Betterment

61 W 23rd St, 4th Floor
New York, NY 10010

August 7, 2018

Via Electronic Filing

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

Re: Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation (SEC Rel. No. IA-4889; File No. S7-09-18);

Regulation Best Interest (SEC Rel. No. 34-83062; File No. S7-07-18); and

Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the use of Certain Names or Titles (SEC Rel. No. 34-83063; File No. S7-08-18)

Dear Mr. Fields:

We are writing on behalf of Betterment LLC, an SEC-registered investment adviser that manages over $14 billion for nearly 400,000 clients, the vast majority of whom are individuals. We applaud the Commission's efforts to improve the quality of advice provided to retail investors and investors' understanding of the options available to them.

The stakes are high. Millions of Americans need to invest, and invest well, in order to fund essential financial goals, including retirement. If the Commission is successful in this rulemaking, more retail investors will receive the right professional guidance for them, which should lead to better outcomes for their lives. This rulemaking has the potential to enhance individual financial security and alleviate the country's broader shortfall in retirement savings.

In this comment letter, we: (1) explain why we believe that this rulemaking is critically important, and (2) offer our views on specific ways that the proposed rules could be strengthened. In particular, we describe our efforts to improve the Commission's new disclosure document, Form CRS, which is intended to provide retail investors with simple, easy-to-understand information about investment firms. We also describe the results of investor testing of Form CRS that we have conducted in recent weeks. That testing indicates that our proposed changes to Form CRS--which are intended to make it clearer, more focused, and more visually appealing--improve its effectiveness. We hope that the Commission will consider our findings, alongside its own investor testing, as it finalizes Form CRS.

In particular, we encourage the Commission to revise Form CRS to distinguish more prominently between firms that have financial incentives to recommend particular investments and firms, like Betterment, that do not. Although the Commission's proposal recognizes the importance of this distinction, our testing shows that the proposed Form CRS does not make it sufficiently clear. In our investor testing, our suggested treatment of this conflict outperformed the approach proposed by the Commission, with more than ten times as many investors indicating that they found this section of the disclosure useful to them. We believe that Form CRS should detail all the ways that firms are making money from the investors they serve and, ideally, just how much money.

Although better disclosures alone cannot address all of the current issues associated with retail investment advice, we are confident that better informed investors will make better choices and drive positive changes in the overall marketplace. With small but critical modifications, Form CRS can be a powerful tool supporting the Commission's mission to protect retail investors.

I. Americans Need Quality Investment Advice

At Betterment, our mission is to "empower people to do what's best for their money, so they live better." We seek to use technology to provide high-quality, low-cost investment advisory services to as many investors as possible. We believe that it is critically important to ensure that retail investors broadly participate in the capital markets. It's our mission, our reason for existing. Accordingly, and because of our investments in technology, we can invest as little as $10 into a globally diversified portfolio of index-tracking ETFs and provide rebalancing, tax loss harvesting, goal-based advice, and much more, all for an advisory fee of just 25 basis points.

As Chairman Clayton recently observed, it is "more important than ever that people save and invest for their own futures."[1] Many Americans face a significant shortfall in their retirement savings, exacerbated by soaring health care costs and longer life expectancies. At the same time, the shift from defined benefit plans to defined contribution plans has placed greater responsibility on individuals to navigate the complexities of the markets themselves.[2] In this environment, access to personalized investment advice is crucial. Indeed, not only can advice help Americans decide how to invest, it can play a critical role in getting them comfortable investing in the first place. As a recent Treasury report observed, "[e]stablishing a pattern of saving and investing during the early period of an individual's career can significantly increase the probability of long-term success in accumulating wealth and building retirement savings."[3] At

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[1] "Chairman Jay Clayton, "The Evolving Market for Retail Investment Services and Forward-Looking Regulation — Adding Clarity and Investor Protection while Ensuring Access and Choice," Address at Temple University (May 2, 2018), *available at* https://www.sec.gov/news/speech/speech-clayton-2018-05-02 ("Temple University Address").
[2] See GAO Report, "The Nation's Retirement System" (Oct. 2017), *available at* https://www.gao.gov/assets/690/687797.pdf.
[3] U.S. Dep't of the Treasury, "A Financial System that Creates Economic Opportunities - Bank Financials, Fintech, and Innovation" (July 2018) at 161, *available at* https://home.treasury.gov/sites/default/files/2018-07/A-Financial-System-that-Creates-Economic-Opportunities---Nonbank-Financi....pdf.

Betterment, we spend considerable time ensuring that we are explaining financial concepts simply, designing (and testing) appealing user experiences, and effectively serving both seasoned and first-time investors.

II. Investors Deserve Better Than the Status Quo

Although access to financial advice is essential, in some cases “bad advice” can be worse than no advice at all. We’ve seen the impact firsthand: many of our clients have been poorly served by other investment firms with high costs and conflicted business models. For example, under current law, broker-dealers are explicitly permitted to favor their own financial interests at the expense of their customers. As Chairman Clayton recently observed:

> [A] broker-dealer is not prohibited from recommending to you a security that makes the broker-dealer more money (e.g., because the broker-dealer is selling out of inventory, or the product is a proprietary one that the broker-dealer manufactures), as compared to another security that better fits your needs, but pays the broker-dealer less, so long as both securities are “suitable.”[4]

And, even though investment advisers are fiduciaries, and thus subject to a higher duty of loyalty than broker-dealers, the business models of some investment advisers have similar conflicts. That is, some advisers recommend investments that result in additional revenue to them, whether in the form of proprietary funds or revenue streams embedded in products. Such financial conflicts inevitably shift these firms’ incentives and, as a result, threaten the quality of the advice they provide. We agree with the recent words of the AARP: “as a general rule, nonconflicted advice, in any form, is superior to conflicted advice.”[5]

At Betterment, we strive at every turn to build a business that aligns our interests with those of our clients. For example, we are entirely financially independent of the investment products that we recommend to our clients: we receive the same asset-based fee regardless of which investments we select on their behalf. As a result, when we identify better or less costly investments, we have every incentive to select them, allowing us to continually drive down individual portfolio costs and generating significant market pressure in favor of lower fee products.[6] Our clients can also trust that, when we recommend a particular investment to them, our professional judgment is not compromised by our financial interests. Unfortunately, this is not the case across much of the industry, where hidden kickbacks and conflicted product advice are widespread. Most investors have no sense of all the different ways that firms are making money from their accounts and would be hard-pressed to find out, even with (and perhaps because of) today’s extensive disclosure documents.

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[4] Temple University Address (emphasis added).
[5] Comment letter of AARP (Sept. 6, 2017) at 7, *available at* https://www.sec.gov/comments/ia-bd-conduct-standards/cll4-2278279-160981.pdf.
[6] As our proposed Form CRS specifically states, the median portfolio cost for a Betterment client is currently just 10 basis points.

While it is undoubtedly challenging to effectively communicate conflicts to investors, that is not the whole story. As Chairman Clayton observed, "some investment professionals may not be entirely straightforward about the existence or scope of their conflicts of interest, or the ways in which they make money from their customer or client's investment activity."[7] Indeed, some firms go to extraordinary lengths to obfuscate the existence and nature of their financial conflicts, as well as the types of services they actually provide. Some bury descriptions of backdoor revenue in dense legalese. Others use slick marketing to foster the impression of a relationship of trust and confidence, only to subsequently disclaim it in the fine print.[8]

As a result, conflicted advice imposes a significant drag on the economic security of millions of American households. While it is difficult to fully pinpoint the financial impact of conflicted advice on retail investors, both in the form of higher fees and lost returns, estimates are in the tens of billions of dollars each year.[9]

This would be bad enough if investors actually understood key differences in firms' conflicts, obligations, and revenue streams. If that were the case, at least investors could consciously decide whether to do business with particular firms, fully aware of the attendant risks. Unfortunately, countless studies have shown that investors' current awareness of these considerations is limited, such that they are poorly equipped to protect themselves.[10] The current disclosure system allows firms to hide their revenue streams and conflicts. It also does not effectively communicate that less conflicted options are available.

