



March 12, 2012

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

-- Via email --

**Re: Comment Request for Study Regarding Financial Literacy Among Investors  
Release 34-66164; File 4-645**

*Thank you for considering these important issues. I submit these comments from an educator's perspective. An educator with experience in financial services, but without ties to any one firm, may be in the best position to inform your study. I have been teaching investors how to make prudent choices since 1992, but do not sell or recommend financial products or services. Both companies I founded, the Institute for Private Investors in 1991, and the Investor Education Collaborative in 2004, focus on education and financial literacy. Over 2000 investors have participated in various programs over the past 20 years. I am also a guest lecturer for the Wharton Private Wealth Management curriculum, which I co-created in 1999 with The Wharton School at the University of Pennsylvania. Since 1999, 619 private investors from 38 countries and 41 states have attended this five-day on campus program now held annually. Earlier in my career, I spent 20 years on Wall Street, from 1971-1990, marketing to investors on behalf of financial services firms.*

**i. Comment on methods to improve the timing, content and format of disclosures.**

**Timing** - needs to be separated from the marketing interaction where other factors play too influential a role. The best time for an investor to learn is before a marketing pitch is made, not during it. Yale Professor Daylian Cain's research shows the outcomes are worse for the customer in spite of disclosures because the customer 'lets down their guard.'

**Content** – risk, incentives, costs and expected (as well as past) returns are essential. The content is best taught using case studies, simple charts and a quiz format such as cited by others who submitted comments. Even more vital is teaching financial literacy K-12. Investors will make better decisions later on with this stronger foundation.

**Format** – Questions asked by the financial services professional like, "How much risk do you wish to take?" or "How do you feel about volatility?" are viewed as being helpful to the client. That's like asking a 12 year old how fast they want to drive the car when they have never driven and do not even have a license. Experiential education using interactive technology is available but not widely used. Just as pilots learn to fly through simulations, investors should experience the consequences of their decisions in a simulation.

**ii. Comment on information that retail investors need to make informed financial decisions on hiring a financial intermediary or purchasing an investment product or service typically sold to retail investors, including mutual funds.**

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For the same reason why no one reads the instruction manual for their remote control device, investors do not read up on investments. The information is out there, but very few investors have the time – much less the desire – to wander through complex site maps online or read the fine print of a prospectus. The array of choices is simply too overwhelming, and no one knows exactly how to begin, until the salesman suggests a simple solution – 'trust me to help!'

Investor education should be about the investor, not investments. As other comments have noted, a first step should be a self-assessment of what the financial goals are, what the investor personality is. These factors then point to possible investments needed and optimum delivery method (advisor, do-it-yourself, online chat, broker).

This 'before you invest' assessment survey should be available on [www.sec.gov](http://www.sec.gov) and also on all financial services web sites. Filling out the survey could be required for any new 401-k participant, at retirement counseling classes and upon high school/college graduation. Investors could complete the survey at different points in their lives in order to capture changing needs and goals. A feedback matrix would show each investor where he or she falls vis-a-vis others in the same age and economic bracket.

**iii. In addition, the SEC seeks comment on how to make investment expenses and conflicts of interest in investment transactions more transparent to investors.**

Informed new car buyers rely on the 'blue book' when shopping around for a new car. In contrast investors have no idea what the wholesale price is of any investment product, and no reference book exists to guide them on the mark-up. Investor groups have made only modest strides on revealing comparative fees, primarily relying on private online communities to openly discuss how different providers charge for their services. Mutual funds are more transparent, and have done the best job of fee comparison when a chart shows how a given fund's fees compare to the industry average.

Business models of financial services firms are notoriously opaque. Just as in a grocery store, where the customer does not know why one brand is prominently exhibited in the front of the store while another is in the back, conflicts in investment transactions are often hidden. However, conflicts of interest in investments have far graver consequences to an individual than buying an overpriced or over marketed, i.e., subsidized, product in a grocery store.

To understand how conflicts of interest might be subsidizing the transaction, investors need more knowledge. Today investors do not even know what questions to ask, much less know if they will be told the full truth. For instance, is a firm paid by another to distribute its products? How much? Must they disclose that fee if asked outright? A short list of questions with complete but succinct answers could be mandatory and included in marketing material, and not in legalese. The ADV and other disclosures should be more straightforward and user friendly to search for online.  
[Andrew Gluck comments].

