

Mr. Brent J. Fields
Secretary
Securities And Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-07-18: Regulation Best Interest; File No. S7-08-18: Form CRS Relationship Summary; and File No. S7-09-18: Enhanced Investment Adviser Regulation

Dear Mr. Fields:

I am writing to comment on the SEC's recent proposals to enact a new Regulation Best Interest standard of conduct for broker-dealers, the new Form CRS Relationship Summary, and the proposals for Enhanced Investment Adviser Regulation.

The Commission's intended goals of the proposals, to enhance investor protection and industry transparency, while preserving choice for retail investors, is laudable and to be commended.

However, based on my experience as both a former insurance agent and registered representative, a current principal of an independent RIA ([Pinnacle Advisory Group](http://www.pinnacleadvisory.com/)¹), the co-founder and executive of an Advisor Network that serves more than 700 independent RIA firms providing financial advice to retail clients ([XY Planning Network](https://www.xyplanningnetwork.com/)²), and an active speaker, publisher, and researcher on advisory industry trends through the [Nerd's Eye View at Kitces.com](https://www.kitces.com/)³, I have substantial concerns that many of the proposals as written will compound consumer confusion and reduce clarity regarding the choices that retail investors have when engaging with the financial services industry.

In addition, and even more significant, Regulation Best Interest as proposed would appear to violate the existing "broker-dealer exception" under [Section 202\(a\)\(11\)\(C\) of the Investment Advisers Act of 1940](#)⁴ ("the '40 Act"), which provides only a very specific and narrow scope for a limited range of broker-dealer services to avoid being construed as "advice" that would trigger a requirement to register as an investment adviser (and the fiduciary duty that attaches thereof). In essence, the '40 Act affirms that Congress intended for there to be a distinction between the services of investment advisers and the services of brokers... which the proposed Regulation Best Interest (and the supporting proposed Form CRS) fail to properly recognize.

The Separation Of Brokers And Investment Advisers

¹ <http://www.pinnacleadvisory.com/>

² <https://www.xyplanningnetwork.com/>

³ <https://www.kitces.com/>

⁴ <https://www.law.cornell.edu/uscode/text/15/80b-2>

The core framework of the separation between brokers and investment advisers dates back to the origin of the Investment Advisers Act of 1940, which occurred after the Securities Exchange Act of 1934 and specifically created a new class of (registered) investment advisers to whom additional and higher standards of care would apply, and from which only a delineated segment of broker-dealers may be carved out.

Specifically, [the '40 Act declared that an investment adviser included](#)⁵:

"...any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to ...the advisability of investing in, purchasing, or selling securities.... "

In turn, to ensure that consumers still have the choice of engaging with an investment adviser or a broker-dealer, Congress specifically carved out the Section 202(a)(11)(C) exception for broker-dealers, stating that the "investment adviser" term did *not* include:

*"...any broker or dealer whose performance of such services is **solely incidental** to the conduct of his business as a broker or dealer and **who receives no special compensation therefor**..."* (emphasis mine)

Notably, this language implicitly suggests that Congress fully anticipated that there would be broker-dealers whose level of advice *did* arise to the point that it necessitated investment adviser registration, such that broker-dealers giving any level of advice could avoid it *only* if they received no special compensation *and* the advice was no more than solely incidental to the delivery of brokerage services.

The [Merriam-Webster dictionary](#)⁶ defines "incidental" as:

- 1) being likely to ensue as a **chance or minor consequence**; or
- 2) occurring merely **by chance or without intention or calculation**

In this context, "solely incidental" advice would constitute advice that occurs either: a) by chance; b) as a *consequence* of product sales (i.e., that the sale would precede the advice, and not the other way around, such that the advice was a consequence and not an antecedent); or c) *without* intent to give advice.

Accordingly, even [the final Appeals Court ruling in the case of FPA vs SEC \(2007\)](#)⁷ noted that "the text and structure of paragraph of 202(a)(11) make it evident that Congress intended to define 'investment adviser' broadly and create only a precise exemption for broker-dealers" and further that "where the statutory text is clear, an agency may not use general clauses [under 202(a)(11)(F), now 202(a)(11)(H)] to redefine the jurisdictional boundaries set by the statute."