Our proposed enhancements to Form CRS, discussed below, attempt to address these critical gaps in investor understanding. Specifically, we are proposing a new section for Form CRS titled "Alignment of Interests" that more clearly indicates whether firms have financial incentives to recommend particular investments. Firms with such conflicts would be referred to as "variable fee" investment advisers or broker-dealers; firms that avoid these conflicts would be referred to as "level fee," a concept borrowed from the Department of Labor's fiduciary rulemaking. We believe that prominently distilling this distinction between firms is one of the most important functions that Form CRS could serve. Firms should also list all of the revenues they receive from investor accounts and provide examples of specific amounts that might be generated by a typical account. For example, firms would need to clearly state how much revenue they typically receive from proprietary funds, from payment for order flow, or from a spread on cash balances.

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[7] Temple University Address.

[8] See Consumer Federation, "Financial Advisor or Investment Salesperson? Brokers and Insurers Want to Have it Both Ways" (Jan. 18, 2017) *available at* https://consumerfed.org/reports/financial-advisor-or-investment-salesperson-brokers-and-insurers-want-to-have-it-both-ways/.

[9] "Regulation Best Interest," SEC Rel. No. 34-83062 (Apr. 18, 2018) at fn. 460, *available* at https://www.sec.gov/rules/proposed/2018/34-83062.pdf.

[10] See 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"); 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), *available at* www.sec.gov/news/studies/2011/913studyfinal.pdf ("913 Study").

Our investor testing, discussed below, shows that our proposed changes to Form CRS improve investors' understanding of product-level conflicts. By incorporating our suggested changes and other insights from investor testing into the final version of the form, the Commission can ensure that it is providing additional clarity on the most important issues to retail investors, not simply adding to the volume of existing disclosures.

III. Retail Investors Would Benefit from Heightened Standards of Care

Although this comment letter largely focuses on Form CRS, the effectiveness of any disclosure is partially dependent on the strength and clarity of the underlying legal regime. Accordingly, we offer a few observations on the balance of the Commission's proposed rules.

We support the Commission's efforts to heighten the standards of care applicable to broker-dealers through Regulation BI. As noted above, the current suitability standard is inconsistent with investors' reasonable expectations and exposes them to abuse. Unless and until a comprehensive, rigorous study equivalent to the RAND Study[11] indicates that the vast majority of Americans understand that broker-dealers are not fiduciaries, and can distinguish them from investment advisers, it is critical to impose a strict and meaningful standard of care.

Yet it is not entirely clear how high a standard Regulation BI will actually set. Our greatest concern is that investors will believe that broker-dealers are subject to a fiduciary duty or some other truly protective standard when that is not the case. It is very difficult to hear the phrase "best interest" and imagine anything other than an utmost duty of loyalty. To the extent that Regulation BI would allow firms to consider their own interests, at any level, in making recommendations to retail investors, the standard must have a new name to avoid fundamental confusion that could undo any benefit of the rule. The Commission should also ensure, through investor testing, that the public is able to understand the contours of any new standard and how it differs from a fiduciary obligation. Absent such evidence, broker-dealers should be required to meet a fiduciary standard unless they clearly and prominently identify themselves as <u>salespeople who are providing sales recommendations and not advice</u>.

Relatedly, we agree with the Commission's proposal to prevent broker-dealers from describing themselves with the terms "advisor" or "adviser." Broker-dealers who use these terms cause significant confusion regarding the nature of the services they provide and the standards of care to which they are subject. But the Commission should go even further and preclude broker-dealers from holding themselves out in a manner that is inconsistent with the nature of their services and obligations, whatever specific words they are using. Absent such restrictions, misleading marketing may well drown out any additional clarity provided by more effective disclosures. The Commission should also ensure that dual registrants clearly and consistently communicate which of their services are advisory in nature.

[11] See n. 10 *supra*.

We appreciate the Commission's additional guidance regarding the contours of investment advisers' fiduciary duties. In particular, we were pleased that the guidance does not in any way detract from the Commission's prior statements about the ability of digital advice to meet the fiduciary standard.[12] The Commission's flexible, principles-based approach has allowed for innovative and investor-friendly services to develop and flourish. We also agree that it is critically important for all firms, regardless of the extent to which they provide digital advice, to ensure that investors have a clear understanding of the actual services they offer. That view also informs our belief in the importance of designing an effective Form CRS.

IV. Form CRS, With Certain Enhancements, Could Meaningfully Improve Investor Understanding

The Commission has, for the most part, identified the key issues that Form CRS should cover, including firms' differing legal obligations, fee structures, and conflicts.

As set out below, we also believe that the form can be improved in several ways:

- The form should more clearly highlight how firms differ with respect to conflicts arising from product-level revenue and should clearly identify all forms of revenue associated with particular accounts.
- The form should be better organized, streamlined, and clarified.
- The form should better implement design principles that have been shown to facilitate visual appeal and comprehension.

We don't just <u>believe</u> that these changes would make Form CRS more effective, we've confirmed it through our own investor testing. That testing indicates that our proposed form, which makes the enhancements listed above, materially improves the form's value to investors.

A. The Commission's Proposal

In support of its proposed Form CRS, the Commission notes that there are important distinctions among firms and among business models that investors do not adequately understand.[13] According to Chairman Clayton:

> Our proposed disclosure rules would require investment professionals to be clear and transparent about the type of professional that they are, the services they provide (and

[12] <u>See</u> Investment Management Guidance Update on Roboadvisers (Feb. 2017), *available at* https://www.sec.gov/investment/im-guidance-2017-02.pdf.

[13] <u>See</u> "Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the use of Certain Names or Titles," SEC Rel. No. 34-83063 (Apr. 18, 2018) at 8, *available* at https://www.sec.gov/rules/proposed/2018/34-83063.pdf ("Form CRS Proposing Release").

> do not provide), the fees they charge, the conflicts of interest they have, and other key information such as any disciplinary history.[14]

We agree with these objectives. Although the information that Form CRS seeks to convey is extremely important, many investors do not currently have a good understanding of it. As a result, they choose providers with limited awareness of alternative options or the key distinctions among firms.[15] There is truth in the maxim that typically "financial products are sold, not bought."

We also agree with many of the fundamental principles that inform the Commission's approach to the design of Form CRS. For example, the Commission seeks to provide concise information regarding certain fundamental characteristics of a firm in a clear and easily digestible format.[16] That is, rather than simply replicating existing--and potentially sprawling--disclosure documents, the Commission has set out to create something new that is more focused, more compelling, and more digestible. The Commission has publicly emphasized its desire to standardize the format of Form CRS and certain aspects of its content to facilitate high-level comparisons by investors. Finally, the Commission has explained its desire to incorporate design principles and to test the effectiveness of its disclosure with real investors.[17]

Although we have different views about certain aspects of the implementation of these principles, which we explain below, we are enthusiastic about the Commission's fundamental goals and approach. We are particularly supportive of the Commission's efforts to shed light on conflicts of interest arising from financial incentives associated with proprietary products and revenue sharing arrangements. We could not agree more strongly with this statement from the Proposing Release:

> Limitations on investments offered could have a significant effect on investor choice and performance of the account over time. In particular, <u>firms that offer proprietary products exclusively preclude investor access to competing products that could offer lower fees or result in better performance over time.</u>[18]

A recent <u>Wall Street Journal</u> article illustrates how proprietary products, and the hidden revenue they generate, can harm investors.[19] Specifically, many investment firms place uninvested cash (e.g., from dividends and other distributions) into sweep accounts that pay investors minuscule amounts of interest, even as the firms reap more than ten times as much revenue from the same accounts.

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[14] Temple University Address.
[15] <u>See</u> 917 Financial Literacy Study.
[16] Form CRS Proposing Release at 9.
[17] <u>See</u> <u>id.</u> at 18-19.
[18] <u>Id.</u> at 40 (emphasis added).
[19] Jason Zweig, "How Your Brokers Can Make 10 Times More on Your Cash Than You Do," <u>Wall Street Journal</u> (Aug. 3, 2018), *available at* https://blogs.wsj.com/moneybeat/2018/08/03/how-your-brokers-can-make-10-times-more-on-your-cash-than-you-do/.