Thank you for considering these issues.

Sincerely,

  
Charlotte B. Beyer  
Founder & CEO

# Investor Education: What's Broken and How to Fix It

By Charlotte B. Beyer

”Sophisticated” investors living in Palm Beach and Greenwich, whom one could assume were well educated, did not seem to escape what appears to be the greatest Ponzi scheme of all time. The SEC, FINRA, exclusive funds of funds and famous global private banks also lost face and many billions. As a result, many investors are fearful of being duped, losing money or trusting the wrong advisor!

Complicating this challenge, inside one online community immediately after the Lehman collapse, an investor quipped, “I trust a fellow investor more than the professionals.”<sup>1</sup> But, is peer-to-peer a safer or a more treacherous way to become more educated about investments? Does this new peer-to-peer preference mean that more traditional didactic education will or should be abandoned? To answer these questions, one first must address three additional issues:

- Would a better-educated investor be better at selecting an advisor or choosing a money manager?
- Who should create the curriculum for investor education?
- How should the outcome of this education be measured?
- Should there be a “best practices” for investors – and who should be the author?

This paper argues that the traditional approach to investor education is not sufficient to meet the needs of investors and that radical reform is needed. Perhaps investment advisory firms have been reluctant to admit the shortcomings of today’s investor education because they fear that a more educated investor might choose the “freedom”<sup>2</sup> of being a do-it-yourselfer over having assets managed by any firm. According to a number of studies,<sup>3</sup> however, even these do-it-yourself investors aren’t as successful as they could be. After observing how one group of investors<sup>4</sup> learned far more in experiential settings, the author submits that these investors might be convincing proof that experiential investor education is superior. Signaling good news for the investment advisory industry, the hiring, use and retention of advisors by these same better-educated investors is stable. This group also expressed positive views of how well served they are by the industry overall.<sup>5</sup> While the ultra-wealthy arguably might have easier access to superior advisors, the author believes that overhauling investor education will benefit all investors, not just the wealthiest.

## A short history of investor education

In the beginning were books, books and more books. For the same reason no one reads the instruction manual, few investors wish to curl up with an asset allocation textbook. Traditional investor education has focused more on delivering a “body of knowledge” and not enough on understanding investors’ actual frame of reference. Lectures, texts and other forms of didactic education may establish the groundwork,

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<sup>1</sup> Online communities are active within many investor membership groups such as Family office Exchange and IPI. Comments are excerpted or paraphrased from conversations within the IPI online community on Memberlink®.

<sup>2</sup> In his August 17, 2009 *Wall Street Journal* op-ed Charles Schwab used this term in describing why investors enjoy being do-it-yourself investors

<sup>3</sup> Odean, Terrance, “Are Investors Reluctant to Realize their Losses,” *Journal of Finance*, Vol. LIII, No. 5, October 1998, pp. 1775-1798 – the first of many papers Professor Odean and his co-authors published highlighting mistakes individual investors are prone to make

<sup>4</sup> The group referred to here includes 544 participants in the Wharton five-day Private Wealth Management program as well as several hundred private investor members of IPI observed over the past 19 years

<sup>5</sup> In IPI’s November 2009 survey of ultra-high-net-worth investors, 61% of the respondents felt well served by the industry, and over two-thirds of respondents had employed their primary advisor for more than four years.

but until experiential learning occurs, there will not be full comprehension<sup>6</sup> at the level necessary to make smart decisions. Learning from the written and spoken word can point an investor in the right direction, but that might not lead to deep enough understanding.<sup>7</sup> Especially when faced with sudden portfolio losses, private clients can panic without having ever fully grasped or internalized the “body of knowledge.” Personal hands-on experience can help. The Internet seemed prepared to deliver just that.

