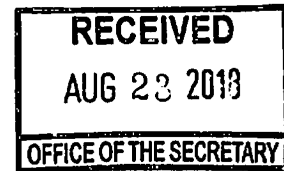


Brent J. Fields, Secretary
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, D.C. 20549-1090

August 6, 2018

Regarding File Number S7–07–18: Proposed Regulation Best Interest

Dear Mr. Fields and SEC Staff:

Ameriprise Financial's serial abuse of its customers provides a compelling case study of the investment advisory industry warranting strong actions by the Commission in its Proposed Interpretation Regarding Standard of Conduct for Investment Advisers and in its Proposed Regulation Best Interest. A few recent examples of financial depredations by one of the country's largest investment advisor and broker dealer organizations demonstrates excessive failures of fiduciary duty that current regulations did not prevent.

- On February 28, 2018, the SEC Ameriprise agreed to settle charges for recommending and selling higher-fee mutual fund shares to retail retirement account customers and for failing to provide sales charge waivers. According to the SEC's order, Ameriprise Financial Services Inc. disadvantaged certain retirement account customers by failing to ascertain their eligibility for less expensive mutual fund share classes.

  Ameriprise recommended and sold these customers more expensive mutual fund share classes when less expensive share classes were available. Ameriprise also failed to disclose that it would receive greater compensation from the purchases and that the purchases would negatively impact the overall return on the customers' investments.

  "Ameriprise generated greater revenue for itself but lower returns for its retirement account customers by recommending higher-fee share classes," said Anthony S. Kelly, Co-Chief of the SEC Enforcement Division's Asset Management Unit. "As evidenced by our recently announced Share Class Selection Disclosure Initiative, pursuing these types of actions remains a priority for the Division as we seek to get money back in the hands of harmed investors."

  Approximately 1,791 customer accounts paid a total of $1,778,592.31 in unnecessary up-front sales charges, contingent deferred sales charges, and higher ongoing fees and expenses because of Ameriprise's practices. In its litigation release[i] the Commission explained that Ameriprise customers did not have sufficient information

to understand that Ameriprise had a conflict of interest resulting from compensation it received for selling the more expensive share classes. The Commission emphasized that Ameriprise omitted material information concerning its compensation when it recommended the more expensive share classes to these Eligible Customers.

Ameriprise's knowing recommendation of higher fee mutual funds to advisory customers was not some innocent recent development. Both the SEC and FINRA have warned investors about these abuses for over a decade in SEC Investor Alerts and Bulletins[ii] and FINRA Investor Alerts[iii].

- In March 2015, Ameriprise settled a lawsuit[iv] for $27.5 million before trial on an action brought by a group of current and former employees of Ameriprise. The suit alleged that Ameriprise violated their fiduciary obligations as the sponsor of the 401(k) plan it offers to employees. The main issue is that Ameriprise offered several its proprietary mutual funds as options in the plan and that these proprietary funds were unreasonably expensive compared to other non-proprietary options that could have been utilized. Further the lawsuit alleged that these funds paid revenue sharing and other fees to Ameriprise and several of its subsidiaries.

- In 2011, Ameriprise Financial, the largest employer of certified financial planners in the United States, was sued by six people,[v] including one current employee, for stuffing its 401(k) plan with expensive, underperforming mutual funds that came from the company's own investment management arm. According to a news story, Ameriprise's menu of mutual funds splayed out in the litigation, complete with details on poor performance and a handy chart showing fees that are three to five times what they are at Vanguard. The story's[vi] author quite properly asked "if it turns out that Ameriprise didn't even get its own 401(k) right, why would you put your financial future in the company's hands?"

- In July 2009, the Commission took an enforcement action against Ameriprise for receiving millions of dollars in undisclosed compensation as a condition for offering and selling certain real estate investment trusts to its brokerage customers. Ameriprise agreed to pay $17.3 million to settle the SEC's charges. "Few things are more important to investors than getting unbiased advice from their financial advisers," said Robert Khuzami, Director of the SEC's Division of Enforcement. "Ameriprise customers were not informed about the incentives its brokers had to sell these investments." Ameriprise did not disclose to investors that additional payments were being made in connection with the sale of REIT shares, or the conflicts of interest these additional payments created. The SEC's order found that Ameriprise issued a variety of mislabeled invoices to the REITs as a means of

collecting the undisclosed revenue sharing payments that appeared to be legitimate reimbursements for services provided by Ameriprise.

