

# Analysis of ACLI Board Principles Against the SEC Best Interest Standard of Care Proposals

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## **1. A RECOMMENDATION MUST REFLECT CARE, SKILL, PRUDENCE, AND DILIGENCE.**

### **Principle in Proposed SEC Regulation Best Interest**

Broker-Dealers obligated to “exercise reasonable diligence, care, skill, and prudence.”<sup>1,2</sup>

### **Principle in ACLI Submission to the SEC**

ACLI recommended that a “constructive best interest standard would require financial professionals to put a consumer’s interest first by acting with reasonable care, skill, prudence, and diligence in gathering and evaluating information regarding the consumer that is used to make the recommendation.”<sup>3</sup>

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## **2. A PERSON MAKING A RECOMMENDATION MUST ADDRESS MATERIAL FINANCIAL CONFLICTS OF INTEREST.**

### **Principle in Proposed SEC Regulation Best Interest**

Broker-Dealer should “reasonably disclose to the retail customer, in writing, the material facts relating to the scope and terms of the relationship with the retail customer and all material conflicts of interest associated with the recommendation” and the “fees and charges that apply to the retail customer’s transactions, holdings, and accounts.”<sup>4</sup>

### **Principle in ACLI Submission to the SEC**

ACLI recommended that a “constructive best interest standard would require financial professionals to put a consumer’s interest first by avoiding, disclosing, or otherwise reasonably managing material conflicts of interest.”<sup>5</sup>

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## **3. CONSUMERS SHOULD KNOW THE TYPES AND SCOPE OF SERVICES THEY WILL RECEIVE AS WELL AS THE TYPES OF COMPENSATION TO BE RECEIVED BY THE PERSON MAKING THE RECOMMENDATION.**

### **Principle in Proposed SEC Regulation Best Interest**

Under the regulation’s disclosure obligation, the SEC emphasized that salespersons should disclose “the scope and terms of the relationship with the retail customer” and the “fees and charges that apply to the retail customer’s transactions, holdings, and accounts.” “It is necessary to impose a more explicit disclosure obligation on broker-dealers than what currently exists under the federal securities laws and SRO rules.”<sup>6</sup>

### **Principle in ACLI Submission to the SEC**

ACLI recommended that a “constructive best interest standard would require financial professionals to put a consumer’s interest first by providing full and fair disclosure of the recommended product’s features, fees, and charges and, fairly disclosing how and by whom the financial professional is compensated.”<sup>7</sup>

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**4. THE STANDARD IS TO APPLY WHEN A RECOMMENDATION IS MADE WITH NO FURTHER OR ONGOING OBLIGATION TO THE CONSUMER UNLESS OTHERWISE AGREED TO.**

**Principle in Proposed SEC Regulation Best Interest**

The SEC explained that “the best interest obligation would not extend beyond a particular recommendation or generally require a broker-dealer to have a continuous duty to a retail customer or impose a duty to monitor the performance of the account.”<sup>8</sup>

**Principle in ACLI Submission to the SEC**

ACLI recommended that “the uniform standard of care is a transaction based standard that is applied when a recommendation is made, and there is no further or ongoing obligation under the standard.”<sup>9</sup>

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**5. RULES MUST BE NEUTRAL TO BUSINESS MODEL, PRODUCT TYPE, AND COMPENSATION APPROACH SUCH AS COMMISSIONS OR SALES CHARGES, OR OTHER FEES OR VARIABLE COMPENSATION.**

**Principle in Proposed SEC Regulation Best Interest**

The SEC explained that “under proposed Regulation Best Interest, broker-dealers would have the flexibility to establish systems that are tailored to their business models, and to focus on specific areas of their business that pose the greatest risk of violating the Conflict of Interest Obligations.”<sup>10</sup> SEC states that the overall intent of Section 913 [of the Dodd-Frank Act] “did not prohibit, mandate or promote particular types of products or business models, and preserved investor choice among such services and products and how to pay for these services and products (e.g., by preserving commission-based accounts, episodic advice, principal trading and the ability to offer only proprietary products to customers).”<sup>11</sup>

**Principle in ACLI Submission to the SEC**

ACLI stated that “compensation in the delivery of financial advice and products has evolved to include different business models and to utilize advances in technology. These market-based developments provide a wide range of choice for both consumers and advisers. Regulation of compensation practices, however, should be unbiased and permit a broad spectrum of compensation arrangements.”<sup>12</sup>

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**6. THE FACT THAT AN ADVISOR OR FIRM ONLY OFFERS OR RECOMMENDS PROPRIETARY OR A LIMITED RANGE OF PRODUCTS OR PRODUCT TYPES OR RECEIVES COMMISSIONS OR OTHER VARIABLE COMPENSATION IS NOT INCONSISTENT WITH A BEST INTEREST STANDARD.**