Beginning in the 1990’s the industry tried to teach via web sites. Unfortunately, the sites for investors looked more like books with “clicks.” Videos, a more advanced web experience, were more like the traditional lecture, but viewed on a laptop screen. Next came the era of quizzes, which moved closer to experiential education because they analyzed what the investor actually input. Telling the investor and their advisor what the investor might want or need, even if on a superficial level, was a step forward. Artist renderings of cloudy days or sunny days indicated if savings for retirement were adequate using visual imagery, which can be an effective teaching tool.<sup>8</sup>

A wide variety of seminars claimed to teach investors what they needed to know. Topics included how to retire rich, make more tax-free money or set up a tax-advantaged estate plan. In a recent “urgent and confidential” mailing received by the author from a California investment firm, the firm explained why they teach investors: “Why are we sending this expensive kit at our own expense? We’ve found educating investors is good for our business.” The investment seminar is viewed as a “proven business-getting client-closing strategy,” according to many a trade journal. That logic is sound: make investors feel smarter, and they will be grateful to you, will trust you and, most importantly, will give you assets to manage. Unfortunately, in the medical devices industry that same strategy backfired when Medtronic faced a public relations nightmare. The “training” offered was intended to develop customers, according to their own PowerPoint presentation, and trust in the industry dissolved. Embarrassed, Medtronic ceased the program.<sup>9</sup> Financial services are not immune to such public upbraiding, and current calls for a Consumer Protection Agency indicate just how low the level of trust is today.

None of these prior approaches to investor education is without value. Investors, however, need to learn far more than any of these methods can deliver by themselves.

### **On-the-job training comes too late for high-net-worth investors**

The need for a new model of education is supported by commonly acknowledged traits of the typical high-net-worth client. Most individuals, once they have sold a business or inherited wealth, realize they have been catapulted into a new position, namely CEO of My Wealth, Inc., a job for which few have had adequate training or experience. Too often these investors learn one or more of the wrong lessons first:

- “If I’m so rich, I must be smart,” leading to overconfidence
- The one with the most money gets to call the shots, leading to a sense of entitlement
- Money must be constantly watched, controlled 24/7, leading to paranoia, paralysis and inability to trust anyone
- “I should be able to do this by myself; besides it’s cheaper to be a do-it-yourselfer,” leading to a disappointing experience for many.

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<sup>6</sup> John Dewey first described this thesis in his 1938 book, *Experience and Education*.

<sup>7</sup> Simpson, Steven, *The Leader Who Is Hardly Known: Self-less teaching from the Chinese tradition*. Wood ‘N’ Barnes Publishing & Distribution, 2003, page 28.

<sup>8</sup> Tufte, Edward, *The Visual Display of Quantitative Information*, second edition, Graphics Press, 2001.

<sup>9</sup> “At Medtronic a Profit Goal for Training,” by Barry Meier, *The New York Times*, September 10, 2009.

## 2008 – tilt– game over!@#!

The severity of losses in 2008 frightened many investors. Confidence in markets – and market gurus – vanished. The Madoff affair broke just as the S&P 500 lost 38%. What investors might have learned about long-term investing was washed away by a tidal wave of fear, uncertainty and doubt. “I trust a fellow investor more than the professionals” was a more consoling, less isolating assessment to make in 2008-9. But, like any other extreme event we humans experience, reactions can be too extreme as well.

### Peer-to-peer learning can be perilous

Whether in an online investor chat room or face-to-face at an investor forum, the potential perils of peer-to-peer education reveal themselves:

1. **The loudest voice is heard most** – Human nature does not change inside an online community. A referee who insures equal airtime is not likely to be found inside the chat room or the boardroom.
2. **The man with a motive moves the room** – An investor whose pride is tied to a famous hedge fund’s success may convince the rest of his peers that the strategy is still sound despite losses or GP turnover.
3. **PLU syndrome** – Most of us prefer to be around people like us (PLU) and make decisions or voice opinions just like those same PLU. We may not hear any opposing views because we may have surrounded ourselves with PLU who share our views. Very comforting but treacherous.
4. **Hardening of the opinions** – Cass Sunstein first identified the phenomenon of group polarization in his studies of news filtering online.<sup>10</sup> If individuals filter out those news sites that do not agree with their views, if they read only the news sites or blogs that are in concert with their opinions, not surprisingly, their confidence in their own views will increase and opinions harden into absolute certainty. Or, as Peter Bernstein so aptly puts it, “The greatest risks we take are those where we are certain of the outcome.”<sup>11</sup>

### Whose experience is this anyway?

Experiential education is vital to investor education. Why? If an investor is to experience the true lessons of behavioral finance, the teaching must first help students discover their own investor personality. Not every investor is the right client for an advisor. A knowledgeable but nervous investor with a need to be in control is often unhappy in a discretionary account relationship with an investment advisor. An unsophisticated investor with little interest in the markets is often the “patsy” in a high-stakes poker game, taken advantage of by unscrupulous salesmen.

