registered broker-dealer and are required to give a *relationship summary* to a *retail investor*, you must complete Form CRS and file it electronically in a text-searchable format with the Electronic Data Gathering, Analysis and Retrieval System ("EDGAR").

If you do not have any *retail investors* to whom you must deliver a *relationship summary*, you are not required to prepare one.

Note to instruction 5(a): If you are a *dual registrant* and are required to give a *relationship summary* to one or more *retail investor* clients or customers of both your advisory and brokerage businesses, you must prepare only one *relationship summary* and file it on IARD and EDGAR.

Information for investment advisers on how to file with IARD is available on the Commission's website at www.sec.gov/iard. Information for broker-dealers on how to file with the Commission on EDGAR is available on the Commission's website at https://www.sec.gov/edgar.

b. **Initial delivery.** You must give a *relationship summary* to each *retail investor*, if you are an investment adviser, before or at the time you enter into an investment advisory agreement with the *retail investor*, or if you are a broker-dealer, before or at the time the *retail investor* first engages your services. See SEC Advisers Act rule 204-5(b)(1) and SEC Exchange Act rule 17a-14(c)(1). You must deliver the *relationship summary* even if your agreement with the *retail investor* is oral. A *dual registrant* should deliver the *relationship summary* at the earlier of entering into an investment advisory agreement with the *retail investor* or the *retail investor* engaging the firm's services.

c. **Transition provisions for initial filing and delivery after the effective date of the new Form CRS requirements**.

(i) If you are a broker-dealer, you must file your initial *relationship summary* with the Commission as required by instruction 5.a, by [INSERT DATE SIX MONTHS AFTER EFFECTIVE DATE OF RULES/FORM]. If you are an investment adviser or a *dual registrant*, you must amend your Form ADV by electronically filing with IARD your initial *relationship summary* as part of the next annual updating amendment you are required to file after [INSERT DATE SIX MONTHS AFTER EFFECTIVE DATE OF RULES/FORM].

(ii) As of the date by which you are first required to electronically file your *relationship summary* with the Commission, you must begin to deliver your *relationship summary* to new and prospective clients and customers who are *retail investors* as required by Instruction 5.b.

(iii) Within 30 days after the date by which you are first required to electronically file your *relationship summary* with the Commission, you must deliver your *relationship summary* to each of your existing clients and customers who are *retail investors*.

6. Updating Relationship Summary.

   a. You must update your *relationship summary* within 30 days whenever any information in the *relationship summary* becomes materially inaccurate.

   b. You must communicate any changes in the updated *relationship summary* to *retail investors* who are existing clients or customers of the firm within 30 days after the updates are required to be made and without charge. You can make the communication by delivering the amended *relationship summary* or by communicating the information in another way to the *retail investor*.

   c. You must file each amended *relationship summary* electronically with the Commission, on IARD if you are an investment adviser or *dual registrant*, and on EDGAR if you are a broker-dealer.

7. Additional Delivery Requirements to Existing Clients and Customers.

   a. You must deliver the *relationship summary* to a *retail investor* who is an existing client or customer before or at the time: (i) a new account is opened that is different from the *retail investor's* existing account(s); or (ii) changes are made to the *retail investor's* existing account(s) that would materially change the nature and scope of your relationship with the *retail investor*. For example, you must deliver a *relationship summary* before or at the time you recommend that the *retail investor* transfers from an investment advisory account to a brokerage account, transfers from a brokerage account to an investment advisory account, or moves assets from one type of account to another in a transaction not in the normal, customary or already agreed course of dealing. Whether a change would require delivery of the *relationship summary* would depend on the specific facts and circumstances.

   b. You also must deliver the *relationship summary* to a *retail investor* within 30 days upon the *retail investor's* request.

8. Electronic Posting and Manner of Delivery.

   a. You must post the current version of the *relationship summary* prominently on your public website, if you have one, in a location and format that is easily accessible for *retail investors*. If you do not have a public website, include in your *relationship summary* a toll-free number that *retail investors* may call to request documents.

   b. You may deliver the *relationship summary* electronically, including updates, consistent with SEC guidance regarding electronic delivery of documents, in particular *Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information*, which you can find at www.sec.gov/rules/concept/33-7288.txt.

   c. If the relationship summary is delivered on paper and not as a standalone document, you

should ensure that it is the first among any documents that are delivered at that time.

9. Definitions.

For purposes of this Form CRS, the following terms have the meanings ascribed to them below:

a. **Affiliate:** Any persons directly or indirectly controlling or controlled by you or under common control with you.

b. **Dual registrant:** A firm that is dually registered as a broker-dealer and an investment adviser and offers services to *retail investors* as both a broker-dealer and an investment adviser.

c. **Portfolio Manager:** An investment adviser that manages investments in a *wrap fee program*.

d. **Relationship summary:** A written disclosure statement that you must provide to *retail investors*. *See* Advisers Act rule 204-5; Exchange Act rule 17a-14; Form CRS.

e. **Retail investor:** A prospective or existing client or customer who is a natural person (an individual). This term includes a trust or other similar entity that represents natural persons, even if another person is a trustee or managing agent of the trust.

f. **Standalone investment adviser** and **standalone broker-dealer:** A *standalone investment adviser* is a registered investment adviser that offers services to *retail investors* and (i) is not dually registered as a broker-dealer or (ii) is dually registered as a broker-dealer but does not offer services to *retail investors* as a broker-dealer. A *standalone broker-dealer* is a registered broker-dealer that offers services to *retail investors* and (i) is not dually registered as an investment adviser or (ii) is dually registered as an investment adviser but does not offer services to *retail investors* as an investment adviser.

g. **Wrap fee program**: An advisory program under which a specified fee or fees not based directly upon transactions in a *retail investor's* account is charged for investment advisory services (which may include portfolio management or advice concerning the selection of other investment advisers) and the execution of *retail investor* transactions.

[Form ADV, Part 3:] Form CRS

Item 1: Introduction

A. State your name, whether you are registered with the Securities and Exchange Commission as a broker-dealer, investment adviser, or both, and the date of the *relationship summary*. This information should be disclosed prominently on the first page, and can be included in the header or footer.

B. **Standalone Broker-Dealers:** If you are a *standalone broker-dealer*, include the title "Is a Brokerage Account Right for You?" Include the following introductory paragraphs (emphasis required):

"There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you.

We are a broker-dealer and provide brokerage accounts and services rather than advisory accounts and services. This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page [ ]."

C. **Standalone Investment Advisers:** If you are a *standalone investment adviser*, include the title "Is an Investment Advisory Account Right for You?" Include the following introductory paragraphs (emphasis required):

"There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you.