**Principle in Proposed SEC Regulation Best Interest**

SEC states that the overall intent of Section 913 [of the Dodd-Frank Act] “did not prohibit, mandate or promote particular types of products or business models, and preserved investor choice among such services and products and how to pay for these services and products (e.g., by preserving commission-based accounts, episodic advice, principal trading and the ability to offer only proprietary products to customers).”<sup>13</sup>

**Principle in ACLI Submission to the SEC**

ACLI explained that “the Dodd-Frank Act provides that offering a limited range of products, including offering only proprietary products, would be disclosed and permissible under any new standard of care. Any post-CRFI SEC or FINRA rulemaking should not require or mandate that a BD expand the securities products or services it offers. Conversely, in implementing this requirement, the SEC or FINRA must also be careful to avoid promulgating rules or guidance that would unnecessarily favor one type of securities product over another or lessen retail customer access to, what some may view as more complicated securities products or, proprietary products when other securities products are available.”<sup>14</sup>

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## **7. THE BEST INTEREST STANDARD MUST NOT REQUIRE A RECOMMENDATION OF THE LEAST EXPENSIVE OR “BEST” PRODUCT AVAILABLE.**

### **Proposed SEC Regulation Best Interest**

SEC states that Proposed Regulation Best Interest also would not necessarily obligate a broker-dealer to recommend the “least expensive” or the “least remunerative” security or investment strategy, provided the broker-dealer complies with the Disclosure, Care, and the Conflict of Interest Obligations.”<sup>15</sup>

### **ACLI Recommendations in Submission to the SEC**

ACLI’s submission stated that a “uniform standard of care does not require a recommendation of the least expensive or ‘best’ product available.”<sup>16</sup>

## Citations to ACLI Positions in SEC Initiatives

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### **SEC Regulation Best Interest Reference to ACLI Submission**

SEC statement: “commenters asserted that the commission-based model may be more appropriate for many investors.”<sup>17</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>18</sup>

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### **SEC Regulation Best Interest Reference to ACLI Submission**

SEC statement that “many commenters have stressed the importance of clear fee disclosure to retail investors.”<sup>19</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>20</sup>

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### **SEC Regulation Best Interest Reference to ACLI Submission**

SEC explained that the proposal “provides broker-dealers with flexibility in determining the most appropriate way to meet this Disclosure Obligation depending on each broker-dealer’s business practices, consistent with the principles set forth below and in line with the suggestion of some commenters that stressed the importance of allowing broker-dealers to select the form and manner of delivery of disclosure.”<sup>21</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>22</sup>

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### **SEC Proposed Form CRS References to ACLI Submission**

“Commenters recommended a short disclosure document that explains the firm’s services, fees, certain conflicts of interest, and the scope and nature of its services to the retail investor.”<sup>23</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>24</sup>

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### **SEC Proposed Form CRS References to ACLI Submission**

Commentators “recommended that both broker-dealers and investment advisers should provide a uniform disclosure document to retail investors.”<sup>25</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>26</sup>

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### **SEC Proposed Form CRS References to ACLI Submission**

“As several commenters have recommended, we propose requiring that firms use “plain language principles for the organization, wording, and design of the entire relationship summary, taking into consideration retail investors’ level of financial sophistication.”<sup>27</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>28</sup>

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### **SEC Proposed Form CRS References to ACLI Submission**

Succinct disclosure “is consistent with our experience and commenters’ suggestion that brief disclosure is more effective than a long-form narrative to focus retail investors on relevant information, and with suggestions from commenters who advocated for a clear, concise disclosure.”<sup>29</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>30</sup>

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### **SEC Proposed Form CRS References to ACLI Submission**

“Many commenters have stressed the importance of clear fee disclosure to retail investors, including disclosure about differences between advisory and brokerage fees.”<sup>31</sup>

### **SEC Reference to ACLI Recommendation**

Direct citation to ACLI 10.3.17 Submission supporting this outcome.<sup>32</sup>

# Aspects of the SEC Standard of Care Initiatives Not Covered by the Board Principles

The SEC proposals also touch on areas not considered in the Board principles. Those features will be evaluated through ACLI's Committee process to assure they properly mesh with life insurers' interests. Examples in the SEC initiatives outside the Board principles include, among others:

- Clarity and Meaning of the Term "Best Interest;"
- Restrictions on the Use of Certain Advisory Names or Titles;
- Reporting and Recordkeeping Requirements in the Proposed Form Customer Relationship Summary (CRS);
- Proposed Suitability Interpretations Governing Investment Advisers;
- Financial Responsibility or Net Capital Standards for Investment Advisers;
- Required Content in the Proposed Form Customer Relationship Summary (CRS);
- More Rigorous Investment Adviser Regulation;
- Collection and Recordkeeping of Customer Information;
- Whether Investment Professionals Acting Appropriately Can Efficiently Demonstrate Compliance with a New Best Interest Standard;
- Whether the SEC Can Properly Inspect for Compliance with a New Best Interest Standard;
- The Economic and Competitive Impact of the Three Principal SEC Initiatives;
- Investment Adviser Subordination of its Interests to Client's Interest;
- Licensing and Continuing Education Requirements for Investment Adviser Personnel;
- Frequency and Scope of Investment Adviser Account Statements; and,
- Financial Responsibility or Net Capital Standards for Investment Advisers,