Experiencing the ups and downs of the securities markets is best done without real money. The folly of market timing is most convincing when investors have actually tried to do it – though not with their hard-earned money! Case study formats or investment games give clients a chance to experience different scenarios and make decisions that have consequences – at least in the case study – and thus learn lessons that stick.

Even more importantly for the student, investor education should be independent of outside influences encouraging a particular set of decisions or actions. Investors learn more rapidly when they are not on the lookout for a sales pitch, when they can relax and do the more challenging work of self-discovery. Feeling safe is vital. Safety from sales and avoiding the bias of one particular advisor’s point of view are

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<sup>10</sup> Cited in *The New Yorker*, November 2, 2009, pp. 110-114.

<sup>11</sup> “Viewpoint,” by Peter Bernstein, *CFA Magazine*, March-April 2004.

imperatives. Investors then are gently prodded to assume personal responsibility for their own wealth management. Investors then correctly accept the responsibility for defining what financial goals make sense for them and determining if, and what kind of, advisor they need.<sup>12</sup>

### **Learning by doing**

After the heavy lifting of self-discovery, investors are ready to flex their new “insight” muscles. Excellent experiential learning engages students if they feel safe and free to compare notes. They no longer need to appear smarter than they are, and they can share less-than-positive experiences: how awkward or ill equipped they felt in a sales interaction or client meeting. Inside that safe environment, the more experience an investor has watching presentations and looking at firms’ brochures, the more discerning that consumer will be. By actually role-playing an advisor interview, students learn how to ask more searching questions. By questioning the clichés so often spoken during sales presentations, they learn how to delve into a statement like “Our clients sleep well at night” or “We are client-centric.” By examining four or five different marketing pitch books, they learn how to discover all the fees and uncover the conflicts. By looking at how several firms present their performance track record, seeing whether they were compliant with GIPS<sup>®</sup>,<sup>13</sup> they become alert to the “tricks” of performance records. By becoming more informed consumers, students learn how to distinguish substance from slick marketing. This trait of being more discerning or savvy, sometimes called *metis*,<sup>14</sup> cannot easily be taught in the more traditional classroom.

By practicing in a safer, risk-free learning environment, these consumers become more astute in the real world of selecting or monitoring advisors. They learn how to “trust but verify.”<sup>15</sup>

### **Learning objectives must be measurable**

Such practice makes perfect only if the outcome of experiential learning is worth it. Attitudes and behavior must change, and educators must hold themselves accountable and measure results. Sample learning goals for experiential investor education include:

- Identify your investor personality and how good (or bad!) a client you might be, and whether an advisor or manager is appropriate for you.
- Become more self-aware of what you as an investor really want or need from advisor or manager.
- Examine your criteria for looking at advisors or managers.
- Recognize the impact of your personality on expectations and view of risk.
- Come to a realistic assessment of what risk can be assumed given investment goals, determine how the balance is maintained during difficult market environments or manager underperformance.
- Create a personal crib sheet to identify key aspects, attributes, traits, deliverables you seek, and your own biases in the relationship between your advisor/manager and you.
- Identify common traps in marketing material, including omissions and unsubstantiated claims.

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<sup>12</sup> The exercise employed was a self-assessment using the quadrants of sophistication and control. The quadrants were first introduced in 1992 by the author in “Understanding Private Client Characteristics,” ICFA Continuing Education, October 8-9, 1992.

<sup>13</sup> GIPS<sup>®</sup>, Global Investment Performance Standards, are the trademark of the CFA Institute.

<sup>14</sup> *Metis* was used by David Brooks in *Bobos in Paradise* (Simon & Schuster, 2001) to describe this phenomenon of becoming more discerning by experiencing more, page 131.

<sup>15</sup> By use of roleplay in investor education seminars, participants learn how much more they can ask to see or ask to be verified. As a result, they feel more empowered and more informed, a highly satisfying experience, sometimes even salvaging a previously rocky relationship with an advisor.

- Distinguish between what is being sold and what you are buying.
- Discover how conflicts of interest might impact the advice you receive or the products you are sold.