How Regulation Best Interest As Proposed Would Violate The "Solely Incidental" Exception

While the '40 Act requires that those who are in the business of giving advice on investment securities for compensation must register as an investment adviser (unless eligible for one of the specific

⁵ <https://caselaw.findlaw.com/us-dc-circuit/1221705.html>

⁶ <https://www.merriam-webster.com/dictionary/incidental>

⁷ <https://caselaw.findlaw.com/us-dc-circuit/1221705.html>

exceptions), Regulation Best Interest as proposed repeatedly characterizes the broker-dealer model as a “model for advice”, variously calling it a “pay as you go” model for advice ([page 9 of the proposal](#)⁸), suggesting that preserving the broker-dealer model is about “preserving investor choice across products **and advice models**” (emphasis mine, [page 12 of the proposal](#)⁹), and advocating for “continuing existence of the broker-dealer model as an option for retail customers seeking investment advice” ([page 21 of the proposal](#)¹⁰). And the [very announcement of the proposal itself by Commissioner Clayton](#)¹¹ stated: “The specific obligations of investment advisers and broker-dealers would be, however, tailored to the differences in the **types of advice relationships that they [both] offer.**” (emphasis and [clarification] mine)

Explicitly stating that the broker-dealer model is a “model for advice” and that *both* investment advisers *and* broker-dealers offer *advice relationships* directly contravenes the narrow exception for broker-dealers under Section 202(a)(11)(C) of the '40 Act.

While as the SEC itself notes, based on the Opinion of General Counsel as expressed in Advisers Act Release No. 2, “The broker-dealer exclusion shows, on the one hand, that Congress recognized broker-dealers may give a certain amount of advice to their customers in the course of their regular business as broker-dealers and that it would be inappropriate to bring them within the scope of the Advisers Act merely because of this aspect of their business.”

Nonetheless, as noted previously, Congress limited the broker-dealer exception to *only* “solely incidental” advice, where advice can only be incidental if it occurs by chance, as a *consequence* of a product sale, or *without* intent to give advice. Clearly, declaring broker-dealers as a *model* for advice directly violates the plain language of the narrow solely incidental exception, which [FPA vs SEC already noted that the SEC does not have purview to expand](#)¹².

Unfortunately, the situation is complicated by the fact that, [as I and others in the past have noted, the SEC itself has been lax in enforcing the plain language of the solely incidental rule as written](#)¹³, leading to [an acknowledgement by 2008 in the RAND Study](#)¹⁴ that consumers could no longer clearly distinguish the separation between investment advisers and registered representatives of broker-dealers.

In turn, as a part of [its prior 2005 rule proposal “Certain Broker-Dealers Deemed Not To Be Investment Advisers”](#)¹⁵, the SEC suggested that “solely incidental” should be defined as when advisory services rendered are “in connection with and reasonably related to the brokerage services provided”, a definition [the SEC still put forth as recently as 2013](#)¹⁶.

⁸ <https://www.sec.gov/rules/proposed/2018/34-83062.pdf>

⁹ Ibid.

¹⁰ Ibid.

¹¹ <https://www.sec.gov/news/press-release/2018-68>

¹² <https://caselaw.findlaw.com/us-dc-circuit/1221705.html>

¹³ <https://www.kitces.com/blog/is-the-sec-failing-to-enforce-the-solely-incidental-advice-exemption-for-broker-dealers-under-the-investment-advisers-act-of-1940/>

¹⁴ https://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf

¹⁵ <https://www.sec.gov/rules/final/34-51523.pdf>

¹⁶ https://www.sec.gov/about/offices/oia/oia_investman/rplaze-042012.pdf

Yet the reality is that the 2005 Broker-Dealer Exemption rule itself was [vacated by the DC Circuit Court of Appeals in 2007¹⁷](#), and the current Regulation Best Interest proposal appears to once again extend and inappropriately expand the solely incidental exception even further, by recharacterizing the broker-dealer model as one of advice, specifically a “pay as you go” or “transactional” model of advice. Even worse, the Commission makes this change to the scope of the “solely incidental” advice clause without acknowledging it is doing so, or justifying how such a change is legally permissible (especially in light of [the court’s ruling in FPA vs SEC¹⁸](#) (2007) regarding the Commission’s limitation to expand the broker-dealer exemption under [202\(a\)\(11\)\(F\)-now-202\(a\)\(11\)\(H\)¹⁹](#)).