If Form CRS is to meaningfully serve investors, it must quantify the actual impact of conflicted products and practices. That is, the form should provide a dollar measure of either foregone investor returns and/or the revenue generated for the investment firm and its affiliates.[20] A generic statement that proprietary products imply limited options and potential opportunity costs is simply not enough, particularly given the potential for hidden revenues to subsidize what might otherwise seem like an appealing, low-cost service. Using the above article as an example, investors should be explicitly informed that their investment firms are making ten times their own returns on conflicted sweep accounts. Any argument by firms about the difficulty of making such disclosures should only underscore their necessity. If large financial firms can't clearly delineate their revenues, what are the chances for individual investors to understand them?

More broadly, Form CRS should surface differences in firms' revenue streams and financial incentives in a prominent, consistent way. We believe that our proposed version of the form furthers that important objective.

B. Potential Issues with the Proposed Form

We appreciate the Commission's openness to feedback about potential ways to improve Form CRS. In particular, we were happy to see specific invitations for feedback from investment firms and "experts in financial literacy, information design, and marketing."[21] These disciplines are core to our work at Betterment and were central to our own assessment of Form CRS.

In reviewing the Commission's proposal, we looked at the instructions provided by the Commission, as well as its sample "mock ups." We also prepared a hypothetical Form CRS for Betterment's advisory services, based on our own understanding of the proposed instructions.[22] We then identified potential areas for improvement.

First and foremost--as indicated above--we think the form could more effectively educate investors on hidden revenue streams and conflicts arising from financial incentives to recommend particular investment products. When we followed the instructions to prepare a version of the form specific to Betterment, we were left with blank space in the section designed to set out such conflicts. That section states, without more, "**Conflicts of Interest.** *We benefit from the advisory services we provide to you.*"

Conflicts of Interest. *We benefit from the advisory services we provide to you.*

[20] For investment products, it will likely be easier to quantify the revenue generated for the investment firm and its affiliates. To the extent it cannot be precisely quantified, firms should provide an approximation that would be understandable to a reasonable investor. They should also update this information in the event of any material changes.

[21] Dalia Blass, Remarks at the PLI Investment Management Institute 2018 (Apr. 30, 2018), *available at* https://www.sec.gov/news/speech/blass-remarks-pli-investment-management-institute-2018.

[22] See the "SEC Form" in the Appendix to the attached investor research report.

While we appreciate this implicit recognition (however unintended!) that our business model avoids some of the most significant possible conflicts, this presentation could be confusing and misleading. In our view, the better approach would be to allow firms that avoid product-level financial incentives to make a clear, affirmative statement to that effect. Our specific proposal for this is detailed below.

Relatedly, under the Commission's proposed approach, where Form CRS is prepared by a firm that does receive obscure sources of revenue and have product-level conflicts, there would be no way for an investor to know that less conflicted alternatives exist. To the contrary, an investor might simply assume that any listed conflicts are boilerplate and apply to all firms, leading them to ignore this portion of the disclosure altogether. If so, the disclosure could even be harmful.[23] Our own approach would draw a clearer contrast between the characteristics of the disclosing firm and other potential options.

We identified additional ways in which the proposed form might be improved.

- **Clear Takeaways and Focus.** The proposed form does not clearly convey the most important, high-level takeaways for an investor considering a particular firm. It tries to cover too many topics, rather than crisply addressing the most important ones. It should also state clearly, at the outset, why investors are receiving the form and the purpose it serves. Additionally, because investors stand to benefit from comparing the forms prepared by other providers, the form should state plainly that it is required of every firm that serves retail investors.

- **Improved Clarity and Readability.** The form is fairly dense and visually uniform. It is lacking in white space and other design elements that have been shown to facilitate comprehension and retention.[24]

- **Better Organization.** At the moment, there is some redundancy, as well as separation between related concepts (e.g., information related to fees is scattered, key characteristics of broker-dealers are grouped together rather than placed alongside related information about an adviser providing the disclosure).

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[23] See generally Sunita Sah et al., "Conflict of Interest Disclosure as an Expertise Cue: Differential Effects of Automatic and Deliberative Processing," Organizational Behavior and Human Decision Processes (July 2018); Daylian Carin et al., "The Dirt on Coming Clean: Perverse Effects of Disclosing Conflicts of Interest," Journal of Legal Studies (Jan. 2005).

[24] See, e.g., Margaret Hagan, "Designing 21st Century Disclosure Methods for Financial Decision Making" (2016), *available at* https://law.stanford.edu/wp-content/uploads/2016/10/Hagan-Designing-21st-Century-Disclsoures-for-Wise-Financial-Decision-Making-FINAL-2016.pdf; Angela Hung et al., "Effective Disclosures in Financial Decisionmaking" (July 2015), *available at* https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/proposed-regulations/1210-AB32-2/effective-disclosures-in-financial-decision-making.pdf; 917 Financial Literacy Study.

- **Elimination of Confusing and Potentially Misleading Content.** Some of the prescribed language could lead an investor to conclude that a broker-dealer has a higher (or the same) obligations as an investment adviser,[25] that a broker-dealer would always be the most cost-effective option, or that a wrap fee would always be the least cost-effective option. The prescribed content also obscures, rather than clarifies, some of the diversity within the universe of advisory accounts (suggesting, for example, that all advisory services are discretionary). Such generalizations may lead to more confusion than they clear up.

- **Stylistic Changes to Make the Document More Compelling**. The form makes extensive use of prescribed language that is phrased in a way that makes it appear to be boilerplate, rather than specific information about a particular firm (this is exacerbated by the use of the first person rather than the name of the firm). As a result, the form does not clearly convey information about the firm in question or facilitate meaningful comparisons to other options. In some cases, it is not clear whether a description flows from a legal category (e.g., an investment adviser) or is firm-specific. Even the title of the form--"Is an Investment Advisory Account Right For You?"--suggests that it is boilerplate, as opposed to specific information about a particular firm. The boilerplate approach is not particularly compelling and conveys the impression that investors may not have other choices available to them.

- **A Lack of Specificity on Key Subjects.** In some cases, particularly around fees and expenses, the form provides generalizations where specific information and examples would be far more useful and compelling to individual investors. Although costs are one of the most important subjects for an investor to comprehend, they are often not clearly disclosed and, as a result, are poorly understood. The form misses a valuable opportunity to close this gap.

- **Conflicts are Not Described Clearly.** Some of the prescribed language related to conflicts and incentives could be improved, such as the description of an asset-based fee as creating "an incentive to increase the assets in [an investor's] account to increase [the firm's] fees." There is also not enough description of how conflicts could impact advice (e.g., identifying the possibilities of churning or reverse churning). Without such explanation, we fear that investors will not pay much attention to conflicts (which are already a difficult subject to communicate in a clear and compelling way).

[25] This is attributable in part to the some ambiguity in the actual standard of care that would govern broker-dealers, as discussed above.

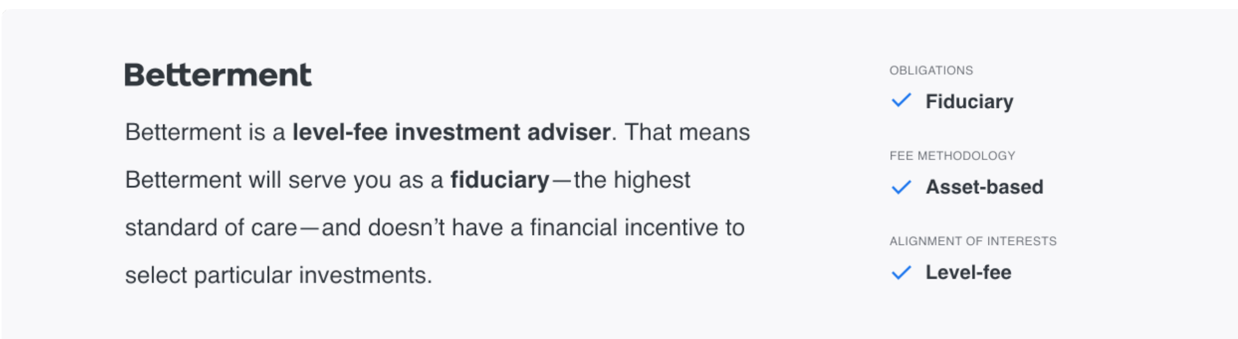
C. Betterment's Efforts to Enhance Form CRS