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## Endnotes

- <sup>1</sup> Proposed SEC Regulation Best Interest requires broker-dealers exercise reasonable diligence, care, skill, and prudence to understand potential risks and rewards and have a reasonable basis for believing that the recommended transaction or investment strategy is in the best interest of the retail customer. See Proposed Regulation Best Interest at 1, 8, 44, 133,136,141, 150, 156, 157, 161, 162, 192, 249, 263, 285, 379, 393, 404. Proposed paragraph (a) (25) to Rule 17a-3 would impose new record-making obligations on broker-dealers subject to Regulation Best Interest, while the Proposed Amendment to Rule 17a-4(e)(5) would impose new record retention obligations on broker-dealers subject to Regulation Best Interest.
- <sup>2</sup> ACLI submitted a [response](#) to the SEC Chairman's *Request for Information about Standards of Conduct for Broker-Dealers and Investment Advisers* (Oct. 3, 2017) found at <https://www.sec.gov/comments/ia-bd-conduct-standards/cl4-2640466-161282.pdf>. ACLI filed other submissions with the SEC at different stages of similar matters, including: ACLI's July 5, 2013 [Submission](#) in response to the SEC's *Request for Data and Information on Brokers, Dealers and Investment Advisers*; ACLI's August 30, 2010 Submission in response to the SEC's request for information on its [Study on the Responsibilities of Brokers, Dealers, and Investment Advisers](#) in fulfillment of Section 913 of the Dodd-Frank Act; and ACLI's December 13, 2007 [Submission](#) in response to the *RAND Study on Broker-Dealer and Investment Advisory Issues*.
- <sup>3</sup> See ACLI comment letter at 10.
- <sup>4</sup> See Proposed SEC Regulation Best Interest Proposal at 98.
- <sup>5</sup> See ACLI comment letter at 10.
- <sup>6</sup> See Proposed SEC Regulation Best Interest Proposal at 98.
- <sup>7</sup> See ACLI comment letter at 10.
- <sup>8</sup> See Proposed SEC Regulation Best Interest Proposal at 79.
- <sup>9</sup> See ACLI comment letter at 8.
- <sup>10</sup> See Proposed SEC Regulation Best Interest Proposal at 399.
- <sup>11</sup> See Proposed SEC Regulation Best Interest Proposal at 49.
- <sup>12</sup> ACLI Comment Letter at 14.
- <sup>13</sup> See Proposed SEC Regulation Best Interest Proposal at 49.
- <sup>14</sup> ACLI Comment Letter at 21.

- <sup>15</sup> See Proposed SEC Regulation Best Interest Proposal at 54.  
<sup>16</sup> *Id.* at 8.  
<sup>17</sup> See Proposed Regulation Best Interest Release at 38.  
<sup>18</sup> See Proposed Regulation Best Interest Release at footnote 82, noting ACLI statement that “[r]ecurrent annual fees may be ill-suited to individuals with moderate assets needing little annual advice, and may exceed the total value of a commissioned-based adviser.”  
<sup>19</sup> See Proposed Regulation Best Interest Release at 105.  
<sup>20</sup> See Proposed Regulation Best Interest Release at footnote 191 noting ACLI recommended “among other things, full and fair disclosure of the recommended product’s features, fees, and charges, and fairly disclosing how and by whom the financial professional is compensated.”  
<sup>21</sup> See Proposed SEC Regulation Best Interest Proposal at 114.  
<sup>22</sup> See Proposed Regulation Best Interest Release at footnote at 206 noting ACLI’s comments.  
<sup>23</sup> See Proposed Form CRS Release at 8.  
<sup>24</sup> See Proposed Form CRS Release at footnote 8.  
<sup>25</sup> See Proposed Form CRS Release at 11.  
<sup>26</sup> See Proposed Form CRS Release at footnote 15.  
<sup>27</sup> See Proposed Form CRS Release at 18.  
<sup>28</sup> See Proposed Form CRS Release at footnote 40.  
<sup>29</sup> See Proposed Form CRS Release at 19.  
<sup>31</sup> See Proposed Form CRS Release at footnote 45.  
<sup>32</sup> See Proposed Form CRS Release at 59.  
<sup>32</sup> See Proposed Form CRS Release at footnote 134.



**American Council of Life Insurers**

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