In fact, it is ironic that the SEC suggests that broker-dealers should be exempt for investment adviser registration because of their episodic or transactional advice, yet routinely requires advisors who provide similar episodic or transactional advice on an hourly or standalone project fee-for-service basis to register as (typically state-based) investment advisers, recognizing that such advisors are clearly in the business of providing advice (albeit transactional or episodic) for compensation regarding investment securities. The fact that hourly, project-fee, and other “transactional or episodic advice” advisors are required to register means the SEC has long since recognized that offering transactional or episodic advice still constitutes being “in the business of advice”... which means broker-dealers providing similar advice would *also* be in the business of advice and *cannot* be providing it in a “solely incidental” manner (which is enough to trigger investment adviser registration under Section 202(a)(11)(C), regardless of whether the broker-dealer receives special compensation as well).

In turn, once the SEC properly recognizes that broker-dealers providing even just transactional or episodic advice must register as investment advisers and conduct those advice activities under the scope of their investment adviser registration (and not as a registered representative of the broker-dealer), the entire framework of Regulation Best Interest becomes largely moot, applying only to a scope of advice services that Congress proscribes broker-dealers from providing in the first place.

In this context, I would actually suggest that the entire nature of a new and different standard of care for broker-dealers is *unnecessary*. The suitability standard was designed to reflect a reasonable standard of care in a *sales* relationship, and once proscribed advice activities are properly conducted under the aegis of an investment adviser registration, the only remaining sales activities *can* be effectively regulated by the existing suitability standard. In other words, the solution to consumer confusion is not to lift the standard for brokerage sales to a best-interests standard because it also entails a substantial amount of advice; instead, [the better solution is to simply assert and maintain the bright line that Congress already created to separate sales from advice, and allow the existing fiduciary and suitability standards to clearly apply to those activities²⁰](#).

Furthermore, the Commission’s proposed change to expand the permissible scope of advice delivered under the broker-dealer model risks adversely affecting competition for the delivery of financial advice in the marketplace. Congress explicitly provided for a narrow, limited-scope exemption for broker-dealers to be subject to an alternative (lower) standard, while lifting the standard for actual (non-

¹⁷ <https://caselaw.findlaw.com/us-dc-circuit/1221705.html>

¹⁸ *Ibid.*

¹⁹ <https://www.law.cornell.edu/uscode/text/15/80b-2>

²⁰ <https://www.kitces.com/blog/why-i-do-not-believe-the-sec-should-create-a-uniform-fiduciary-standard-for-all-brokers-and-investment-advisers/>

incidental) advice, to provide a clear and distinct choice to consumers. The Commission's proposal under Regulation Best Interest would narrow and blur that distinction, allowing brokers to more directly compete with investment advisers in the marketplace for advice (beyond the narrow scope defined by Congress), without fully subjecting the broker's advice to the advice standards set forth by Congress.

As [the Committee Reports to the Investment Advisers Act of 1940 itself noted](#)²¹, the essential purpose of the act was "to protect the public from the frauds and misrepresentations of unscrupulous tipsters and touts and to safeguard the honest investment adviser against the stigma of the activities of these individuals by making fraudulent practices by investment advisers unlawful." Simply put, the entire purpose of the '40 Act was to clearly distinguish and separate the recommendations of brokers from the advice of investment advisers, specifically to safeguard the competitive positioning of the investment adviser's advice relative to the broker's "tips" and recommendations.

Accordingly, even the creation of ERISA maintained a clear distinction between the delivery of (fiduciary) investment advice and the sales of products under the broker-dealer model, such that [the Fifth Circuit Court of Appeals struck down the Department of Labor's fiduciary rule](#)²² specifically on the basis that it "improperly dispense[d] with this distinction". Yet the Commission does not appear to acknowledge the relevance of or give any consideration to this legal precedent: that in both ERISA and the '40 Act itself, Congress acted with intent to maintain a clear separation between sales and advice, for which attempts to narrow this intended distinction may not be permitted by the courts (and in the case of the Department of Labor's fiduciary rule, were not for this very reason).

