July 10, 2018

The Honorable Jay Clayton, Chairman
c/o Brent J. Fields, Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090
Rule-comments@sec.gov

File Number S7-07-18

Dear Chairman Clayton:

On behalf of the Valuentum team, thank you for your tireless efforts to make the financial industry a trusted place for millions of Americans to save for retirement. We applaud “Regulation Best Interest,” in spirit, but it is in the very idea of its name that we think clarity in definition will be paramount to its intent, as it is not the name that it is important, but rather the substance behind its definition that matters. That this rule is about investors and their hard-earned savings, and not an extension of broker or advisor influence, be a guiding light to its development and refinement.

As the name will imply to the retail investor, we must ask, in truth, can brokers truly know what is in their client’s best interest without perfect knowledge of the future? The risk of a rule defined as “Regulation Best Interest” is of considerable implications. Without a crystal ball, isn’t such a rule prone to the views of the popular opinion of the day, which may or may not be “correct?” Financial theory continues to live, breathe, and evolve, and such a “Regulation Best Interest” rule implies that finance has a perfect answer to the question of the future. It doesn’t, and rules should enhance the flexibility of a broker (and the advisor) to truly be able to put their client’s best interest first.

The name “Regulation Best Interest” is confusing in an industry that is already a challenging place to navigate for consumers, and we encourage efforts to explain/define to the public the differences and roles of brokers, financial advisors/planners, asset managers and even unregistered financial publishers/journalists/newsletter publishers. Just like estimates suggest “roughly 90% of wealth management clients are not fully aware of what they pay,” many investors may believe a broker or financial advisor/planner is an investment manager, but with many financial advisors outsourcing investment-management functions and pursuing passive, indexing strategies more and more via asset-allocation monitoring, industry functions are vastly changing.

That investment management is now but a small portion of overall financial planning, new rules should reevaluate which advisor revenue models may be in the best interest of clients, too, especially given the spirit of new rules for brokers titled “Regulation Best Interest.” We encourage new rules to incentivize less new-client asset growth at advisors and incentivize more the quality and efficacy of the financial plan for each individual client at advisories. An AUM-driven advisory model, for example, may not be the

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2 Somai, Sameer S., “Five Reasons to Start Your Own Firm and Four Steps to Take to Do It.” https://blogs.cfainstitute.org/investor/2016/01/04/five-reasons-to-start-your-own-firm-and-four-steps-to-take-to-do-it/#___prnt=KaKubITp
one that offers the least conflicts and therefore “best interest” advice, particularly in that such models have unique conflicts that may not otherwise be present in a per-hour, retainer-type arrangement with milestone bonuses as progression toward a plan is achieved, for example. This per-hour advisory model has been successful in advisory practices⁴ and is common with accountants and lawyers. The spirit of new rules, if not the rules themselves, should be applied consistently across both brokers and advisors/fiduciaries. Is a broker, for example, that recommends a product that benefits his firm indirectly any more potentially conflicted than an advisor/fiduciary that may recommend a product that reduces the cyclicalities of their client base⁴ and streamlines business’ research and overhead costs, benefiting the advisory’s profits indirectly, or directly?

We estimate, for example, that over the course of a trailing 20-year period (8/1/97-6/1/17) that a 1% annual financial advisor fee just to oversee an index ETF tracking the S&P 500 (SPY) to have cost the client roughly $66,000 cumulatively over 20 years on a $100,000 initial investment. Might this client have been better served with just a one-time brokerage commission of a few dollars if indexing may be in the client's best interest? Prevailing opinions of the day about active management, active stock selection, and passive management can influence social views of what might be in a client’s best interest based on past data, but as indexing and passive management becomes more prevalent, a focus on the cost of applying what may be in a client’s perceived best interest becomes equally, if not the most important, consideration. It follows that a focus on fee structure and transparency, may be the clearest route to ensuring that client’s best interest always come first, as future performance can never be predicted with precision.

That as many as 90% of wealth management clients may not even know what they are paying speaks loudly of the need for more fee transparency, particularly with respect to financial advisor fees on indexed products, and particularly within wealth management. There may not be a more transparent advisory business model than a per-hour, retainer-type arrangement with milestone bonus as plan goals are steadily achieved. We think new rules should embrace/promote advisory fee transparency and facilitate the disclosure of fees for advisory services nationwide in a searchable/sortable database, so investors can compare/contrast expected returns after advisor fees for similar services, perhaps as simply as they can do today with mutual funds. As Warren Buffett once quipped: “Performance comes, performance goes. Fees never falter.” It may be with this understanding that the concept of “Regulation Best Interest” consider rules focused on what can be controlled: how much investors pay for brokerage and advisory services by increasing fee transparency and mitigating the conflicts surrounding the business models that sell them.

Sincerely,

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