We are an investment adviser and provide advisory accounts and services rather than brokerage accounts and services. This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page [ ]."

D. **Dual Registrants:** If you are a *dual registrant*, include the title "Which Type of Account is Right for You – Brokerage, Investment Advisory or Both?" Include the following introductory paragraphs (emphasis required):

"There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you.

Depending on your needs and investment objectives, we can provide you with services in a brokerage account, investment advisory account, or both at the same time. This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page [ ]."

Item 2: Relationships and Services

A. Include the heading "[Types of] Relationships and Services." If you are a *standalone broker-dealer* or *standalone investment adviser*, omit the bracketed language. If you are a *dual registrant*, include the bracketed language in the heading, and include the following after the heading: "Our accounts and services fall into two categories."

B. **Brokerage Account Services:** If you are a broker-dealer that offers brokerage accounts to *retail investors*, summarize the principal brokerage services that you provide to *retail investors*. You must address the following, unless not applicable:

1. Include the following (emphasis required): "If you open a brokerage account, you will pay us a ***transaction-based fee***, generally referred to as a commission, every time you buy or sell an investment."

2. If you offer accounts in which you offer recommendations to *retail investors*, state that the *retail investor* may select investments or you may recommend investments for the *retail investor's* account, but the *retail investor* will make the ultimate investment decision regarding the investment strategy and the purchase or sale of investments. If you only offer accounts in which you do not offer recommendations to *retail investors* (*e.g.*, execution-only brokerage services), state that the *retail investor* will select the investments and the *retail investor* will make the ultimate investment decision regarding the investment strategy and the purchase or sale of investments.

3. State if you offer to *retail investors* additional services, including, for example: (a) assistance with developing or executing the *retail investor's* investment strategy (*e.g.*, you discuss the *retail investor's* investment goals or you design with the *retail investor* a strategy to achieve the *retail investor's* investment goals), or (b) monitoring the performance of the *retail investor's* account. Indicate whether these services can be offered as additional services or are part of the standard brokerage account services, and whether a retail investor will pay more for these services. If you offer monitoring (as reflected in (b) above), as part of the standard brokerage account services, indicate how frequently you monitor the performance. Briefly describe any regular communications you have with *retail investors*, including the frequency and method of the communications.

4. If you significantly limit the types of investments available to *retail investors* in any accounts, include the following: "We offer a limited selection of investments. Other firms could offer a wider range of choices, some of which might have lower costs." You significantly limit the types of investments if, for example, you only offer one type of asset (*e.g.*, mutual funds, exchange-traded funds, or variable annuities), you only offer mutual funds or other investments sponsored or managed by you or an affiliate (*i.e.*, proprietary products), or you only offer a small number of investments. If such limits only apply to certain accounts that you offer, identify those accounts.

C. **Investment Advisory Account Services**: If you are an investment adviser that offers investment advisory accounts to *retail investors*, summarize the principal investment advisory services that you provide to *retail investors*. You must address the following, unless not applicable:

1. State the type of fee you receive as compensation if the *retail investor* opens an investment advisory account. For example, state if you charge an on-going asset-based fee based on the value of cash and investments in the advisory account, a fixed fee, or some other fee arrangement. Emphasize the type of fee in bold and italicized font. If you are a *standalone adviser*, also state how frequently you assess the fee.

2. State that you offer advice on a regular basis, or, if you do not offer advice on a regular basis, state how frequently you offer advice. State the services you offer to *retail investors* including, for example, (a) assistance with developing the *retail investor's* investment strategy (*e.g.*, you discuss the *retail investor's* investment goals or you design with the *retail investor* a strategy to achieve the *retail investor's* investment goals); or (b) how frequently you monitor the *retail investor's* accounts. Briefly describe any regular communications you have with *retail investors*, including the frequency and method of the communications.

3. State if you offer advisory accounts for which you exercise discretion (*i.e.*, discretionary accounts), accounts where you do not exercise discretion (*i.e.*, non-discretionary accounts), or both. Emphasize the type of account (discretionary and non-discretionary) in bold and italicized font. If you offer a discretionary account, state that it allows you to buy and sell investments in the *retail investor's* account, without asking the *retail investor* in advance. If you offer a non-discretionary account, state that you give advice and the *retail investor* decides what investments to buy and sell.

4. If you significantly limit the types of investments available to *retail investors* in any accounts, include the following: "Our investment advice will cover a limited selection of investments. Other firms could provide advice on a wider range of choices, some of which might have lower costs." You significantly limit the types of investments if, for example, you only offer one type of asset

(*e.g.*, mutual funds, exchange-traded funds, or variable annuities), you only offer mutual funds or other investments sponsored or managed by you or an affiliate (*i.e.*, proprietary products), or you only offer a small number of investments. If such limits only apply to certain accounts that you offer, identify those accounts.

D. **Affiliate Services:** If you are a *standalone investment adviser or standalone broker-dealer* and have *affiliates* that offer to *retail investors* brokerage or advisory services, respectively, you may state that you provide *retail investors* with certain brokerage or advisory services of your *affiliates*, as applicable.

Item 3: Standard of Conduct

A. Include the heading "Our Obligations to You" and the following language after the heading: "We must abide by certain laws and regulations in our interactions with you."

B. **Broker-Dealers**: If you are a broker-dealer that offers brokerage accounts to *retail investors*, include the following:

1. "[We must act in your best interest and not place our interests ahead of yours when we recommend an investment or an investment strategy involving securities.] When we provide any service to you, we must treat you fairly and comply with a number of specific obligations. Unless we agree otherwise, we are not required to monitor your portfolio or investments on an ongoing basis." Include the bracketed language only if you offer recommendations subject to Exchange Act Rule 15*l*-1 ("Regulation Best Interest").

2. "Our interests can conflict with your interests. [When we provide recommendations, we must eliminate these conflicts or tell you about them and in some cases reduce them]." Include the bracketed language only if you offer recommendations subject to Regulation Best Interest.

C. **Investment Advisers**: If you are an investment adviser that offers investment advisory accounts to *retail investors*, include the following:

1. "We are held to a fiduciary standard that covers our entire investment advisory relationship with you. [For example, we are required to monitor your portfolio, investment strategy and investments on an ongoing basis.]" If you do not provide ongoing advice (for example, if you only provide a one-time financial plan), omit the bracketed sentence.

2. "Our interests can conflict with your interests. We must eliminate these conflicts or tell you about them in a way you can understand, so that you can decide whether or not to agree to them."