Form CRS To Reduce Retail Investor Confusion Regarding Broker-Dealers Vs Investment Advisers And Standards Of Care

One of the stated goals of proposed Regulation Best Interest and the newly proposed Form CRS is to "address investor confusion about the nature of their relationships with investment professionals through a new short-form disclosure document — a customer or client relationship summary" ([Commissioner Clayton's announcement regarding the proposed rules](#)²³). Yet the irony is that the SEC actually amplifies the level of confusion in its very declaration of the need for Form CRS as a "customer or client" relationship summary.

The [Merriam-Webster dictionary defines "client" as](#)²⁴:

- 1) one that is under the protection of another [dependent]
- 2) a person who engages the professional advice or services of another

By contrast, [a "customer" is defined as](#)²⁵:

- 1) one that purchases a commodity or service

²¹ <https://www.kitces.com/wp-content/uploads/2018/07/HRReportNo76-2639.pdf>

²² <https://www.kitces.com/5th-circuit-court-of-appeals-decision-on-dol-fiduciary/>

²³ <https://www.sec.gov/news/press-release/2018-68>

²⁴ <https://www.merriam-webster.com/dictionary/client>

²⁵ <https://www.merriam-webster.com/dictionary/customer>

Stated more simply, the key distinction is that [clients purchase advice from advisors, while customers purchase products \(commodities\) from businesses that manufacture them or salespeople who sell them](#)²⁶.

In essence, the very *label* of “customer” versus “client” describes a substantively different relationship, and the SEC’s use of either/both terms fundamentally recognizes that there is a difference between an advice relationship (with an investment adviser) and a product sales relationship (with a broker-dealer). Yet unfortunately, the proposed disclosures of Form CRS itself do not, at any point, clarify this relationship. In fact, neither the word “client” nor “customer” (and certainly not the distinction between them) is ever actually mentioned in the sample versions of Form CRS as a clear way to explain the nature of the consumer’s relationship, despite both terms being used liberally in the description of the Form CRS proposal itself!

Instead, the details of Form CRS itself, despite its “relationship summary” title, primarily characterize the nature of the products or services being offered, the compensation to be paid, and the standards of conduct that will apply... and fail to ever actually define the *relationship* itself as one of client (with an advisor) or customer (with a broker).

To the extent the *nature* of the relationship itself is defined and distinguished at all between the broker-dealer and investment adviser versions of Form CRS, it is referred to only obliquely in recognizing that the broker-dealer’s standard of care only applies “[when we recommend an investment or an investment strategy involving securities](#)”²⁷ while an investment adviser’s applies to “[our entire investment advisory relationship with you](#)”²⁸. In other words, the investment adviser’s duty of care extends to an *ongoing* advice relationship, while the broker’s standard of care applies only to episodic moments of advice... which is both a not-clearly-delineated difference in the scope of relationships, in addition to actually being a violation of the solely incidental exemption under the ’40 Act anyway.

Furthermore, the Commission’s [sample language with respect to the services of broker-dealers explicitly states](#)²⁹ with respect to brokerage versus advisory accounts:

*You can **receive advice** in either type of account, but you may prefer paying: (emphasis mine)*

- 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.

Such an assertion in Form CRS explicitly violates the “solely incidental” exemption for broker-dealers by stating that broker-dealers are in the business of providing such advice, which both further obfuscates the nature of the relationship difference between brokers versus investment advisers from the consumer perspective (by implying the only choice is the difference in how to pay for advice, and not the scope, nature, and limitations on the advice), and risks causing substantial competitive harm to

²⁶ <https://www.kitces.com/blog/financial-advisor-client-vs-customer-book-of-business/>

²⁷ <https://www.sec.gov/news/statements/2018/annex-b-2-bd-registrant-mock-up.pdf>

²⁸ <https://www.sec.gov/news/statements/2018/annex-b-3-ia-registrant-mock-up.pdf>

²⁹ <https://www.sec.gov/news/statements/2018/annex-b-2-bd-registrant-mock-up.pdf>

investment advisers (whose advice, as noted earlier from [the contemporaneous Committee Report](#)³⁰, Congress specifically intended to protect and separate from brokers in establishing the '40 Act). Such anti-competitive pressures against investment advisers are especially problematic given [the identical suggested disclosure in the investment adviser sample of Form CRS](#)³¹, which forces investment advisers to suggest brokers provide equivalent advice for which the only differentiating factor is the nature of the compensation in a transaction-based account.