- According to a news story[vii], Ameriprise Financial Services has long been accused of possessing a culture that's more concerned with sales commissions than compliance. The article notes that allegations against the company from the New Hampshire Bureau of Securities Regulation suggest that may still be very much the case. In July 2005, the firm paid $7.4 million to the New Hampshire Bureau of Securities for fines, penalties and restitution related to illegal incentives, conflicts of interest and lack of proper disclosure to its clients.

- FINRA fined Ameriprise Financial Services $12.3 million[viii] in connection with its receipt of directed brokerage in return for providing preferential treatment to certain mutual fund companies. The Securities and Exchange Commission (SEC) has also sanctioned the firm for related conduct.
  The action involves violations of FINRA's Anti-Reciprocal Rule, which prohibits firms from favoring the sale of shares of mutual funds based on brokerage commissions received by the firm. Among other things, the rule prohibits a firm from recommending funds or establishing preferred lists of funds in exchange for receipt of directed brokerage.

  The Anti-Reciprocal Rule is an important regulatory tool that is designed to ensure that firms recommend mutual funds on their merits and not because of the receipt of brokerage commissions, which are assets of the mutual fund shareholders and should not be used for marketing purposes.

  In this case, from January 2001 through December 2003, Ameriprise operated two shelf space (or revenue sharing) programs in which participating mutual fund companies paid a fee in return for preferential treatment by Ameriprise. That treatment included enhanced access to Ameriprise's sales force, including participation in conferences and meetings, distribution and display of marketing materials at Ameriprise branches, and in-office visits with Ameriprise registered representatives - all designed to increase sales of those mutual funds.

  In addition, Ameriprise promoted the funds on its internal website, identifying the mutual funds as "Preferred Providers," and posted sales literature for the funds as well as information about the funds and their fund managers. Ameriprise also charged its advisors reduced sales ticket charges for the sale of Preferred Provider funds. None of these benefits were available to non-participating mutual funds.

> While Ameriprise sold funds offered by approximately 32 fund companies during the period at issue, 24 were Preferred Providers.
>
> The mutual fund complexes that participated in these programs paid extra fees for the preferential treatment they received. Seven of the 24 fund complexes paid their fees *for* participating in the programs by directing approximately $41 million in mutual fund portfolio brokerage commissions to Ameriprise. The funds accomplished this by directing portfolio trades to the trading desks of clearing firms designated by Ameriprise, and the clearing firms then remitted a portion of the trading commissions - generally 75 to 86 percent - to Ameriprise, the designated "introducing broker."
>
> The commissions paid under these arrangements were sufficiently large to pay for the preferential treatment and other benefits received by the funds as ~~well as the~~ costs of trade execution. This use of directed brokerage allowed the fund complexes to use assets of the mutual funds instead of their own money to meet their revenue sharing obligations. The remaining fund complexes paid their fees for participating in the Preferred Provider program in cash to Ameriprise.

So, what is the point of highlighting these Ameriprise abuses in response to Commission's Request for Comment on Enhancing Investment Advisor and Broker Dealer Regulation? Simply this: if one of the largest, supposedly well-respected investment advisory firms demonstrated these profound abuses (and this is only a short recitation), then the current regulations are inadequate to protect consumers. Change is immediately necessary. Other similarly situated investment advisers, large and small, have likely committed analogous abuse of their customers under the current regulatory system. Consumers are gravely unprotected as these few Ameriprise examples demonstrate.

The Commission needs to act and quickly, in several areas where comment was invited:

1. Non-cash compensation standards should apply to all securities sales.

The proposal asks whether sales contests and trips should be banned as conflicts of interest. Under current FINRA standards, only mutual funds, variable insurance products, and direct participation programs have meaningful, comprehensive limits protecting consumers against conflicts due to sales contests, gifts and trips to lavish and exotic locations. Interestingly, FINRA invited its membership comment on whether these same prohibitions should be applied to all securities products in August 2016 (FINRA Regulatory Notice 16-29) that followed FINRA's December 2014 Retrospective Rule Review Report on Gifts, Gratuities and Non-Cash Compensation). FINRA stated its belief that "the general prohibitions regarding the payment or receipt of non-cash compensation should be extended beyond investment company securities, variable insurance contracts, DPPS and public offerings of

securities." This change would preclude abusive contests and non-cash compensation programs. So far, FINRA has not acted to adopt the rule proposal following its request for member commentary. The current rules for mutual funds, variable insurance products and DPPs work very well, and should be extended to all products. There is not good reason to limit these sensible rules to just these smaller product areas. Perhaps the large broker dealer firms stood in the way of this rule through the FINRA governance which they dominate. The Commission should instruct FINRA to adopt the proposed rule 3221 ASAP!