Item 4: Summary of Fees and Costs

A. Include the heading "Fees and Costs" and the following language after the heading: "Fees and costs affect the value of your account over time. Please ask your financial professional to give you personalized information on the fees and costs that you will pay."

B. **Brokerage Account Fees and Costs**: If you are a broker-dealer that offers brokerage accounts to *retail investors*, summarize the principal fees and costs that *retail investors* will incur.

1. If you are a *dual registrant* include the following (emphasis required): "*Transaction-based fees.* You will pay us a fee every time you buy or sell an investment. This fee, commonly referred to as a commission, is based on the specific transaction and not the value of your account." If you are a *standalone broker-dealer* include the following: "The fee you pay is based on the specific transaction and not the value of your account."

2. Include the following (emphasis required):

   (a) "With stocks or exchange-traded funds, this fee is usually a separate commission. With other investments, such as bonds, this fee might be part of the price you pay for the investment (called a "***mark-up***" or "***mark down***"). With mutual funds, this fee (typically called a "***load***") reduces the value of your investment."

   (b) State that some investments impose additional fees that will reduce the value of *retail investors'* investments over time and provide examples of such investments that you offer to *retail investors* (*e.g.*, mutual funds and variable annuities). Also state that a *retail investor* could be required to pay fees when certain investments are sold (*e.g.*, surrender charges for selling variable annuities).

3. State whether your fees vary and are negotiable, and describe the key factors that you believe would help a reasonable *retail investor* understand the fee that he or she is likely to pay for your services (*e.g.*, how much the *retail investor* buys or sells, what type of investment the *retail investor* buys or sells, and what kind of account the *retail investor* has with you).

4. State, if applicable, that a *retail investor* will also pay other fees in addition to the firm's principal fees. List other fees the *retail investor* will pay, including, but not limited to, custodian fees, account maintenance fees and account inactivity fees.

5. Include the following: "The more transactions in your account, the more fees we charge you. We therefore have an incentive to encourage you to engage in

transactions."

6. If you are a *dual registrant* include the following: "From a cost perspective, you may prefer a transaction-based fee if you do not trade often or if you plan to buy and hold investments for longer periods of time."

C. **Investment Advisory Account Fees and Costs**: If you are an investment adviser that offers investment advisory accounts to *retail investors*, summarize the principal fees and costs that *retail investors* will incur. Your determination of the principal fees for investment advisory services should align with the type of fee(s) that you report in response to Form ADV Part 1A, Item 5.E. Include information about each type of fee you report that is responsive to this Item 4.C.

1. If you are a *dual registrant* include the following if you charge an asset-based fee (emphasis required): "*Asset-based fees*. You will pay an on-going fee [at the end of each quarter] based on the value of the cash and investments in your advisory account." Replace the brackets with how frequently you assess the fee. If you charge another type of fee instead of an asset-based fee for your advisory services, briefly describe that fee and how frequently it is assessed.

2. Include the following: "The amount paid to our firm and your financial professional generally does not vary based on the type of investments we select on your behalf. [The asset-based fee reduces the value of your account and will be deducted from your account.]" Include the bracketed language if you charge an ongoing asset-based fee for your advisory accounts. If you charge another type of fee, succinctly describe how it is assessed and the impact it has on the value of the *retail investor's* account.

3. If you provide advice to *retail investors* about investing in a *wrap fee program* (and do not also offer *retail investors* another type of advisory account), include the following (emphasis required): "We offer advisory accounts called ***wrap fee programs***. In a ***wrap fee program***, the asset-based fee will include most transaction costs and fees to a broker-dealer or bank that will hold your assets (called "***custody***"), and as a result wrap fees are typically higher than non-wrap advisory fees." If you offer *retail investors* a *wrap fee program* as well as another type of advisory account, include the following (emphasis required): "For some advisory accounts, called ***wrap fee programs***, the asset-based fee will include most transaction costs and custody services, and as a result wrap fees are typically higher than non-wrap advisory fees."

4. State that some investments impose additional fees that will reduce the value of *retail investors'* investments over time and provide examples of such investments that you offer to *retail investors* (*e.g.*, mutual funds and variable annuities). Also state that a *retail investor* could be required to pay fees when certain investments are sold (*e.g.,* surrender charges for selling variable

annuities).

5. State whether your fees vary and are negotiable, and describe the key factors that you believe would help a reasonable *retail investor* understand the fee that he or she is likely to pay for your services (*e.g.*, the services your receive and the amount of assets in your account).

6. State, if applicable, that a *retail investor* will pay transaction-based fees when you buy and sell an investment for the *retail investor* (*e.g.*, commissions paid to broker-dealers for buying or selling investments) in addition to the firm's principal fee it charges *retail investors* for the firm's advisory accounts. Also state, if applicable, that a *retail investor* will pay fees to a broker-dealer or bank that will hold the *retail investor's* assets and that this is called custody. List other fees the *retail investor* will pay, including, but not limited to, account maintenance services.

7. If you provide advice to *retail investors* about investing in a *wrap fee program*, include the following: "Although transaction fees are usually included in the wrap program fee, sometimes you will pay an additional transaction fee (for investments bought and sold outside the wrap fee program)."

8. If you charge an ongoing asset-based fee, include the following: "The more assets you have in the advisory account, including cash, the more you will pay us. We therefore have an incentive to increase the assets in your account in order to increase our fees. You pay our fee [insert frequency of fee (e.g., quarterly)] even if you do not buy or sell." Replace the brackets with the frequency of your fee.

9. If you provide advice to *retail investors* about investing in a *wrap fee program*, also include the following: "Paying for a wrap fee program could cost more than separately paying for advice and for transactions if there are infrequent trades in your account."

10. If you are a *dual registrant* that charges an ongoing asset-based fee, include the following: "An asset-based fee may cost more than a transaction-based fee, but you may prefer an asset-based fee if you want continuing advice or want someone to make investment decisions for you." If you provide advice to *retail investors* about investing in a *wrap fee program*, also include the following: "You may prefer a *wrap fee program* if you prefer the certainty of a [insert frequency of the wrap fee (e.g., quarterly)] fee regardless of the number of transactions you have." Replace the brackets with the frequency of the wrap fee.

Item 5: Comparisons to be provided by *standalone investment advisers and standalone broker-dealers*

A. If you are a *standalone investment adviser*, include the heading "Compare with Typical Brokerage Accounts," and include the following under the heading (emphasis required): "You could also open a brokerage account with a ***broker-dealer***, where you will pay a ***transaction-based fee,*** generally referred to as a commission, when the broker-dealer buys or sells an investment for you." Include "Features of a typical brokerage account include:" and then include the following statements, each set off by a bullet point (except as specified below), in the following order:

1. "With a broker-dealer, you may select investments or the broker-dealer may recommend investments for your account, but the ultimate decision for your investment strategy and the purchase and sale of investments will be yours."