A better approach to the laudable goal of a relationship summary would be to *actually* address the nature of the *relationship* between the consumer and the broker-dealer or investment adviser, by clarifying (in this order):

- 1) **The nature of the relationship:** is the consumer a client or a customer, in a relationship that is either for advice (with an investment adviser) or for products (with a broker);
- 2) **The scope of the relationship:** is the relationship one of ongoing advice (an investment adviser), or episodic/transaction (which may be *either* a broker selling transactional products, or an investment adviser providing episodic advice);
- 3) **The compensation of the relationship:** how is the broker or advisor compensated for the relationship, either in the form of commissions or fees, and the nature of the commissions (what types of products and what percentages) or the fees (hourly, project-based, subscription/retainer, AUM, etc.);
- 4) **The standard of care of the relationship:** the broker's suitability standard for product sales, or the investment adviser's fiduciary standard of care.

This simple four-pronged approach *actually* clarifies the nature of the relationship between the consumer and the investment adviser or broker, with the first prong being by far the most important. While [the RAND study](#)³² clearly showed that consumers do not understand the differences between the suitability and fiduciary standard of care, consumers *do* clearly understand the simple and plain language difference between an advisor and a salesperson. Simply reflecting the nature of the advice versus sales relationship on Form CRS, and attaching the associated standard of care based on how the individual holds out, would go far to rectify consumer confusion about their available choices.

In the meantime, to the extent that the SEC is considering further revisions to Form CRS, I would urge the SEC to allow proper time for consumer testing of the specific language of the form, including a potential 90-day extension to the current comment period, especially with respect to the statements contained in the "Our Obligations To You" section of Form CRS.

Currently, Form CRS stipulates that broker-dealers "must act in your best interest and not place our interests ahead of yours" while investment advisers "are held to a fiduciary standard" which [the SEC itself in its related Fiduciary Interpretative Guidance declares is where the fiduciary investment adviser "must act in the best interest of its client"](#)³³. Simply put, consumer confusion is *not* alleviated by stating

³⁰ <https://www.kitces.com/wp-content/uploads/2018/07/HRReportNo76-2639.pdf>

³¹ <https://www.sec.gov/news/statements/2018/annex-b-3-ia-registrant-mock-up.pdf>

³² https://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf

³³ <https://www.federalregister.gov/documents/2018/05/09/2018-08679/proposed-commission-interpretation-regarding-standard-of-conduct-for-investment-advisers-request-for>

that the difference between broker-dealers and investment advisers is that the former must act in your best interests, while the latter have a fiduciary obligation to act in your best interests (as well).

Why Title Reform Is Essential— Consumer Confusion And Standards Of Care

While [the RAND study](#)³⁴ has shown that consumers do not understand the differences in standards of care between broker-dealers and investment advisers, I believe the fundamental cause of confusion is not the definitions in the standards of care themselves, in the ways that investment advisers and broker-dealers market themselves to the public.

[Bogert's Trusts and Trustees](#)³⁵ states that a fiduciary relationship arises where "special intimacy or... trust and confidence" exists between the parties. In other words, a trusted advice relationship *is* a fiduciary relationship by definition.

And the very nature of marketing and holding out *as* a trusted advisor begins the process of creating this special relationship of trust and confidence. Accordingly, [the Consumer Federation of America recently found that in a review of the websites of 25 leading broker-dealers \(and insurance companies\)](#)³⁶, *all* of them used titles that explicitly or implicitly identify as advisors (or a substantively similar term), and the firms routinely used language such as "help you create a plan tailored to your needs", "[Our] Financial Advisors build long-term relationships with our clients and their families", and "For over 80 years, our advisors have offered straightforward advice, personalized solutions, and industry expertise to individuals, families, and businesses."

In other words, consumer confusion stems not from the difficulty in distinguishing between the standards of care of broker-dealers versus investment advisers, but the fundamental confusion that arises when broker-dealers *hold out as being advisors in the business of providing advice* to the public while still being allowed to rely on an exemption that they are not and do not. Or stated more simply, consumer confusion about the nature of their advice (or non-advice) relationship starts from the moment that the investment adviser or broker-dealer holds out as such. Most consumers simply cannot comprehend how a firm can state that is it offering a trusted advice relationship that by definition would be a fiduciary relationship of trust and confidence... and then not be subject to a fiduciary standard for that fiduciary relationship.