## Maintaining the balance of power

Once educated in this new way, the individual is likely to be a far better client because he selects more appropriately. Still, unless both advisor and client profit from the relationship, the ultimate outcome is less than optimal. The analogy to the doctor-patient relationship is apt: Who is responsible for outcomes? Most people reply “the doctor” until they reflect a bit more. Just as a doctor cannot cure me if I don’t tell her my symptoms and maintain a healthy lifestyle, the advisor cannot successfully advise the client without the client actively participating in the process. Like the doctor and patient, the advisor and the client should view the partnership as one between equals, who genuinely respect each other’s unique contribution to the partnership. Neither wins if the investor abdicates, and too frequently firms permit their clients to take a passive approach to their own wealth. Stuart Lucas’s book, *Wealth*,<sup>16</sup> is a favorite among investors because he wrote from the first-hand experience of an inheritor. He and his family decided to “own the primary responsibility” – sage advice given by Charley Ellis nearly 20 years ago.<sup>17</sup> Lucas’s description of the journey from abdication to delegation is compelling.

## Ultimate purpose of education – a very different body of knowledge!

One liberal arts college boasts that they teach students how to think, not how to recite facts and figures. Similarly, investor education should teach individuals how to think about their own wealth, not necessarily how to become a day trader or portfolio manager! How to approach wealth management has had no definitive guidelines because, by definition, each investor possesses a unique frame of reference and set of expectations. However, ten Principles of Principal might point toward a “best practices” and capture how the most successful investors have approached the process.<sup>18</sup>

1. **Self awareness is critical**, more vital than any other principle for your ultimate success. You are the expert on your own values, needs and the goals for your wealth. This might take more time than you imagine, and that is the foundation of any successful advisory relationship you might have.
2. **Know your expectations, goals and immediate needs**, at least in broad terms, and test them against reality by your own financial education.
3. **Decide whether or not to hire an advisor** and overall financial planner before any fund or investment manager is hired.
4. **Know the conflicts** in the transactions of wealth management. Any business model will hold a natural conflict with your highest expectations/hopes. Still, all conflicts should be documented and monitored. Conflicts of interest are everywhere!
5. **Define outcomes** and be sure they are understood and accepted, then clearly communicated to your team of advisors and money managers.
6. **Measure outcomes** in simple formats, review at time intervals that permit mid-course adjustments.

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<sup>16</sup> Lucas, Stuart, *Wealth: Grow It, Protect It, Spend It, and Share It*, Wharton School Publishing, 2006.

<sup>17</sup> Ellis, Charles D., *Winning the Loser’s Game*, third edition, McGraw-Hill, 1998, page xvii.

<sup>18</sup> The author observed these successful investors over the past 30 years, with success being defined by the investors themselves, not the author.

7. **Insist on consistent communications**, timely, easy to read, and complete. The goal is “no surprises,” and you need to insist that the reports are of value to you.
8. **Know when to do a “reset.”** Define it within the written policy guidelines and, once triggered, attend to it immediately by revisiting prior decisions, outcomes and/or expectations in the light of new environments or family events.
9. **Successful wealth management is a journey not a destination.** Once you complete the process, you cannot abdicate the responsibility to monitor what you have created, oversee your advisors and document how close you come to outcomes originally set out.
10. **Successful wealth management should free you up!** To be true to your values, do what you love, pursue your passion, have the freedom to discover your own life’s work. If all this feels more like a burden, you have missed something vital in executing these ten principles.

Or, as two investors have so eloquently expressed their experiences with investor education:<sup>19</sup>

*“It is rare that we get to practice our thinking on real life decision-making problems and compare notes with other smart people with very different backgrounds.”*

*“I have to tell you that a lot of what I’ve been exposed to...seems to be percolating up for me in the form of a sense of creating my own wealth management as I need to have it. It’s like I’m waking up, rubbing some sand from my eyes and discovering it for the first time. Or RE-discovering something – a spirit, fascination, which got sort of beaten down. We really have to find our own, unique ways. And I feel like I’m being blessed with friends and companions on the path. It truly is a wonderful journey.”*

Endnote: The author is indebted to many professionals whose writings and interactions have inspired, directed and gently guided her, opening new vistas in investor education for us all. Among them:

Judy Barber, Jean Brunel, Scott Budge, Charles Collier, Charles Ellis, Patricia Frazee, Joline Godfrey, Sharna Goldseker, Lee Hausner, Dr. Fredda Herz-Brown, James E. Hughes, Stuart Lucas, Ellen Perry, Dr. Jeb Schenck, Roy Williams, Thayer Willis.

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<sup>19</sup> These comments come from two individuals in the group described earlier in footnote 4