2. "A broker-dealer must act in your best interest and not place its interests ahead of yours when the broker-dealer recommends an investment or an investment strategy involving securities. When a broker-dealer provides any service to you, the broker-dealer must treat you fairly and comply with a number of specific obligations. Unless you and the broker-dealer agree otherwise, the broker-dealer is not required to monitor your portfolio or investments on an ongoing basis."

3. "If you were to pay a transaction-based fee in a brokerage account, the more trades in your account, the more fees the broker-dealer charges you. So it has an incentive to encourage you to trade often."

4. Include "You can receive advice in either type of account, but you may prefer paying:" and then present the following information in this sub-item in a tabular format, comparing a transaction-based fee and an asset-based fee side-by-side. In one column, include the following (emphasis required): "***a transaction-based fee*** from a cost perspective, if you do not trade often or if you plan to buy and hold investments for longer periods of time." In the other column, include the following (emphasis required): "***an asset-based fee*** if you want continuing advice or want someone to make investment decisions for you, even though it may cost more than a transaction-based fee."

B. If you are a standalone *broker-dealer*, include the heading "Compare with Typical Advisory Accounts," and include the following under the heading (emphasis required): "You could also open an advisory account with an ***investment adviser***, where you will pay an ongoing ***asset-based fee*** that is based on the value of the cash and investments in your advisory account." Include "Features of a typical advisory account include:" and then include the following statements, each set off by a bullet point (except as specified below), in the following order (emphasis required):

1. "Advisers provide advice on a regular basis. They discuss your investment goals, design with you a strategy to achieve your investment goals, and regularly monitor your account."

2. "You can choose an account that allows the adviser to buy and sell investments in your account without asking you in advance (a "***discretionary account***") or the adviser may give you advice and you decide what investments to buy and sell (a "***non-discretionary account***")."

3. "Advisers are held to a fiduciary standard that covers the entire investment advisory relationship. For example, advisers are required to monitor your portfolio, investment strategy and investments on an ongoing basis."

4. "If you were to pay an asset-based fee in an advisory account, you would pay the fee periodically, even if you do not buy or sell. You may also choose to work with an investment adviser who provides investment advice for an hourly fee, or provides a financial plan for a one-time fee."

5. "For an adviser that charges an asset-based fee, the more assets you have in an advisory account, including cash, the more you will pay the adviser. So the adviser has an incentive to increase the assets in your account in order to increase its fees."

6. Include "You can receive advice in either type of account, but you may prefer paying:" and then present the following information in this sub-item in a tabular format, comparing a transaction-based fee and an asset-based fee side-by-side. In one column, include the following (emphasis required): "***an asset-based fee*** if you want continuing advice or want someone to make investment decisions for you, even though it may cost more than a transaction-based fee." In the other column, include the following (emphasis required): "***a transaction-based fee*** from a cost perspective if you do not trade often or if you plan to buy and hold investments for longer periods of time."

Item 6. Conflicts of Interest

A. Include the heading, "Conflicts of Interest." *Standalone broker-dealers* must include the following after the heading: "We benefit from our recommendations to you." *Standalone investment advisers* must include the following after the heading: "We benefit from the advisory services we provide to you." *Dual registrants* must include the following after the heading: "We benefit from the services we provide to you."

B. Briefly describe the following conflicts of interest, as they are applicable to you. If all or a portion of a conflict is inapplicable to your business, omit that conflict or portion thereof. If you are a *dual registrant* and a conflict only applies to your

brokerage accounts or to your investment advisory accounts, only include that conflict in the applicable column.

1. State that you have a financial incentive to offer or recommend the *retail investor* to invest in certain investments because (a) they are issued, sponsored or managed by you or your affiliates, (b) third parties compensate you when you recommend or sell the investments, or (c) both. Provide examples of such investments. State that your financial professionals receive additional compensation if the *retail investor* buys these investments.

2. State that you have an incentive to offer or recommend the *retail investor* to invest in certain investments because the manager or sponsor of those investments or another third party (such as an intermediary) shares with you revenue it earns on those investments. Provide examples of such investments.

3. State that you can buy investments from a *retail investor*, and sell investments to a *retail investor*, from your own accounts (called "acting as principal"). State that you can earn a profit on these trades, and that you have an incentive to encourage the *retail investor* to trade with you. If this activity is part of your investment advisory business, state that the *retail investor's* specific approval on each such transaction is required.

Item 7. Additional Information.

A. Include the heading, "Additional Information" and include the following after the heading: "We encourage you to seek out additional information."

B. Include the following: "We have legal and disciplinary events" if you or one of your financial professionals currently disclose, or are required to disclose, the following information:

1. Disciplinary information in your Form ADV (Item 11 of Part 1A or Item 9 of Part 2A).

2. Legal or disciplinary events in your Form BD (Items 11 A-K) (except to the extent such information is not released to BrokerCheck, pursuant to FINRA Rule 8312).

3. Disclosures for any of your financial professionals in Items 14 A-M on Form U4 (Uniform Application for Securities Industry Registration or Transfer), or in Items 7(a) and 7(c)-(f) of Form U5 (Uniform Termination Notice for Securities Industry Registration) or on Form U6 (Uniform Disciplinary Action Reporting Form) (except to the extent such information is not released to BrokerCheck, pursuant to FINRA Rule 8312).

C. Regardless of your response to Item 7.B, you must state the following: "Visit Investor.gov for a free and simple search tool to research our firm and our financial professionals."

D. Include the following: "To report a problem to the SEC, visit Investor.gov or call the SEC's toll-free investor assistance line at (800) 732-0330. [To report a problem to FINRA, [ ].] If you have a problem with your investments, investment account or a financial professional, contact us in writing at [insert your primary business address]." If you are a broker-dealer or *dual registrant*, include the bracketed language. It is your responsibility to review the current telephone numbers for the SEC and FINRA no less often than annually and update as necessary.

E. State where the *retail investor* can find additional information about your brokerage and investment advisory services.

1. If you are a broker-dealer, state that for additional information about your brokers and services, visit BrokerCheck, your website, and the *retail investor's* account agreement. Include a link to the portion of your website that provides up-to-date information for *retail investors* and the following link to BrokerCheck: Brokercheck.Finra.org. If you do not have a public firm website, then you must include a toll-free telephone number where *retail investors* can request up-to-date information.