In its proposal to enact title reform, the SEC does take initial steps to reduce consumer confusion, but fundamentally fails to achieve its goal by limiting the scope of title reform to *just* the "financial advisor" title. This approach grants broker-dealers the ability to use synonymous titles to intimate that same fiduciary relationship of trust and confidence with their customers, while not actually treating those customers as advisory clients or being subjected to the associated fiduciary standards.

In fact, not only does the ability to market as a financial advisor *or synonymous term* create investor confusion by allowing broker-dealers to market an advice-based relationship without being subject to an advice-based standard of conduct, but arguably the act of marketing such financial advice services

³⁴ https://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf

³⁵ <https://legalsolutions.thomsonreuters.com/law-products/Treatises/Bogert-Trusts-and-Trustees-rev-2d-and-3d/p/100028541>

³⁶ https://consumerfed.org/wp-content/uploads/2017/01/1-18-17-Advisor-or-Salesperson_Report.pdf

should *also* require that broker-dealer to register all of its activities as a (fiduciary) investment adviser *anyway*, as *marketing* financial advice services fundamentally contradicts the very definition of the word “incidental”.

Simply put, a firm should not be able to market itself as being in the business of advice and using financial advisors or synonymous titles, and then rely on an exemption to avoid being held accountable for that advice under the '40 Act that was only intended to apply to “incidental” advice that is occurring *by chance or without intent*. The marketing *itself* of such firms unequivocally affirms that the advice is *not* incidental and *not* occurring by chance or without intent; marketing is a deliberate statement of intent about the services to be delivered (or that the consumer should anticipate will be delivered). Yet [in its briefs filed against the Department of Labor’s fiduciary rule³⁷](#), both the Financial Services Institute (FSI) and the Securities Industry and Financial Markets Association (SIFMA), in representing the broker-dealer community, insisted that [their brokers should not be held to a standard that they are in a relationship of trust and confidence³⁸](#) with their customers (which in turn would make Regulation Best Interest unnecessary)... [all their consumer marketing notwithstanding³⁹?](#)!

Either the brokerage industry should be believed for their marketing and use of titles as financial advisors (per [the Consumer Federation of America’s study that such firms hold out as being in the business of advice⁴⁰](#)), or should be believed for their statements to the Fifth Circuit Court of Appeals in the Department of Labor’s fiduciary rule that they are *not* in the business of advice and not in an advice relationship of trust and confidence with their customers. But it surely cannot be both, and it remains unclear whether or how the Commission is considering and giving weight to [the statements various broker-dealer firms have made in court regarding the Department of Labor’s fiduciary rule⁴¹](#) (particularly briefs filed in Fifth Circuit by FSI and SIFMA on behalf of the brokerage industry), and whether or to what extent their services delivered are consistent with their own marketing, use of titles, and reliance on the broker-dealer exemption under the '40 Act (as if the firms are not eligible for the exemption, Regulation BI and Title Reform are rendered moot).

Permitting Dual-Hat-Switching Also Belies The Solely Incidental Exemption Under The '40 Act

Recognizing that increasing the standards for broker-dealers is a moot point for those broker-dealers that simply shift the delivery of their advice to an affiliated investment adviser, the SEC (reasonably) carves out the new Regulation Best Interest and Title Reform proposals for dual-registered advisors. After all, if all the advice is happening under the umbrella of a firm’s registered investment adviser entity, ostensibly there’s no longer a need to increase the standards for broker-dealer-based advice in the first place.

Yet as currently constituted, the SEC’s proposed exemptions for dual-registered advisors risk amplifying consumer confusion and increasing harm, by failing once again to clarify the nature of the consumer’s

³⁷ <https://www.kitces.com/wp-content/uploads/2018/03/SIFMA-FSI-IRI-District-Brief.pdf>

³⁸ <https://www.kitces.com/blog/dol-fiduciary-5th-circuit-appeals-court-ruling-financial-product-distribution-sales-advice-trust-confidence/>

³⁹ https://consumerfed.org/wp-content/uploads/2017/01/1-18-17-Advisor-or-Salesperson_Report.pdf

⁴⁰ https://consumerfed.org/wp-content/uploads/2017/01/1-18-17-Advisor-or-Salesperson_Report.pdf

⁴¹ <https://www.kitces.com/wp-content/uploads/2018/03/SIFMA-FSI-IRI-District-Brief.pdf>

relationship with the broker or investment adviser *as it may change over time* – specifically in situations where the servicing individual “switches hats” between broker and investment adviser roles. Especially given that the broker would be exempt from advisor title reform as long as he/she engages in *any* advice relationship with *any* client... which means an “advisor” who provides one hour of advice to one client as an investment adviser then has unfettered access to use the “advisor” title with the next 99 clients even if he/she intends to solely operate as a broker from that point forward!