2. Minimum standards of education, experience, background and honesty must be established for registered investment advisors

Investment advisors should have minimum standards of education, experience, background, and honesty before they are licensed to offer investment advice. Currently, any one with any (or no) background, experience or education can register as an investment adviser. The public assumes if the Commission grants an investment adviser registration that the individual has the requisite expertise to provide financial advice. In actuality, investment advisors can and do provide advice based on unfounded theories, such as the cycle of the astrological chart. Other charlatans obtain phony (but impressive sounding) mail order investment advisor certificates. Commissioner Piwowar showed in his comments at the Commission meeting a picture of the flimsy investment advisor degree he obtained from a mail order certification organization that had no standards at all other than paying a fee. In the 1990s, an organization called the Financial Planner Registry maintained a public list of qualified financial planners and charged a fee to administer the registry. A journalist had an application for his dog "Fido" accepted in the registry, even after indicating the he was canine and had little human education.

It is flat wrong to continue to allow SEC registration of wholly incompetent people to dabble in consumers' most important financial assets. A basic understanding of financial, economic, and financial products is critically necessary for investment advisors to be authorized to direct customer's assets for investment. That is missing now. Broker dealers must be members of FINRA and must pass entry examinations and fulfill regular continuing education. The same should be required for investment advisers. The current system allows poorly educated "snake oil salesmen" to masquerade as government certified professionals. Even cosmetologists are required to demonstrate their proficiency, training and education before being licensed. Shouldn't at least the same be true for investment advisers?

In response to this problem, some organizations have voluntarily created standards of competence and ethical behavior, such as the CFP Board. Their standards are impressive, but toothless and potentially harmful to consumers. If a CFP certificate holder violates the organization's standards, they just get kicked out of the organization. There is no enforcement, no penalty. That is meaningless and provides no consumer protection. A better approach would be to delegate to FINRA the testing and examination authority

over investment advisers to insure compliance with the new Commission interpretations and regulatory requirements. A bill in congress a few years ago would have mandated this. The Commission should pursue statutory authority mandating FINRA testing, examination, continuing education, and prosecution pursuant to the investment advisor act rules and regulations.

3. The SEC should require Investment Advisors to regularly obtain continuing education.

Other professionals charged with important responsibilities, such as doctors, lawyers, teachers, and securities salespeople are required to obtain continuing education. There are no good reason investment advisers are not currently required to obtain continuing education as well. Continually changing financial products and rapidly changing laws are complex. Not requiring continuing education is wholly inexcusable and allows malpractice. A minimum of 25 hours per year of continuing education by approved training organizations must be required for investment advisers. FINRA could administer compliance with this important improvement in the delivery of qualified advice.

4. Investment Advisors should have significant net capital requirements.

It is preposterous that investment advisers do not have to maintain a safe margin of net capital like broker dealers. Had Madoff been subject to net capital standards, the damage he inflicted could have been limited. Instead, he and other investment advisory crooks have no financial brakes on committing fraud with customer assets. Reserving, margin, net capital, and leverage ratios are required by other financial regulators, and something like that should be imposed on investment advisors. Investment advisors should also have something like SIPC to protect consumers' assets under management when advisors go bankrupt.

5. Investment Advisors should be prohibited from identifying themselves as "registered investment advisors" and should be banned from using the initials "RIA" following their names and in their advertisements.

The Commission has wisely proposed limits on the use of the term advisor and adviser in its proposed regulation best interest because it conveys a misleading impression in the context of broker dealers. Similarly, investment advisers should be barred from calling themselves <u>registered</u> investment advisers or RIAs because that terminology grossly misleads consumers under the current regulatory standards to believe that the advisor did something more than just filling out the application and paying the registration fee. Until the Commission imposes minimum educational, experience and background standards, it is reckless and irresponsible to allow advisors to cloak themselves in the illusion that they have obtained some measure of government scrutiny preliminary to registration. Individuals using the initials RIA know exactly what they are doing: misleading consumers.