A few months ago, Betterment set out to redesign Form CRS with the goal of testing, with actual investors, whether we could improve its appeal, understandability, and effectiveness. As we sought to improve the Commission's version, we drew upon our extensive experience building user-friendly software and crafting clear client communications.[26]

First, we identified the most important distinctions that the disclosure should communicate. In doing so, we focused on the Commission's explanations of the form's intended purpose and goal of facilitating meaningful comparisons across firms. We identified three fundamental, binary distinctions among firms:

1. **Obligations:** (1) Fiduciary (investment adviser), or (2) "Best Interests" (broker-dealer)
2. **Fee Methodology:** (1) Asset-based, or (2) Transaction-based
3. **Alignment of Interests:** (1) Level-fee, or (2) Variable-fee

To anchor the document on this framework, we designed a summary module that succinctly conveys these key distinctions and serves as a roadmap for the rest of the document. In our view, this should facilitate both comparisons and comprehension. It is effectively an application of the concept of layered disclosure referenced by the Commission in its proposal.[27]



We then reorganized the structure and content of Form CRS around these three key distinctions, stripping out certain information less critical to the core objectives articulated by the Commission (or that could effectively be addressed in other disclosure documents). As a result, even though our proposed form retained the "Additional Information" and "Key Questions to Ask" sections in roughly their original, proposed state, our form had 30% fewer words. We also attempted, where possible, to more clearly define key terms and avoid unnecessarily complicated language.

Within each section of the document, we provided an explanation of a particular classification and its implications (e.g., the particular conflicts or incentives created by an asset-based fee)

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[26] See the "Betterment Form" in the Appendix to the attached investor research report.
[27] Form CRS Proposing Release at 102.

and described how the alternative (a transaction-based fee) would be different.[28] Co-locating alternative options in this way provides a unified picture of individual concepts and allowed us to avoid redundancy. For example, we provided information about broker-dealers directly below our identification of Betterment's status as an investment adviser and explanation of that classification.

Alternative **Broker-dealer**	• Typically makes recommendations about specific securities transactions, rather than ongoing advice and investment monitoring. • Held to a lower standard than fiduciaries; however, recommendations must be consistent with your best interests. • Not required to avoid conflicts of interest, but must disclose any material conflicts and, in some cases, mitigate them.

Our first two distinctions ("Obligations" and "Fee Methodology") are captured, in large part, by the Commission's proposed form, although we attempted to present them more clearly and crisply. For example, our proposed form contrasts directly the proposed "best interests" and fiduciary standards.

We also anchored our description of fee methodology to specific information about the fees that we actually charge and provided a numerical example of how the fees might impact a hypothetical account.

[28] It is our understanding that some commenters have objected to the idea that a disclosing firm should be forced to provide information about other types of firms and have suggested that the Commission itself should fill this educational need outside the context of Form CRS. While that argument has some force, our hypothesis is that crisply articulating high-level distinctions within Form CRS is a more effective way to convey information and ensure that investors actually receive it.

Fee Methodology

Asset-based

As compensation for investment advice and the cost of making trades in your account, you'll pay Betterment an **annual fee of 0.25%** of the value of your assets with it.

$ For an account with a balance of $50,000, this fee would amount to $125 a year.

HOW THIS AFFECTS YOUR RELATIONSHIP

- Betterment has an incentive to increase or maintain the assets in your account to increase its own compensation.
- Because Betterment doesn't separately charge you for trades, it has an incentive to minimize trade frequency to limit its own trading costs.

Our third high-level distinction, concerning "Alignment of Interests," represents more of a departure from the Commission's proposal and is an effort to rethink the "Conflicts of Interests" section (specific to financial incentives to recommend particular investments) in the Commission's proposal. Essentially, we determined that investors should be more clearly informed, at a high-level, whether firms have incentives to choose particular investments, in light of the potential for tainted advice and its significant, demonstrated costs.[29]

In our view, firms, like Betterment, who do not have that fundamental conflict should state that affirmatively; firms with some version of this conflict should describe it specifically. In either case, the alternative possibility should be set out, consistent with our overall approach of defining a key distinction, explaining where a firm falls, setting out the alternative, and outlining the implications of each possibility.

To identify firms that don't have product-level conflicts, we borrowed the term "level fee" from the Department of Labor's fiduciary rule, as it is a concept with which firms already have some familiarity.[30] The Department of Labor identified level-fee firms as less conflicted and therefore subjected them to a less onerous set of requirements. In response, some firms eliminated commissions, whereas other firms created new products like "clean shares" that reduced product-level conflicts. Under our proposal, a broker-dealer could also be "level-fee" if it does

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[29] See Form CRS Proposing Release at 101.
[30] See Regulation BI Proposing Release at 47 (setting out the Commission's desire to draw from principles that apply to investment advice under other regulatory regimes, including the DOL Fiduciary Rule).

not accept variable commissions, recommend proprietary products, or receive product-level revenue streams.

Alignment of Interests

Level-fee

Independent of Betterment's annual fee, you will pay "fund fees" to the companies that manage the funds in which you invest. Betterment does not benefit from these fees in any way.

As in other sections, we also explained the implications of the applicable classification.

HOW THIS AFFECTS YOUR RELATIONSHIP

Betterment has no financial incentive to choose particular funds for you and is fully aligned with your interests.

It is our belief that this distinction would provide a useful entry point for investors struggling to understand the actual implications of product-level conflicts. As the Commission has recognized, retail investors "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."[31] We believe that Form CRS should address this need by providing detailed and specific information about all of the ways that firms actually make money.

Our approach to the disclosure of product-level incentives could also inform and focus the Commission's own oversight priorities, such as risk-based examinations. That is because, all else being equal, firms that do not have this category of conflict are less likely to harm investors through conflicted product advice. Investor choice, another of the Commission's goals, wouldn't be negatively impacted, but investor understanding would be meaningfully enhanced.

We coupled our "Alignment of Interests" section with specific information about the median fund fees that Betterment clients pay (information that, like fees paid to an adviser, is not specifically included in the Commission's proposed form).

The **median annual fund fees** for a portfolio at Betterment total **0.10%**.

$ For an account with a balance of $50,000, these fees would amount to $50 a year.

[31] Form CRS Proposing Release at 104.

We did so for several reasons. First, it makes sense to pair information about product-level expenses with a description of product-based incentives. Second, it is important that investors have some sense of the "all-in" costs that they might expect to pay at a given firm (particularly given the ability of firms with complicated revenue streams to shift costs from "advice" to products).

We believe this type of information is necessary for any meaningful comparison of all-in expenses across firms. Indeed, although it is not included in our current proposal, we would be supportive of an approach that linked out to a calculator that investors could use to generate more individualized calculations of expenses. Some degree of interactivity might also facilitate the disclosure of meaningful fee information for firms who have more byzantine fee structures or a wider dispersion in portfolio costs.

Throughout the drafting of our proposed form, we sought to address the specific issues we initially identified with the Commission's proposal (e.g., by adding an explanation of the purpose of the document and being explicit that other firms are required to prepare it).[32] We also applied a few additional design principles and insights that have proven empirical support:[33]

- We used headings and subheadings throughout the document and followed a clear internal structure and organization.
- We used shading, color, and variation in design to create visual interest and consistent cues regarding the overall organization of the document and the types/importance of information being communicated (e.g., consistent shading for alternatives to Betterment).
- We increased white space (including by limiting the length of lines of text) and used bullets and larger font sizes to make the document less intimidating and easier to read.
- We bolded key terms and altered the size and style of text to convey the relative significance/type of information being conveyed.

We realize that the Commission recognized the value of some of these approaches and considered being more prescriptive about their use, but opted not to mandate them, in part given concerns that not all firms would be capable of applying them.[34] As such, our critique of the Commission's proposed form is not intended to minimize the care that went into its development or the constraints that influenced its approach.