The Commission raises the concern in its proposal that recognizing this reality means that servicing individuals might have to use multiple names and titles in a relationship with clients, and that such changing titles (either from one customer to the next client, or even within a single customer/client relationship over time) could lead to further investor confusion. Yet the reality is that what stokes the consumer confusion itself *is* the fact that the servicing dual-registered individual serves in multiple different relationship capacities in the first place! In this context, clear titles that connote the current role the broker or adviser is engaging in with the client, *at the time of that particular step of the engagement*, does not *cause* confusion, but is [a simplification to clarify what is otherwise an already-confusing and complex relationship](#)⁴²!

In fact, failing to have a clear title and a Form CRS or similar explanatory requirement to connote the exact moment that an investment adviser “switches hats” to begin acting in his/her role as a broker is arguably a necessarily and vital disclosure to ensure that the broker-dealer’s subsequent execution is not subjected to the investment adviser’s fiduciary obligation in the first place. After all, if it’s not clear when the investment adviser *stops* acting in his/her relationship as an adviser, then any advice and its subsequent implementation would have to be pursuant to that investment adviser’s advice, without being able to rely on the solely incidental exemption. In other words, brokerage execution would be subject to the investment adviser’s fiduciary duty, in a manner that most corporate RIAs are not structured to oversee.

Alternatively, a superior approach would simply be to recognize that once an adviser holds out as such and engages in a client relationship as such, *dual-hat switching would no longer be permitted*, as fundamentally the fiduciary relationship attaches to a relationship of trust and confidence, *and the relationship with the adviser does not end or change simply because his/her hat switches*. Otherwise, the investment adviser is knowingly permitted to engage in a relationship of trust and confidence with a client, and then repudiate that relationship – without clear disclosure – at the exact moment of implementation when it matters most to the end client.

Or stated more simply – to the extent that the delivery of advice triggers registration as an investment adviser and engages the client in an advice relationship, the adviser should be bound to the investment adviser’s advice relationship and standards for as long as that relationship continues with the client. Doing so would simply recognize the reality of the relationship from the client’s perspective – an advice relationship of trust and confidence doesn’t cease to be such a relationship from the client’s perspective just because the adviser dons a broker’s hat.

⁴² <https://www.kitces.com/blog/simple-fiduciary-regulation-for-financial-advisors-with-complex-guidance-standards/>

Enhancing Investment Adviser Registration With Continuing Education And Capital Requirements

While much of the focus on the proposed Regulation Best Interest and Form CRS is on lifting and clarifying the standards that apply to broker-dealers, the Commission has also proposed important enhancements to the standards that apply to investment advisers. I applaud the progress of these standards, but hope that consideration will be given to how they are implemented to ensure the thriving ecosystem of small-to-mid-sized investment advisers are not harmed in the process.

With respect to the Commission's proposal of a Continuing Education requirement for investment advisers, I believe that doing so is an important and necessary step to ensure the ongoing competency of investment adviser representatives. However, from a practical perspective, it's very unclear what the scope and nature of such a continuing education requirement could or would be, in an environment where there is no substantive *upfront* educational requirement for investment advisers in the first place! As while the Commission compares this continuing education requirement to those that apply to other popular advisor designations like the Chartered Financial Analyst or Certified Financial Planner designations, it is important to recognize that both of those programs have *substantive* upfront education requirements in the first place, for which the body of knowledge changes and evolves, and continuing education is important. Given that the scope of what is covered by the Series 65 exam is far more limited, and less subject to ongoing change (given the relative stability of state securities laws), it's not clear what the subject scope of "appropriate" continuing education would be. Nonetheless, a modest educational requirement – e.g., 3-4 hours per year, representing a half day of continuing education – is arguably reasonable and minimally burdensome on IARs, especially if studying *for* other advanced designations, or meeting the continuing education requirements for those other advanced designations, counts towards the new RIA/IAR continuing education requirement.