2. If you are an investment adviser, state that for additional information on your investment advisory services, see your Form ADV brochure on IAPD on Investor.gov and any brochure supplement a financial professional provides. If you maintain your current Form ADV brochure on your public website, then you must state the website address. If you do not have a public firm website or if you do not maintain your current Form ADV brochure on your public website, then you must include the following link: adviserinfo.sec.gov. If you do not have a public firm website, then you also must include a toll-free telephone number where *retail investors* can request up-to-date information.

Item 8. Key Questions to Ask.

Under the heading "Key Questions to Ask," include the key questions below and the following: "Ask our financial professionals these key questions about our investment services and accounts."

Use formatting to make the questions more noticeable and prominent (for example, by using larger font, a text box around the heading or questions, different font, or lines to offset the questions from the other sections). You may modify or omit portions of any questions that you determine are inapplicable to your business. If you are a *standalone broker-dealer* or *standalone investment adviser*, you should modify the questions below to reflect the type of account you offer to *retail investors* (*e.g.*, advisory or brokerage account).

Advisers that provide automated advice or broker-dealers that provide services only online without a particular individual with whom a *retail investor* can discuss these questions must include a section or page on their website that answers each of the below questions and should provide a hyperlink in the *relationship summary* to that section or page. If you provide automated advice but make a financial professional available to discuss the existing account with a *retail investor*, you may wish to consider making the financial professional available to discuss these questions with the *retail investor*.

1. Given my financial situation, why should I choose an advisory account? Why should I choose a brokerage account?

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

3. What additional costs should I expect in connection with my account?

4. Tell me how you and your firm make money in connection with my account. Do you or your firm receive any payments from anyone besides me in connection with my investments?

5. What are the most common conflicts of interest in your advisory and brokerage accounts? Explain how you will address those conflicts when providing services to my account.

6. How will you choose investments to recommend for my account?

7. How often will you monitor my account's performance and offer investment advice?

8. Do you or your firm have a disciplinary history? For what type of conduct?

9. What is your relevant experience, including your licenses, education and other qualifications? Please explain what the abbreviations in your licenses are and what they mean.

10. Who is the primary contact person for my account, and is he or she a representative of an investment adviser or a broker-dealer? What can you tell me about his or her legal obligations to me? If I have concerns about how this person is treating me, who can I talk to?

In addition to the abovementioned questions, you may also include any other frequently asked questions you receive following these questions. You may not, however, exceed fourteen questions in total.

APPENDIX C

Hypothetical Relationship Summary for a Dually Registered Investment Adviser and Broker-Dealer
Prepared By SEC Staff – For Illustrative Purposes Only

Which Type of Account is Right for You — Brokerage, Investment Advisory or Both?

There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you.

Depending on your needs and investment objectives, we can provide you with services in a brokerage account, investment advisory account, or both at the same time. This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page 4.

Broker-Dealer Services **Brokerage Accounts**	***Investment Adviser Services*** **Advisory Accounts**
Types of Relationships and Services. *Our accounts and services fall into two categories.*	
• If you open a brokerage account, you will pay us a ***transaction-based fee***, generally referred to as a commission, every time you buy or sell an investment. • You may select investments or we may recommend investments for your account, but the ultimate investment decision for your investment strategy and the purchase or sale of investments will be yours. • We can offer you additional services to assist you in developing and executing your investment strategy and monitoring the performance of your account but you might pay more. We will deliver account statements to you each quarter in paper or electronically. • We offer a limited selection of investments. Other firms could offer a wider range of choices, some of which might have lower costs.	• If you open an advisory account, you will pay an on-going ***asset-based fee*** for our services. • We will offer you advice on a regular basis. We will discuss your investment goals design with you a strategy to achieve your investment goals, and regularly monitor your account. We will contact you (by phone or e-mail) at least quarterly to discuss your portfolio. • You can choose an account that allows us to buy and sell investments in your account without asking you in advance (a "***discretionary account***") or we may give you advice and you decide what investments to buy and sell (a "***non-discretionary account***"). • Our investment advice will cover a limited selection of investments. Other firms could provide advice on a wider range of choices, some of which might have lower costs.
Our Obligations to You. *We must abide by certain laws and regulations in our interactions with you.*	
• We must act in your best interest and not place our interests ahead of yours when we recommend an investment or an investment strategy involving securities. When we provide any service to you, we must treat you fairly and comply with a number of specific obligations. Unless we agree otherwise, we are not required to monitor your portfolio or investments on	• We are held to a fiduciary standard that covers our entire investment advisory relationship with you. For example, we are required to monitor your portfolio, investment strategy and investments on an ongoing basis. • Our interests can conflict with your interests. We must eliminate these conflicts or tell you about them in a way you can understand, so

Broker-Dealer Services **Brokerage Accounts**	***Investment Adviser Services*** **Advisory Accounts**
an ongoing basis. • Our interests can conflict with your interests. When we provide recommendations, we must eliminate these conflicts or tell you about them and in some cases reduce them.	that you can decide whether or not to agree to them.
Fees and Costs. *Fees and costs affect the value of your account over time. Please ask your financial professional to give you personalized information on the fees and costs that you will pay.*	
• *Transaction-based fee*s. You will pay us a fee every time you buy or sell an investment. This fee, commonly referred to as a commission, is based on the specific transaction and not the value of your account. With stocks or exchange-traded funds, this fee is usually a separate commission. With other investments, such as bonds, this fee might be part of the price you pay for the investment (called a "***mark-up***" or "***mark down***"). With mutual funds, this fee (typically called a "***load***") reduces the value of your investment. • Some investments (such as mutual funds and variable annuities) impose additional fees that will reduce the value of your investment over time. Also, with certain investments such as variable annuities, you may have to pay fees such as "***surrender charges***" to sell the investment. • Our fees vary and are negotiable. The amount you pay will depend, for example, on how much you buy or sell, what type of investment you buy or sell, and what kind of account you have with us. • We charge you additional fees, such as custodian fees, account maintenance fees, and account inactivity fees. • The more transactions in your account, the	• *Asset-based fees.* You will pay an on-going fee at the end of each quarter based on the value of the cash and investments in your advisory account. The amount paid to our firm and your financial professional generally does not vary based on the type of investments we select on your behalf. The asset-based fee reduces the value of your account and will be deducted from your account. For some advisory accounts, called ***wrap fee programs***, the asset-based fee will include most transaction costs and custody services, and as a result wrap fees are typically higher than non-wrap advisory fees. • Some investments (such as mutual funds and variable annuities) impose additional fees that will reduce the value of your investment over time. Also, with certain investments such as variable annuities, you may have to pay fees such as "***surrender charges***" to sell the investment. • Our fees vary and are negotiable. The amount you pay will depend, for example, on the services you receive and the amount of assets in your account. • For accounts not part of the wrap fee program, you will pay a transaction fee when we buy and sell an investment for you. You will also pay fees to a broker-dealer or bank