We are of the view, however, that a compelling, clear, and consistent visual presentation is critical to the effectiveness of Form CRS. If these objectives cannot reasonably be met by firms

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[32] Given timing constraints, including the time it takes to conduct investor testing, we did not write out instructions or prepare sample documents for broker-dealers or dual registrants, although hopefully the construction and content of our document indicates what such forms would be like were our approach to be adopted.
[33] See n. 25 *supra*.
[34] See Form CRS Proposing Release at 24-33.

on their own (e.g., using basic word processing programs), we believe the Commission must consider creating tools that could generate such disclosures on their behalf.

For example, the Commission could maintain an online portal (similar to the IARD) where firms would enter text and/or check boxes, such that consistent and visually appealing disclosure documents (with empirically proven effectiveness) could be generated for them. Collecting data in this sort of a structured format could also lead to innovative ways for investors and the Commission to sort and compare firms. If, as our own testing suggests, a well-designed and visually appealing form is critical to its effectiveness, the Commission should not settle for less.

D. Betterment's Investor Research

Like other interested parties who have already commented,[35] we are extremely supportive of the Commission's desire to test and iterate upon its initial proposal for Form CRS. One of the humbling lessons that you learn in building software is that it isn't always possible to predict how products will be received by real people. Here at Betterment, we are constantly testing, learning from our clients, and improving our offering accordingly. We believe that investor research should be a primary factor in determining the final content of Form CRS, particularly given that past testing has shown the difficulty of conveying financial concepts in a way that investors understand.

Thus, although we had initial reactions to the Form CRS and ideas about how to improve it, we felt that it was critical to see whether they were actually good ideas. Would investors find the document useful? Would they read it? Would it serve its intended purposes? And, how would it compare to the form initially proposed by the Commission on each of these metrics?

We were reluctant to advance "enhancements" to the form that could actually be counterproductive. So, we commissioned investor testing to learn whether we had actually improved the form. It is our hope that the Commission will find approaches that are supported by empirical research--both Betterment's and the Commission's own--to be more compelling and weight them accordingly.

We partnered with the research firm Hotspex. They surveyed 304 current or potential investors over June and July, showing them either the version of Form CRS suggested by the Commission (the "SEC Form") or our alternative form (the "Betterment Form"). Hotspex then asked the respondents a series of questions designed to test the usefulness, appeal, and

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[35] See Letter from AARP et al. to Chairman Clayton (May 21, 2018), *available at* https://consumerfed.org/wp-content/uploads/2018/05/groups-ask-SEC-to-delay-comment-deadline-for-best-interest-proposal.pdf; Letter from Investment Adviser Association to Chairman Clayton (May 25, 2018), *available at* https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/publications/May_25__2018_-_IAA_Comment_Letter_to_SEC_re_Proposed_form_CRS__Proposed_Regulation_Best_Interest__Notice_of_Proposed_Commission_Interpretation_Regarding_Standard_of_Conduct_for_Investment_Advisers_-_Request_for_Investor_Testing.pdf. We considered the specific suggestions advanced in these letters in designing our own investor testing.

effectiveness of each document. Hotspex prepared a report summarizing its research, which is attached to this comment. We outline a few of the more important takeaways below.

Significantly, the research indicated that investors are interested in receiving this type of disclosure. Almost 90% of respondents said that Form CRS was either “very” or “somewhat” useful and fewer than 20% said they would not be motivated to read it (broadly consistent across both the Betterment Form and the SEC Form). As the report notes, “[t]hese findings indicate the importance of the disclosure and value of making it as effective as possible.”

The Betterment Form outperformed the SEC Form on a number of key measures. For example, the Betterment Form resulted in a 68% increase (37% v. 22%) in respondents indicating that the information presented was “very easy to understand,” as well as a 44% increase (26% from 18%) in respondents who described the format as “very appealing.”

Notably, the Betterment Form also appears to have been more effective in communicating important information. To test this, respondents who had viewed one of the forms were asked to indicate if a series of ten statements were “true” or “false” (e.g., “Transaction-based fees create an incentive for an investment firm to trade frequently.”). Respondents who viewed the Betterment Form answered these questions correctly at a 17% higher rate than respondents who viewed the SEC Form (answering an average of approximately seven questions correctly, rather than six). The report also notes that “the greater focus on Betterment specifically in the Betterment Form, as opposed to the SEC Form’s approach of discussing investment advisers more generally, drove increased investor comprehension,” particularly with respect to questions about Betterment itself.

Our research identified specific aspects of each form that were particularly useful or particularly unhelpful, both through targeted questions and by asking respondents to highlight particular portions of the form, indicating whether that portion was “Useful” or “Not Useful” and why. For every measure where there was a statistically significant difference between the forms, the Betterment Form performed better. For example, respondents marked information concerning “fees and costs” to be “useful” at a 91% higher rate on the Betterment Form. This is consistent with respondents’ answers to the specific question of which form more effectively conveyed such information: respondents who viewed the Betterment Form were approximately 15% more likely to indicate that information about fees and costs was clearly communicated. The report notes that investors appear to have appreciated the specificity of the Betterment Form, as well as the example of how fees would impact a hypothetical account.

Similarly, sections comparing Betterment to alternatives (e.g., contrasting Betterment’s asset-based fee with a transaction-based fee), were marked as “useful” at a 67% higher rate on the Betterment Form. Respondents receiving the Betterment Form were also 52% more likely to state that the form helped them understand how other investment options differ from Betterment. According to the report, Betterment’s approach of “co-locating” key contrasts throughout the document appears to have been more effective than the approach taken by the SEC Form.

The Betterment Form's explanation of a fiduciary's obligations was marked as useful at a 111% higher rate than the SEC Form. Since the content here was similar across each form, the higher rate appears to be largely attributable to visual optimizations in the Betterment Form, as well as improvements in the document's overall structure and organization. This jump was also notable because the "fiduciary" classification is both important and challenging to effectively communicate.

Finally, and critically, the new "Alignment of Interests" section in the Betterment Form significantly outperformed the corresponding--and largely blank--"Conflicts of Interest" section in the SEC Form. More than ten times as many respondents marked the Betterment section as "useful." Respondents appear to have appreciated receiving specific information about Betterment's client-alignment in selecting investments.

We would respectfully encourage the Commission to review both our proposed disclosure and the full report of our testing for a more complete picture of this research.

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We are strong supporters of the Commission's efforts to improve the quality of advice delivered to retail investors, as well as investors' understanding of the options that are available to them. This is critically important work, and we hope that the Commission finds our input helpful as it finalizes its proposals, particularly our efforts to enhance and test Form CRS. We look forward to continuing to engage on this rulemaking, including with respect to any summaries of investor testing that the Commission releases in the coming weeks.

Sincerely,

Jon Stein Founder and CEO	Benjamin T. Alden General Counsel	Seth Rosenbloom Associate General Counsel

OPTIMIZING THE SEC'S FORM CRS THROUGH INVESTOR TESTING

AUGUST 2018

Report prepared by:
Lauren Foster, Hotspex Inc.
Aron Galonsky, Hotspex Inc.

Commissioned by Betterment LLC

Table of Contents

About Hotspex

Founded in 2000, Hotspex Inc. (Hotspex) is a consumer research consultancy firm based in Toronto, with offices in New York and London. Hotspex works with 15 of the top 20 global advertisers, from over 34 countries, to pilot and deploy innovative new solutions to uncover consumer insights. Hotspex was voted a top 10 most innovative firm globally and #1 most innovative in North America (GRIT 2018). To find out more, please visit http://www.hotspex.ca/.

Introduction

On April 18, 2018, the Securities and Exchange Commission (the "SEC") proposed a package of new rules designed to "enhance the quality and transparency of investors' relationships with investment advisers and broker-dealers." As part of that package, the SEC proposed a new short-form disclosure document -- "Form CRS" -- intended to provide retail investors with simple, easy-to-understand information about investment firms.