Regarding the potential requirement for investment advisers to provide account statements, I fully concur with the Commission's belief that providing such statements to consumers are important. However, in practice RIAs that do not have custody of client assets already typically work with major third-party custodians (e.g., Charles Schwab, Fidelity, TD Ameritrade, Pershing Advisor Solutions, etc.) that routinely provide third-party statements to the end client anyway. Requiring investment advisers to (separately) provide such statements to clients would be duplicative in effort without adding additional information to clients. To the extent the Commission wishes to proceed with ensuring that account statements are delivered to clients, RIAs that can affirm their third-party custodian is providing statements directly should be exempted from the requirement to avoid unnecessary duplicative effort with already-established industry practices.

When it comes to the financial responsibility of registered investment advisers, the Commission should also be commended for wanting to ensure that investment advisers providing advice to consumers have the financial capability to "make good" on any mistakes made, and to be able to ensure the orderly wind-down of the investment adviser if necessary. However, it is important to recognize that not all RIAs engage in the same types of advice, and as a result may have more or less complex businesses to wind down, and more or less exposure to even potentially causing client harm that would have to be rectified in the first place. As a result, the Commission would be best-served to proceed in this regard by implementing a risk-based approach to RIA capital requirements that properly considers not only the size of the RIA, but also whether the RIA:

- Manages portfolio assets, or merely advises on third-party held-away accounts or provides other fee-for-service investment advice (e.g., non-portfolio financial planning);
- Takes fees in advance (particularly more than \$500/client more than 6 months in advance), or only bills in arrears;
- Has discretion or not (which can increase the size and magnitude of trade errors);
- Has custody of client assets or not;
- Has Errors & Omissions insurance (i.e., proper E&O coverage could supplant or reduce any other capital requirements);
- Is bonded (where bonding may also otherwise reduce capital requirements).

Reducing Investor Confusion While Preserving Consumer Choice

Ultimately, the Commission's goal of reducing investor confusion while preserving consumer choice is important, and the current confusion in the investor landscape, dating back to the RAND study and even prior, suggests that reform is long overdue.

That being said, I believe the Commission's approach of trying to adjust the standard that applies to advice delivered by broker-dealers, through the implementation of Regulation Best Interest, is not only an ineffective policy approach that may *amplify* consumer confusion by using overlapping terminology to describe substantively different standards of care, but inappropriately broadens Congress' narrow broker-dealer exemption for "solely incidental" advice.

In fact, arguably Congress has *already* provided the most effective tools to reduce consumer confusion by preserving choice – simply by enforcing the bright line that separates (investment) advice from (broker-dealer) product sales, requiring individuals to use clear titles and labels to correctly describe *at all times* the nature and scope of their relationship, simplifying Form CRS to properly reflect whether the consumer's relationship is as the customer of a salesperson or the client of an advisor, recognizing that when an individual holds out to the public *as* an advisor (or with any similar/synonymous title) it constitutes being in the business of advice such that any subsequent advice delivered *cannot* be "solely incidental" to brokerage services, and similarly recognizing that once an advice relationship of trust and confidence is formed, it continues to be an advice relationship for the consumer (such that all subsequent recommendations must be subjected to the investment adviser's fiduciary duty).

Or stated more simply, the Investment Advisers Act of 1940 as written already presents a framework for consumers to have a choice, between brokerage sales and investment advice, and the Commission doesn't need to rewrite those rules (beyond the scope of what it is permitted to do by Congress anyway) to preserve choice and reduce investor confusion. Instead, it merely needs to ensure clarity by requiring advisors and brokers to use clear titles and labels to connote [the nature of their sales versus advice relationship with consumers](#)⁴³, and hold advisors and brokers accountable to the existing standards based on however it is that those advisors and brokers choose to hold out to the consumers they serve

⁴³ <https://www.kitces.com/blog/the-public-deserves-a-choice-but-its-not-fiduciary-vs-suitability/>

in the first place. At that point, consumers will have a clear choice between sales and advice, and broker-dealers and investment advisers will have their own choice about how they wish to serve consumers, and the standards to which they will be subject... exactly how Congress wrote it in the first place.

Thank you in advance to the Commission for your consideration of these important issues!

Regards,

- Michael Kitces

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