Broker-Dealer Services **Brokerage Accounts**	***Investment Adviser Services*** **Advisory Accounts**
more fees we charge you. We therefore have an incentive to encourage you to engage in transactions. • From a cost perspective, you may prefer a transaction-based fee if you do not trade often or if you plan to buy and hold investments for longer periods of time.	that will hold your assets (called "***custody***"). Although transaction fees are usually included in the wrap program fee, sometimes you will pay an additional transaction fee (for investments bought and sold outside the wrap fee program). • The more assets you have in the advisory account, including cash, the more you will pay us. We therefore have an incentive to increase the assets in your account in order to increase our fees. You pay our fee quarterly even if you do not buy or sell. • Paying for a wrap fee program could cost more than separately paying for advice and for transactions if there are infrequent trades in your account. • An asset-based fee may cost more than a transaction-based fee, but you may prefer an asset-based fee if you want continuing advice or want someone to make investment decisions for you. You may prefer a wrap fee program if you prefer the certainty of a quarterly fee regardless of the number of transactions you have.
Conflicts of Interest. *We benefit from the services we provide to you.*	
• We can make extra money by selling you certain investments, such as [__], either because they are managed by someone related to our firm or because they are offered by companies that pay our firm to offer their investments. Your financial professional also receives more money if you buy these investments. • We have an incentive to offer or recommend certain investments, such as [_], because the manager or sponsor of those investments shares with us revenue it earns on those investments.	• We can make extra money by advising you to invest in certain investments, such as [__], because they are managed by someone related to our firm. Your financial professional also receives more money if you buy these investments. • We have an incentive to advise you to invest in certain investments, such as [_], because the manager or sponsor of those investments shares with us revenue it earns on those investments. • We can buy investments from you, and sell investments to you, from our own accounts

Broker-Dealer Services **Brokerage Accounts**	***Investment Adviser Services*** **Advisory Accounts**
• We can buy investments from you, and sell investments to you, from our own accounts (called "***acting as principal***"). We can earn a profit on these trades, so we have an incentive to encourage you to trade with us.	(called "***acting as principal***"), ***but only with your specific approval on each transaction*****.** We can earn a profit on these trades, so we have an incentive to encourage you to trade with us.

Additional Information. *We encourage you to seek out additional information.*

- We have legal and disciplinary events. Visit Investor.gov for a free and simple search tool to research our firm and our financial professionals.
- For additional information about our brokers and services, visit Investor.gov or BrokerCheck (BrokerCheck.Finra.org), our website (SampleFirm.com), and your account agreement. For additional information on advisory services, see our Form ADV brochure on IAPD, on Investor.gov, or on our website (SAMPLEFirm.com/FormADV) and any brochure supplement your financial professional provides.
- To report a problem to the SEC, visit Investor.gov or call the SEC's toll-free investor assistance line at (800) 732-0330. To report a problem to FINRA, [ ]. If you have a problem with your investments, account or financial professional, contact us in writing at [ ].

Key Questions to Ask. *Ask our financial professionals these key questions about our investment services and accounts.*

1. Given my financial situation, why should I choose an advisory account? Why should I choose a brokerage account?
2. Do the math for me. How much would I expect to pay per year for an advisory account? How much for a typical brokerage account? What would make those fees more or less? What services will I receive for those fees?
3. What additional costs should I expect in connection with my account?
4. Tell me how you and your firm make money in connection with my account. Do you or your firm receive any payments from anyone besides me in connection with my investments?
5. What are the most common conflicts of interest in your advisory and brokerage accounts? Explain how you will address those conflicts when providing services to my account.
6. How will you choose investments to recommend for my account?
7. How often will you monitor my account's performance and offer investment advice?
8. Do you or your firm have a disciplinary history? For what type of conduct?
9. What is your relevant experience, including your licenses, education, and other qualifications? Please explain what the abbreviations in your licenses are and what they mean.
10. Who is the primary contact person for my account, and is he or she a representative of an investment adviser or a broker-dealer? What can you tell me about his or her legal obligations to me? If I have concerns about how this person is treating me, who can I talk to?

APPENDIX D

Hypothetical Relationship Summary for a Registered Broker-Dealer
Prepared By SEC Staff – For Illustrative Purposes Only

Is A Brokerage Account Right For You?

There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you.

We are a broker-dealer and provide brokerage accounts and services rather than advisory accounts and services. This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page 4.

Relationships and Services.

- If you open a brokerage account, you will pay us a ***transaction-based fee,*** generally referred to as a commission, every time you buy or sell an investment.
- You may select investments or we may recommend investments for your account, but the ultimate investment decision as to your investment strategy and the purchase or sale of investments will be yours.
- We can offer you additional services to assist you in developing and executing your investment strategy and monitoring the performance of your account but you might pay more. We will deliver account statements to you each quarter in paper or electronically.
- We offer a limited selection of investments. Other firms could offer a wider range of choices, some of which might have lower costs.

Our Obligations to You. *We must abide by certain laws and regulations in our interactions with you.*

- We must act in your best interest and not place our interests ahead of yours when we recommend an investment or an investment strategy involving securities. When we provide any service to you, we must treat you fairly and comply with a number of specific obligations. Unless we agree otherwise, we are not required to monitor your portfolio or investments on an ongoing basis.
- Our interests can conflict with your interests. When we provide recommendations, we must eliminate these conflicts or tell you about them and in some cases reduce them.

Fees and Costs. *Fees and costs affect the value of your account over time. Please ask your financial professional to give you personalized information on the fees and costs that you will pay.*

- The fee you pay is based on the specific transaction and not the value of your account.
- With stocks or exchange-traded funds, this fee is usually a separate commission. With other investments, such as bonds, this fee might be part of the price you pay for the investment (called a "***mark-up***" or "***mark down***"). With mutual funds, this fee (typically called a "***load***") reduces the value of your investment.
- Some investments (such as mutual funds and variable annuities) impose additional fees that will reduce the value of your investment over time. Also, with certain investments such as variable annuities, you may have to pay fees such as "***surrender charges***" to sell the investment.
- Our fees vary and are negotiable. The amount you pay will depend, for example, on how much you buy or sell, what type of investment you buy or sell, and what kind of account you have with us.
- We charge you additional fees, such as custodian fees, account maintenance fees, and account inactivity fees.
- The more transactions in your account, the more fees we charge you. We therefore have an incentive to encourage you to engage in transactions.

