

**MEMO# 25968**

March 7, 2012

# **ICI Draft Letter in Response to SEC Comment Request for Study Regarding Financial Literacy Among Investors; Member Comments Requested by March 15**

[25968]

March 7, 2012

TO: SEC RULES COMMITTEE No. 16-12 RE: ICI DRAFT LETTER IN RESPONSE TO SEC  
COMMENT REQUEST FOR STUDY REGARDING FINANCIAL LITERACY AMONG INVESTORS;  
MEMBER COMMENTS REQUESTED BY MARCH 15

As we previously informed you, [\[1\]](#) the SEC has requested public comment on issues pertaining to financial literacy among investors in connection with a study it is required to conduct under Section 917 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. [\[2\]](#) Consistent with the express language of the Act, the Commission requested comment on: (i) methods to improve the timing, content, and format of disclosures to investors with respect to financial intermediaries, investment products, and investment services; (ii) the most useful and understandable relevant information that retail investors need to make informed financial decisions before engaging a financial intermediary or purchasing an investment product or service that is typically sold to retail investors, including shares of registered open-end investment companies (“mutual funds”); and (iii) methods to increase the transparency of expenses and conflicts of interest in transactions involving investment services and products, including shares of mutual funds.

The ICI has prepared a draft comment letter, which is attached and summarized below. Comments are due to the SEC no later than March 23, 2012. Please provide your comments on the ICI’s draft letter by March 15 to Tami Salmon at [tamara@ici.org](mailto:tamara@ici.org) or 202-326-5825 or Mara Shreck at [mshreck@ici.org](mailto:mshreck@ici.org) or 202-326-5923.

# Summary of Draft Letter

The draft letter begins by expressing support for a holistic, well-considered, and thorough approach to disclosure to retail investors about the variety of investment products and services sold or offered to them. It then offers comments on each of the issues listed in the Release.

## **I. Methods to improve the timing, content, and format of disclosures to investors with respect to financial intermediaries, investment products, and investment services**

### **a. Methods to Improve the Timing of Disclosure**

The draft letter expresses support for the concept of enhanced disclosure at or before the point of sale, subject to two overarching concerns. First, the Institute has consistently expressed concern about the possibility of limiting any point of sale disclosure requirement to the sale of mutual funds. We believe such an approach would provide incomplete investor protection and may in practice disserve investors. Imposing point of sale obligations only on the offer or sale of mutual funds could create strong incentives for broker-dealers and other financial intermediaries to recommend investment products not subject to the same regulatory burdens, such as variable annuity contracts, collective investment trusts, and separate accounts, even when those products do not offer the same level of regulatory protection and other benefits for investors. To avoid these adverse consequences, any point of sale disclosure obligation should be product-neutral.

Second, any point of sale disclosure requirement must be designed to minimize disruptions to the sales process. Investment sales typically occur by telephone or over the Internet, rather than through face-to-face meetings, so requiring the physical transfer of a disclosure document is not realistic. Relatedly, any required disclosure must be appropriately tailored to the type of financial intermediary providing the disclosure and its relationship with customers.

### **b. Methods to Improve the Content of Disclosure**

The draft letter offers a number of considerations to improve the content of disclosure. First, it is critical to tailor the disclosure to its intended purpose: e.g., to educate investors about a financial intermediary and its services and operations or about an investment product. Second, effective investor research can dramatically strengthen the quality of disclosure rulemaking. Third, a focus on the delivery mechanism for disclosure – and in particular, a considered shift to electronic media – can have a substantial impact on its quality. Specifically, the Internet offers a vehicle for providing investors with exactly the amount of information they want, whenever they want it. Attention to the delivery mechanism for investment information will improve the quality of disclosure by improving the ability of investors to access the information they seek.

### **c. Methods to Improve the Format of Disclosures**

The draft letter recommends that the Commission focus on the delivery

mechanism for disclosure, and in particular electronic delivery. It explains that using the Internet as the primary vehicle for providing information to investors will help to address many of the concerns the Institute has raised about previous point of sale disclosure initiatives.

## **II. The most useful and understandable relevant information that retail investors need to make informed financial decisions before engaging a financial intermediary or purchasing an investment product or service that is typically sold to retail investors, including shares of registered open-end investment companies**

### **a. Information Needed Before Engaging a Financial Intermediary**

The draft letter states that the Institute continues to support disclosures that inform retail investors and potential investors of the services offered by financial intermediaries, as well as the conflicts of interest that may arise in connection with such offerings or recommendations. It recommends that the Commission use Rule 204-3 under the Investment Advisers Act of 1940, the “Brochure Rule,” as a starting point for considering, as part of its current study, the contents and timing of disclosure that broker-dealers should be required to provide to their customers, and suggests specific types of information that should be included in such a “brochure.” It further recommends that such a document be in a standardized and easy-to-read format; be provided to retail customers who contact a retail broker-dealer to effect a transaction or open an account; and be provided either prior to or at the time an account is opened or the customer commences a relationship with the broker-dealer.

### **b. Information Needed Before Purchasing an Investment Product or Service**

The draft letter states that, in addition to information about financial intermediaries, investors and potential investors should be provided with key information about the product or service they are considering or buying. It recommends that, to the extent possible, such content should be similar across products sold to retail investors.

## **III. Methods to increase the transparency of expenses and conflicts of interest in transactions involving investment services and products, including shares of mutual funds**

The draft letter notes that a variety of fees and expenses may be charged to investors in connection with the sale of financial products or the provision of financial services. It states that, to improve the quality of disclosure in these areas, it is critical to recognize that intermediary disclosure and product disclosure are necessarily distinct, and to place the disclosure obligation on the appropriate party.

The draft letter recommends that, to increase the transparency and clarity of disclosure regarding expenses and conflicts of interest, the Commission carefully consider the appropriate source of disclosure for each of these elements. To ensure that investors

recognize that there may be different types of fees associated with their investment – i.e., those charged by the mutual fund or other investment product and those charged by the broker-dealer – these disclosures could cross-reference one another.

Mara Shreck  
Associate Counsel

[Attachment](#)

**endnotes**

[\[1\]](#) See ICI [Memorandum](#) No. 25812, dated Jan. 19, 2012.

[\[2\]](#) See Comment Request for Study Regarding Financial Literacy Among Investors, SEC Release No. 34-66164 (January 17, 2012) (the “Release”), available at: <http://www.sec.gov/rules/other/2012/34-66164.pdf>.

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