Betterment LLC ("Betterment"), an SEC-registered investment adviser, believes that Form CRS has the potential to advance investor understanding, but that the SEC's form could be improved. A team of Betterment employees attempted to prepare a more effective version of Form CRS, drawing on their backgrounds in design, behavioral economics, and marketing. Because Betterment believes that testing is critical to assessing and optimizing investor communications, Betterment engaged Hotspex to test Betterment's form (the "Betterment Form") and the form proposed by the SEC (the "SEC Form").[1]

Executive Summary

Our testing indicates that investors view Form CRS as an important document and are motivated to read it. Our testing also revealed that the Betterment Form significantly improved upon the SEC Form in several key respects:

1. Investors found the Betterment Form more useful and more understandable than the SEC Form.
2. Investors identified the SEC Form's weaknesses as its complexity, lack of specificity, and lack of clarity.
3. Investors identified the Betterment Form's strengths as its clarity and visual appeal, as well as its approach to explaining expenses, alternative types of providers, and the obligations of different providers.
4. Compared to investors who viewed the SEC Form, investors who saw the Betterment Form were better able to answer a series of questions regarding Betterment and alternatives to Betterment.

The results of the testing are discussed in detail below.

[1] The SEC Form and the Betterment Form are included in the Appendix to this report. In preparing the SEC Form, Betterment followed the SEC's instructions and sample designs, using actual information about Betterment's advisory services. The Betterment Form also used actual information about Betterment's advisory services.

How Did Betterment Optimize the SEC Disclosure?

Betterment redesigned the SEC Form, with the goal of improving its appeal, understandability, and effectiveness in communicating key information to investors. Betterment's changes broadly fall into two categories:

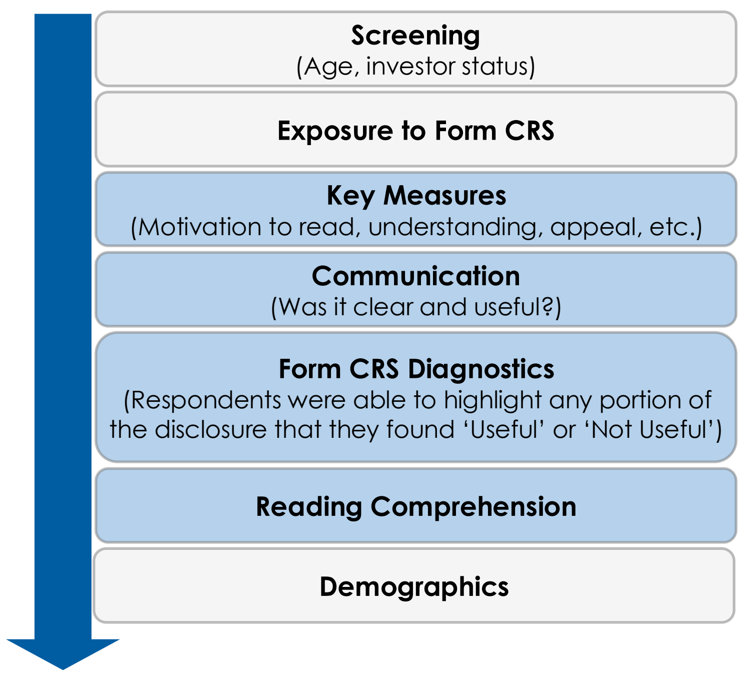
1. **<u>Content Optimizations</u>:** Streamline and focus the information presented, improve the document's organization, and eliminate potentially confusing or misleading content.
2. **<u>Visual Optimizations:</u>** Improve visual hierarchy (e.g., layout, shading), shorten and standardize paragraph lengths to improve legibility, appeal, and retention of information (although the two forms are roughly the same length, the Betterment Form uses 30% fewer words).

How was the Research Conducted?

Hotspex tested the Betterment Form against the SEC Form to assess the relative effectiveness of each disclosure.

Specifically, Hotspex conducted online surveys with a sample of 304 current or potential U.S. investors ages 18 and over from June 28th through July 3rd, 2018. Respondents took an average of twelve minutes to complete the survey. The research design was monadic, with each respondent reviewing and evaluating <u>one</u> of the two versions of Form CRS.

Survey Flow



Individuals were assigned to either the Betterment Form or SEC Form at random, but the samples that were assigned to each group were broadly comparable in terms of demographics. This means that any difference in the results can be attributed to the one variable that changed: *the disclosure itself*.

What Did We Find?

Form CRS is important to investors

Almost **all** respondents (**90%**) indicated that the disclosure (across both the SEC Form and the Betterment Form) was **very** or **somewhat useful. Fewer than 20% of respondents** indicated that it was a document they were not motivated to read. These findings indicate the importance of the disclosure and the value of making it as effective as possible.

Across both forms, a high rate of respondents found the suggested questions to be **very** or **somewhat useful** (82% for the SEC Form and 85% for the Betterment Form). Respondents who viewed the SEC Form were **13% more likely** to indicate that they were **very** or **somewhat likely** to ask the questions (93% v. 81%), suggesting that the Betterment Form itself may have already provided answers to some of the questions.

Relative to the SEC Form, the Betterment Form was more appealing and understandable

The Betterment Form resulted in a **68% increase** (37% v. 22%) in respondents indicating that the information presented was **very easy to understand**, with a **44% increase** (26% v. 18%) in respondents who described the format as **very appealing**. This indicates that Betterment's content and visual optimizations were successful.

Betterment Form:

The Securities and Exchange Commission requires investment firms to provide you with this document to ensure you have a clear picture of the relationship you're considering, as well as the alternatives available to you.

Relationship Summary:
Betterment LLC

As of June 18, 2018

Betterment

Betterment is a **level-fee investment adviser**. That means Betterment will serve you as a **fiduciary**—the highest standard of care—and doesn't have a financial incentive to select particular investments.

OBLIGATIONS
✓ Fiduciary

FEE METHODOLOGY
✓ Asset-based

ALIGNMENT OF INTERESTS
✓ Level-fee

Obligations

Investment adviser – Fiduciary

- As an **investment adviser**, Betterment will provide advice regarding your financial goals and construct and manage investment portfolios on your behalf.
- Betterment, like all **investment advisers**, is held to a **fiduciary** standard that covers its entire relationship with you.
- Betterment must act in your best interest and cannot put its own interests ahead of yours. It is obligated to treat you with the utmost good faith and to provide full and fair disclosure of all material facts.
- Betterment must seek to avoid conflicts of interest and tell you about any remaining conflicts in a way that you can understand, so that you can decide whether you are willing to accept them.
- Betterment is required to monitor your portfolio, investment strategy, and investments on an ongoing basis.

SEC Form:

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 gather information about your investment goals, design with you a strategy to achieve your investment goals, and regularly monitor your account. We will contact you by e-mail at least quarterly to determine whether there have been any changes to your financial situation or goals. • If you open an advisory account, you will authorize us to buy and sell investments in your account without asking you in advance (a "***discretionary account***"). • We will only buy exchange-traded funds ("ETFs") for your account. Other firms may offer a wider range of choices.
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.

- BETTERMENT LLC, an investment adviser registered with the Securities and Exchange Commission, June 18, 2018 -

The Betterment Form better educated investors

Respondents who viewed the Betterment Form demonstrated superior understanding and retention of key information about Betterment, as well as alternative types of investment firms (broker-dealers and differently compensated investment advisers), as compared to respondents who viewed the SEC Form.

Specifically, respondents were asked to indicate if a series of ten statements were true or false. Respondents who viewed the Betterment Form performed **17% better** with respect to their aggregate scores than respondents who viewed the SEC Form (approximately 7 questions answered correctly vs. 6 questions answered correctly).

Among other factors, it appears that the greater focus on Betterment in the Betterment Form, as opposed to the SEC's Form approach of discussing investment advisers more generally, drove increased investor comprehension. Respondents who viewed the Betterment Form scored **17% higher** when asked if Betterment is a fiduciary, **19% higher** when asked if Betterment clients pay fund-level fees in addition to Betterment's fee, and **128% higher** when asked if Betterment benefits financially from some of the funds it recommends to clients. Respondents also scored **28% higher** when asked if Investment advisers are held to a higher standard than broker-dealers.