Compare with Typical Advisory Accounts.

You could also open an advisory account with an ***investment adviser***, where you will pay an ongoing ***asset-based fee*** that is based on the value of the cash and investments in your advisory account. Features of a typical advisory account include:

- Advisers provide advice on a regular basis. They discuss your investment goals, design with you a strategy to achieve your investment goals, and regularly monitor your account**.**
- You can choose an account that allows the adviser to buy and sell investments in your account without asking you in advance (a "***discretionary account***") or the adviser may give you advice and you decide what investments to buy and sell (a "***non-discretionary account***").

- Advisers are held to a fiduciary standard that covers the entire investment advisory relationship. For example, advisers are required to monitor your portfolio, investment strategy and investments on an ongoing basis.

- If you were to pay an asset-based fee in an advisory account, you would pay the fee periodically even if you do not buy or sell. You may also choose to work with an investment adviser who provides investment advice for an hourly fee, or provides a financial plan for a one-time fee.

- For an adviser that charges an asset-based fee, the more assets you have in an advisory account, including cash, the more you will pay the adviser. So the adviser has an incentive to increase the assets in your account in order to increase its fees.

- You can receive advice in either type of account, but you may prefer paying:

an asset-based fee if you want continuing advice or want someone to make investment decisions for you, even though it may cost more than a transaction-based fee.	***a transaction-based fee*** from a cost perspective, if you do not trade often or if you plan to buy and hold investments for longer periods of time.

Conflicts of Interest. *We benefit from our recommendations to you.*

- We can make extra money by selling you certain investments, such as [__], either because they are managed by someone related to our firm or because they are offered by companies that pay our firm to sell their investments. Your financial professional also receives more money if you buy these investments.

- We have an incentive to offer or recommend certain investments, such as [__], because the manager or sponsor of those investments shares with us revenue it earns on those investments.

- We can buy investments from you, and sell investments to you, from our own accounts (called "***acting as principal***"). We can earn a profit on these trades, so we have an incentive to encourage you to trade with us.

Additional Information. *We encourage you to seek additional information.*

- We have legal and disciplinary events. Visit Investor.gov for a free and simple search tool to research our firm and our financial professionals.

- For additional information about our brokers and services, visit Investor.gov, BrokerCheck (BrokerCheck.Finra.org), our web site (SampleFirm.com), and your account agreement.

- To report a problem to the SEC, visit Investor.gov or call the SEC's toll-free investor assistance line at (800) 732-0330. To report a problem to FINRA, [ ]. If you have a problem with your investments, account or financial professional, contact us in writing at [ ].

Key Questions to Ask. *Ask our financial professionals these key questions about our investment services and accounts.*

1. Given my financial situation, why should I choose a brokerage account?
2. Do the math for me. How much would I pay per year for a typical brokerage account? What would make those fees more or less? What services will I receive for those fees?
3. What additional costs should I expect in connection with my account?
4. Tell me how you and your firm make money in connection with my account. Do you or your firm receive any payments from anyone besides me in connection with my investments?
5. What are the most common conflicts of interest in your brokerage accounts? Explain how you will address those conflicts when providing services to my account.
6. How will you choose investments to recommend for my account?
7. How often will you monitor my account's performance and offer investment advice?
8. Do you or your firm have a disciplinary history? For what type of conduct?
9. What is your relevant experience, including your licenses, education, and other qualifications? Please explain what the abbreviations in your licenses are and what they mean.
10. Who is the primary contact person for my account? What can you tell me about his or her legal obligations to me? If I have concerns about how this person is treating me, who can I talk to?

APPENDIX E

Hypothetical Relationship Summary for a Registered Investment Adviser
Prepared By SEC Staff – For Illustrative Purposes Only

Is An Investment Advisory Account Right For You?

There are different ways you can get help with your investments. You should carefully consider which types of accounts and services are right for you.

We are an investment adviser and provide advisory accounts and services rather than brokerage accounts and services. This document gives you a summary of the types of services we provide and how you pay. Please ask us for more information. There are some suggested questions on page 3.

Relationships and Services.

- If you open an advisory account, you will pay an on-going ***asset-based fee*** at the end of each quarter for our services, based on the value of the cash and investments in your advisory account.

- We will offer you advice on a regular basis. We will discuss your investment goals, design with you a strategy to achieve your investment goals, and regularly monitor your account. We will contact you (by phone or e-mail) at least quarterly to discuss your portfolio.

- You can choose an account that allows us to buy and sell investments in your account without asking you in advance (a "***discretionary account***") or we may give you advice and you decide what investments to buy and sell (a "***non-discretionary account***").

- Our investment advice will cover a limited selection of investments. Other firms could provide advice on a wider range of choices, some of which might have lower costs.

Our Obligations to You. *We must abide by certain laws and regulations in our interactions with you.*

- We are held to a fiduciary standard that covers our entire investment advisory relationship with you. For example, we are required to monitor your portfolio, investment strategy, and investments on an ongoing basis.

- Our interests can conflict with your interests. We must eliminate these conflicts or tell you about them in a way you can understand, so that you can decide whether or not to agree to them.

Fees and Costs. *Fees and costs affect the value of your account over time. Please ask your financial professional to give you personalized information on the fees and costs that you will pay.*

- The amount paid to our firm and your financial professional generally does not vary based on the type of investments we select on your behalf. The asset-based fee reduces the value of your account and will be deducted from your account.

- Some investments (such as mutual funds and variable annuities) impose additional fees that will reduce the value of your investment over time. Also, with certain investments such as variable annuities, you may have to pay fees such as "***surrender charges***" to sell the investment.

- Our fees vary and are negotiable. The amount you pay will depend, for example, on the services you receive and the amount of assets in your account.

- You will pay a transaction fee when we buy and sell an investment for you. You will also pay fees to a broker-dealer or bank that will hold your assets (called "***custody***").

- The more assets you have in the advisory account, including cash, the more you will pay us. We therefore have an incentive to increase the assets in your account in order to increase our fees. You pay our fee quarterly even if you do not buy or sell.

Compare with Typical Brokerage Accounts.

You could also open a brokerage account with a ***broker-dealer***, where you will pay a ***transaction-based fee,*** generally referred to as a commission, when the broker-dealer buys or sells an investment for you. Features of a typical brokerage account include:

- With a broker-dealer, you may select investments or the broker-dealer may recommend investments for your account, but the ultimate decision for your investment strategy and the purchase and sale of investments will be yours.