6. The Commission should codify its interpretative positions in formal rules.

The Commission has issued several important interpretive positions in its investment advisor pronouncements. They would have greater legal weight and validity if they were compiled into a formal rule under the investment advisers act.

7. The Commission should reconfirm that investment advisers must fulfill suitability standards when making recommendations to customers.

The Commission's proposal to codify the suitability obligation for investment advisers in a formal rule is very important and necessary. Investment advisory organizations promote that their fiduciary duty is vastly superior to broker dealers' suitability standard. In truth, the fiduciary duty is a hollow standard without any enforcement and no self-regulatory organization backing. The Dodd-Frank Act delegated to the states the responsibility to oversee most investment advisors except for very large advisors. Unfortunately, most states (except for large states like MA, NY, FL, CA, and IL) have tiny securities divisions with ever *shrinking* budgets. Consumers are likely less protected than when the Commission had authority over advisors because at least the SEC had the staff, expertise and inspection framework to properly regulate advisors. The current state system of regulation is a weak patch work quilt of varying standards, expertise and budgets. The Commission should raise investment advisor registration fees and impose annual fees on investment advisors to cover proper regulation and should require a self-regulatory organization membership to fully achieve consumer protection. FINRA could be drafted to perform SRO functions for investment advisors quite effectively, modeled on their broker dealer framework. Many investment advisors commit unpunished breaches of fiduciary duty every day when they stuff all their customers in annual assets under management fees when many customers do not need annual oversight from these individuals, but only need sporadic infrequent guidance that would be best funded by an hourly fee. Their retirement and savings nest eggs are corroded by annual investment adviser fees that greatly reduce net account performance. Likewise, investment advisers that have annual AUM fees allowing a percentage of assets under management should equally share in customers' losses by returning fees. Under current arrangements, these investment advisers gain when account values go up, but do not share equally in losses when values plunge. That should be corrected so that advisers have equitably balanced "skin in the game." To do otherwise is a breach of fiduciary duty.

8. Regulation Best Interest should be adopted as soon as possible

Many investment advisors often wear two hats simultaneously as broker dealers and investment advisers. Some of the Ameriprise abuse discussed in the beginning of this letter involved dual registered advisor-broker dealers. This situation accentuates the opportunity for noxious conflicts of interest and financial fraud. Regulation best interest would better protect consumers together with the proposed Form CRS. Both should be adopted ASAP to prevent abuse by largely unregulated investment advisors. The states and the Commission

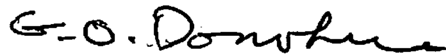
are inadequately equipped to comprehensively inspect and prosecute investment advisors committing fraud and cheating customers through conflicts of interest.

Conclusion.

The Commission has exercised commendable leadership in promulgating proposed rules, codification of interpretations about investment advisors, regulation best interest, and Form CRS. Consumer protection is greatly lacking, and large changes are badly needed to help Americans from being fleeced by investment advisors like the Ameriprise examples highlighted in the front of the letter.

Please act firmly and quickly. The public needs the Commission's commitment to consumer protection and more meaningful regulation as Americans try to achieve financial management and retirement security.

Thank you. Sincerely,



Gordon O. Donohue

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[i] https://www.sec.gov/litigation/admin/2018/33-10462.pdf

[ii] https://www.investor.gov/additional-resources/news-alerts/alerts-bulletins/investor-bulletin-mutual-fund-classes

[iii] https://www.finra.org/sites/default/files/InvestorDocument/p125866.pdf

[iv] https://thechicagofinancialplanner.com/the-ameriprise-401k-lawsuit/; http://www.marottaonmoney.com/ameriprise-sued-by-ameriprise-employees-over-excessive-401k-fees/

[v] https://www.nytimes.com/2011/10/15/your-money/turning-a-lens-on-ameriprise-financial.html

[vi] https://www.nytimes.com/2011/10/15/your-money/turning-a-lens-on-ameriprise-financial.html

[vii] https://www.wealthmanagement.com/regulation/ameriprise-branches-face-potential-fines-fake-financial-plans

[viii] http://www.finra.org/newsroom/2005/nasd-fines-ameriprise-financial-services-123-million-directed-brokerage-violations