True or False	SEC Form	Betterment Form
Total Answering	154	150
Average Reader Score (out of 10):	5.96	6.86
Correctly Identify as TRUE		
Betterment is a fiduciary	71%	83%
Investment advisers are held to a higher standard than broker-dealers	58%	74%
Betterment charges a percentage fee that is based on the value of your account	81%	85%
Transaction-based fees create an incentive for an investment firm to trade frequently	81%	75%
Broker-dealers charge a separate fee each time they buy or sell an investment for you	77%	75%
Betterment clients pay fund-level fees in addition to Betterment's fee	58%	69%
Some investment firms have a conflict of interest because they benefit financially from recommending certain investments	83%	78%
Correctly Identify as FALSE		
Broker-dealers are held to a fiduciary standard	26%	56%
Broker-dealers typically monitor clients' portfolios and provide advice on an ongoing basis	37%	34%
Betterment benefits financially from some of the funds it recommends to clients	25%	57%

Legend	
(green)	Statistically significant at the 95% confidence level

What Were the Specific Strengths of the Betterment Approach?

As noted above, respondents found the Betterment Form more appealing and understandable. Respondents were also asked to highlight specific portions of each document, indicating whether they found those portions "Useful" or "Not Useful." Overall, respondents who reviewed the Betterment Form marked **16% more** (87% v. 75%) of the document useful than respondents who reviewed the SEC Form. While respondents generally indicated the same categories of information were "Useful" or "Not Useful" in both documents, respondents who viewed the Betterment Form were more likely to mark each category of information as useful, as compared to respondents who viewed the SEC Form.

Total "Useful" and "Not Useful" Comments

	"Useful" Comments	**"Not Useful" Comments**
Betterment Form	333 (avg. 2.22 per person)	51 (avg. 0.34 per person)
SEC Form	278 (avg. 1.80 per person)	92 (avg. 0.60 per person)

Visual representations of the results of this portion of the study are available at the below links:

- Betterment Form
- SEC Form

The degree of shading in the highlighting indicates the number of respondents marking a section of the document as "Useful" or "Not Useful," which can be viewed as a percentage by hovering over a particular section.[2]

Fees and Costs

In the Betterment Form, respondents found the inclusion of specific fees (not part of the SEC Form) to be particularly useful. This section was marked useful at a **91% higher** rate than the parallel section in the SEC Form (21% v. 11%). Example respondent comments regarding usefulness of the Betterment Form are shown below.

[2] Note that the percentages reflected in these visual representations may vary slightly from the percentages presented in this report. That is because some of the numbers in the report aggregate sections of the document that are broken out separately in the visual representation.

"Plain and simple, shows an example of what the fees will cost you"

Fee Methodology

Asset-based

As compensation for investment advice and the cost of making trades in your account, you'll pay Betterment an **annual fee of 0.25%** of the value of your assets with it.

$ For an account with a balance of $50,000, this fee would amount to $125 a year.

Alignment of Interests

Level-fee

Independent of Betterment's annual fee, you will pay "fund fees" to the companies that manage the funds in which you invest. Betterment does not benefit from these fees in any way.

"Upfront and easy to understand statement about fees"

The **median annual fund fees** for a portfolio at Betterment total **0.10%**.

$ For an account with a balance of $50,000, these fees would amount to $50 a year.

This is consistent with respondents' answers to the specific question regarding which form more effectively conveyed information about costs and fees. Respondents who viewed the Betterment Form were approximately **15% more likely** (82% v. 71%) than respondents who viewed the SEC Form to indicate that information about costs and fees was **clearly communicated**.

Comparisons to Alternatives

The sections comparing Betterment to alternative types of investment firms (e.g., broker-dealers or investment advisers with different business models) were marked as useful at a **67% higher rate** (15% v. 9%) by respondents who reviewed the Betterment Form. The approach of integrating these contrasts with descriptions of Betterment appears to have been more effective than the approach taken by the SEC Form, which largely isolated broker-dealer comparisons in a standalone section.

"This is an easy to understand explanation of how Betterment differs from other financial services firms"

"Helps to understand the difference between advisory and other financial advisers"

Alternative
Transaction-based

- Offered by broker-dealers.
- Fees are charged any time you buy or sell an investment.
- May be accompanied by additional fees, such as custodian fees, account maintenance fees, and account inactivity fees.
- Create an incentive for broker-dealers to trade frequently in your account to increase their compensation.

Alternative
Broker-dealer

- Typically makes recommendations about specific securities transactions, rather than ongoing advice and investment monitoring.
- Held to a lower standard than fiduciaries; however, recommendations must be consistent with your best interests.
- Not required to avoid conflicts of interest, but must disclose any material conflicts and, in some cases, mitigate them.

Alternative
Variable-fee

- Firms with variable fees make more money when they select certain investments for you.
- Some receive payments from the companies that manage funds, or manage the funds themselves, allowing them to benefit directly from the fund fees you pay.
- These firms have a conflict of interest because their financial interests don't always align with your interests.

Again, this is consistent with how respondents answered a question about each form's effectiveness in drawing comparisons with other options. Respondents who saw the Betterment Form were **52% more likely** (35% v. 23%) to indicate that the disclosure helped them **understand** how other investment firms differ from Betterment.

Obligations

The Betterment Form was **111% more useful** (19% v. 9%) in explaining the obligations of a fiduciary, a difficult concept to comprehend, but an important distinction between investment advisers and broker-dealers.

"Many brokers focus on their own best interests, not their clients'. This document explains how Betterment cannot do that"

Obligations
Investment adviser – Fiduciary

- As an **investment adviser**, Betterment will provide advice regarding your financial goals and construct and manage investment portfolios on your behalf.
- Betterment, like all **investment advisers**, is held to a **fiduciary** standard that covers its entire relationship with you.
- Betterment must act in your best interest and cannot put its own interests ahead of yours. It is obligated to treat you with the utmost good faith and to provide full and fair disclosure of all material facts.
- Betterment must seek to avoid conflicts of interest and tell you about any remaining conflicts in a way that you can understand, so that you can decide whether you are willing to accept them.
- Betterment is required to monitor your portfolio, investment strategy, and investments on an ongoing basis.

Alignment of Interests

The Betterment Form added a new section called "Alignment of Interests" to replace and clarify the section on the SEC Form titled "Conflicts of Interest." The Betterment Form was significantly more useful (10% v. 0.81%) than the parallel section on the SEC Form.

"This is important to understand the fees that I might pay"

Alignment of Interests
Level-fee

Independent of Betterment's annual fee, you will pay "fund fees" to the companies that manage the funds in which you invest. Betterment does not benefit from these fees in any way.

The **median annual fund fees** for a portfolio at Betterment total **0.10%**.

$ For an account with a balance of $50,000, these fees would amount to $50 a year.

HOW THIS AFFECTS YOUR RELATIONSHIP

Betterment has no financial incentive to choose particular funds for you and is fully aligned with your interests.

Investors appear to have appreciated the specific information about Betterment's client-alignment. They did not find the largely blank section regarding "Conflicts of Interest" on the SEC Form to be particularly useful.

> **Conflicts of Interest.** *We benefit from the advisory services we provide to you.*

What Further Improvements Could be Made?

While the Betterment Form significantly improved upon the SEC Form in several respects, additional optimizations may be possible.

1. **Understanding of Broker-Dealers**: Regardless of which form they saw, most respondents failed to understand that broker-dealers do not typically monitor portfolios or provide advice on an ongoing basis. Similarly, across both forms, many investors failed to understand that broker-dealers are not fiduciaries.

2. **Understanding of Differences in Conflicts**: Although respondents who reviewed the Betterment Form demonstrated significantly greater understanding of conflicts of interest, there may be room for improvement. For example, even though the Betterment Form almost doubled the number of investors who correctly understood that Betterment does not financially benefit from recommending investments, almost half of respondents still answered that question incorrectly.

3. **Unclear Terminology**: Across both tested forms, respondents found certain terminology (e.g., "fiduciary," "asset-based," "ETF") to be unclear or lack sufficient detail (e.g., references to "portfolio monitoring").

Conclusion

Form CRS could play an important role in helping investors better understand investment firms, as well as alternative options that are available to them. Although further enhancements of the form are still possible, our testing indicates that Betterment has successfully identified optimizations that significantly improve its effectiveness.