- A broker-dealer must act in your best interest and not place its interests ahead of yours when the broker-dealer recommends an investment or an investment strategy involving securities. When a broker-dealer provides any service to you, the broker-dealer must treat you fairly and comply with a number of specific obligations. Unless you and the broker-dealer agree otherwise, the broker-dealer is not required to monitor your portfolio or investments on an ongoing basis.

- If you were to pay a transaction-based fee in a brokerage account, the more trades in your account, the more fees the broker-dealer charges you. So it has an incentive to encourage you to trade often.

- You can receive advice in either type of account, but you may prefer paying:

a transaction-based fee from a cost perspective, if you do not trade often or if you plan to buy and hold investments for longer periods of time.	***an asset-based fee*** if you want continuing advice or want someone to make investment decisions for you, even though it may cost more than a transaction-based fee.

Conflicts of Interest. *We benefit from the advisory services we provide to you.*

- We can make extra money by advising you to invest in certain investments, such as [__], because they are managed by someone related to our firm. Your financial professional also receives more money if you buy these investments.

- We have an incentive to advise you to invest in certain investments, such as [_], because the manager or sponsor of those investments shares with us revenue it earns on those investments.

- We can buy investments from you, and sell investments to you, from our own accounts (called "***acting as principal***"), ***but only with your specific approval on each transaction***. We can earn a profit on these trades, so we have an incentive to encourage you to trade with us.

Additional Information. *We encourage you to seek additional information.*

- We have legal and disciplinary events. Visit Investor.gov for a free and simple search tool to research our firm and our financial professionals.

- For additional information on our advisory services, see our Form ADV brochure on IAPD on Investor.gov or on our website (SampleFirm.com/FormADV) and any brochure supplement your financial professional provides.

- To report a problem to the SEC, visit Investor.gov or call the SEC's toll-free investor assistance line at (800) 732-0330. If you have a problem with your investments, account or financial professional, contact us in writing at [ ].

Key Questions to Ask. *Ask our financial professionals these key questions about our investment services and accounts.*

1. Given my financial situation, why should I choose an advisory account?
2. Do the math for me. How much would I pay per year for an advisory account? What would make those fees more or less? What services will I receive for those fees?

3. What additional costs should I expect in connection with my account?
4. Tell me how you and your firm make money in connection with my account. Do you or your firm receive any payments from anyone besides me in connection with my investments?
5. What are the most common conflicts of interest in your advisory accounts? Explain how you will address those conflicts when providing services to my account.
6. How will you choose investments to recommend for my account?
7. How often will you monitor my account's performance and offer investment advice?
8. Do you or your firm have a disciplinary history? For what type of conduct?
9. What is your relevant experience, including your licenses, education, and other qualifications? Please explain what the abbreviations in your licenses are and what they mean.
10. Who is the primary contact person for my account? What can you tell me about his or her legal obligations to me? If I have concerns about how this person is treating me, who can I talk to?

Your Relationship with Your Financial Professional: Feedback on the Relationship Summary

We would like to know what you think about a proposed Relationship Summary that describes your relationship with your investment adviser or your broker-dealer (your firm) and your financial professionals. This document summarizes:

- the services the firm offers and the types of fees and costs associated with those services;
- the firm's obligations to you;
- certain conflicts of interest;
- how to find additional information about the firm and its financial professionals and research disciplinary history for the firm or its financial professionals;
- how to report a problem with your investments, investment account or a financial professional; and
- some questions to ask your financial professional to get more information.

It is important to us at the SEC to understand what you, the investor, think so that we can make it easier for you to choose the type of investment services relationship that is right for you. We prepared sample Relationship Summaries to illustrate what they may look like.

- Sample Relationship Summary for a broker-dealer
- Sample Relationship Summary for an investment adviser
- Sample Relationship Summary for firms that are both an investment adviser and broker-dealer

Please take a few minutes to review one or more of the samples and answer any or all of these questions. Please provide your comments by [insert date 90 days after publication in the Federal Register] – and thank you for your feedback!

If you are interested in background information on the proposed Relationship Summary, or want to provide feedback on additional questions, click here (https://www.sec.gov/rules/proposed/2018/34-83063.pdf).

Questions

1. Overall, do you find the Relationship Summary useful? If not, how would you change it?

2. How useful is each section of the Relationship Summary? Please consider explaining your responses in the comments.

	Very Useful	Useful	Not Useful	Unsure	Comments
a. Types of Relationships and Services	○	○	○	○	
b. Our Obligations to You	○	○	○	○	
c. Fees and Costs	○	○	○	○	
d. Comparisons to different account types[1]	○	○	○	○	
e. Conflicts of Interest	○	○	○	○	
f. Additional Information	○	○	○	○	
g. Key Questions to Ask	○	○	○	○	

[1] Not applicable for firms that are both an investment adviser and broker-dealer.

3. Please answer the following questions. Please consider explaining your responses in the comments.

	Yes	No	Somewhat	Comments
a. Do you find the format of the Relationship Summary easy to follow?	○	○	○	
b. Is the information in the appropriate order?	○	○	○	
c. Is the Relationship Summary easy to read?	○	○	○	
d. Should the Relationship Summary include additional information about different account types?	○	○	○	
e. Would you seek out additional information about a firm's disciplinary history as suggested in the Relationship Summary?	○	○	○	

4. Are there topics in the Relationship Summary that are too technical or that could be improved? If so, what topics and how can they be improved?

5. Is there additional information that we should require in the Relationship Summary, such as more specific information about the firm or additional information about fees? Is that because you do not receive the information now, or because you would also like to see it presented in this summary document, or both? Is there any information that should be made more prominent?

6. Is the Relationship Summary an appropriate length? If not, should it be longer or shorter?

7. Do you find the 'Key Questions to Ask' useful? Would the questions improve the quality of your discussion with your financial professional? If not, why not?

8. Do you have any additional suggestions to improve the Relationship Summary? Is there anything else you would like to tell us?

How to Provide Feedback

You can send us feedback in the following ways (include the file number S7-08-18 in your response):

Mail	Secretary, Securities and Exchange Commission 100 F Street, NE Washington, DC, 20549-1090
Email	rule-comments@sec.gov
SEC Website	https://www.sec.gov/rules/proposed.shtml

We will post your feedback on our website. Your submission will be posted without change; we do not redact or edit personal identifying information from submissions. You should only make submissions that you wish to make available publicly.

Thank you!

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