Appendix[3]

Betterment's Proposed Form CRS
(the "Betterment Form")

[3] For each form, we have provided examples of how the form would appear in a web browser (which was tested with investors) and a printable version of the document.

The Securities and Exchange Commission requires investment firms to provide you with this document to ensure you have a clear picture of the relationship you're considering, as well as the alternatives available to you.

Relationship Summary: Betterment LLC

As of June 18, 2018

Betterment

Betterment is a **level-fee investment adviser**. That means Betterment will serve you as a **fiduciary**—the highest standard of care—and doesn't have a financial incentive to select particular investments.

OBLIGATIONS
✓ Fiduciary

FEE METHODOLOGY
✓ Asset-based

ALIGNMENT OF INTERESTS
✓ Level-fee

Obligations

Investment adviser – Fiduciary

- As an **investment adviser**, Betterment will provide advice regarding your financial goals and construct and manage investment portfolios on your behalf.
- Betterment, like all **investment advisers**, is held to a **fiduciary** standard that covers its entire relationship with you.
- Betterment must act in your best interest and cannot put its own interests ahead of yours. It is obligated to treat you with the utmost good faith and to provide full and fair disclosure of all material facts.
- Betterment must seek to avoid conflicts of interest and tell you about any remaining conflicts in a way that you can understand, so that you can decide whether you are willing to accept them.
- Betterment is required to monitor your portfolio, investment strategy, and investments on an ongoing basis.

Alternative
Broker-dealer

- Typically makes recommendations about specific securities transactions, rather than ongoing advice and investment monitoring.
- Held to a lower standard than fiduciaries; however, recommendations must be consistent with your best interests.
- Not required to avoid conflicts of interest, but must disclose any material conflicts and, in some cases, mitigate them.

Fee Methodology

Asset-based

As compensation for investment advice and the cost of making trades in your account, you'll pay Betterment an **annual fee of 0.25%** of the value of your assets with it.

$ For an account with a balance of $50,000, this fee would amount to $125 a year.

HOW THIS AFFECTS YOUR RELATIONSHIP

- Betterment has an incentive to increase or maintain the assets in your account to increase its own compensation.
- Because Betterment doesn't separately charge you for trades, it has an incentive to minimize trade frequency to limit its own trading costs.

Alternative
Transaction-based

- Offered by broker-dealers.
- Fees are charged any time you buy or sell an investment.
- May be accompanied by additional fees, such as custodian fees, account maintenance fees, and account inactivity fees.
- Create an incentive for broker-dealers to trade frequently in your account to increase their compensation.

Alignment of Interests

Level-fee

Independent of Betterment's annual fee, you will pay "fund fees" to the companies that manage the funds in which you invest. Betterment does not benefit from these fees in any way.

The **median annual fund fees** for a portfolio at Betterment total **0.10%**.

$ For an account with a balance of $50,000, these fees would amount to $50 a year.

HOW THIS AFFECTS YOUR RELATIONSHIP

- Betterment has no financial incentive to choose particular funds for you and is fully aligned with your interests.

Alternative
Variable-fee

- Firms with variable fees make more money when they select certain investments for you.
- Some receive payments from the companies that manage funds, or manage the funds themselves, allowing them to benefit directly from the fund fees you pay.
- These firms have a conflict of interest because their financial interests don't always align with your interests.

Important Questions to Ask Your Adviser

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. 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?
4. 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.
5. How will you choose investments to recommend for my account?
6. How often will you monitor my account's performance and offer investment advice?
7. Do you or your firm have a disciplinary history? For what type of conduct?
8. What is the relevant experience of your investment professionals, including licenses, education, and other qualifications?
9. 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?

Additional Information

- Form ADV brochure (detailed explanation of Betterment's advisory services)
- Relationship summaries provided by other firms
- Investor.gov (for resources and research about any firm and its advisory professionals including disciplinary history)

The Securities and Exchange Commission requires investment firms to provide you with this document to ensure you have a clear picture of the relationship you're considering, as well as the alternatives available to you.

Relationship Summary: Betterment LLC

As of June 18, 2018

Betterment

Betterment is a **level-fee investment adviser**. That means Betterment will serve you as a **fiduciary**—the highest standard of care—and doesn't have a financial incentive to select particular investments.

OBLIGATIONS

✓ **Fiduciary**

FEE METHODOLOGY

✓ **Asset-based**

ALIGNMENT OF INTERESTS

✓ **Level-fee**

Obligations

Investment adviser – Fiduciary

- As an **investment adviser**, Betterment will provide advice regarding your financial goals and construct and manage investment portfolios on your behalf.
- Betterment, like all **investment advisers**, is held to a **fiduciary** standard that covers its entire relationship with you.
- Betterment must act in your best interest and cannot put its own interests ahead of yours. It is obligated to treat you with the utmost good faith and to provide full and fair disclosure of all material facts.
- Betterment must seek to avoid conflicts of interest and tell you about any remaining conflicts in a

way that you can understand, so that you can decide whether you are willing to accept them.

- Betterment is required to monitor your portfolio, investment strategy, and investments on an ongoing basis.

Alternative **Broker-dealer**	• Typically makes recommendations about specific securities transactions, rather than ongoing advice and investment monitoring. • Held to a lower standard than fiduciaries; however, recommendations must be consistent with your best interests. • Not required to avoid conflicts of interest, but must disclose any material conflicts and, in some cases, mitigate them.

Fee Methodology

Asset-based

As compensation for investment advice and the cost of making trades in your account, you'll pay Betterment an **annual fee of 0.25%** of the value of your assets with it.

$ For an account with a balance of $50,000, this fee would amount to $125 a year.

HOW THIS AFFECTS YOUR RELATIONSHIP

- Betterment has an incentive to increase or maintain the assets in your account to increase its own compensation.
- Because Betterment doesn't separately charge you for trades, it has an incentive to minimize trade frequency to limit its own trading costs.

Alternative **Transaction-based**	• Offered by broker-dealers. • Fees are charged any time you buy or sell an investment. • May be accompanied by additional fees, such as custodian fees, account maintenance fees, and account inactivity fees. • Create an incentive for broker-dealers to trade frequently in your account to increase their compensation.

Alignment of Interests

Level-fee

Independent of Betterment's annual fee, you will pay "fund fees" to the companies that manage the funds in which you invest. Betterment does not benefit from these fees in any way.

The **median annual fund fees** for a portfolio at Betterment total **0.10%**.

$ For an account with a balance of $50,000, these fees would amount to $50 a year.

HOW THIS AFFECTS YOUR RELATIONSHIP

Betterment has no financial incentive to choose particular funds for you and is fully aligned with your interests.

Alternative **Variable-fee**	• Firms with variable fees make more money when they select certain investments for you. • Some receive payments from the companies that manage funds, or manage the funds themselves, allowing them to benefit directly from the fund fees you pay. • These firms have a conflict of interest because their financial interests don't always align with your interests.

Important Questions to Ask Your Adviser

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The SEC's Proposed Form CRS
(the "SEC Form")

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 gather information about your investment goals, design with you a strategy to achieve your investment goals, and regularly monitor your account. We will contact you by e-mail at least quarterly to determine whether there have been any changes to your financial situation or goals.
- If you open an advisory account, you will authorize us to buy and sell investments in your account without asking you in advance (a "***discretionary account***").
- We will only buy exchange-traded funds ("ETFs") for your account. Other firms may offer a wider range of choices.

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.

- BETTERMENT LLC, an investment adviser registered with the Securities and Exchange Commission, June 18, 2018 -

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.
- 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.
- The ETFs that we will purchase for your account impose additional fees that will reduce the value of your investment over time.
- Our fees are not negotiable, but we may reduce or waive them in certain circumstances.
- 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.

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.*

Additional Information. *We encourage you to seek additional information.*

- 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 (www.betterment.com/adv).
- 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 61 W. 23rd Street, 4th Floor, New York, NY 10010 or at legal@betterment.com.

Key Questions to Ask. *Ask us these key questions about our investment services and accounts.*

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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?
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