

A photograph of a woman with dark hair pulled back, smiling warmly. She is wearing a white long-sleeved button-down shirt under a dark blue apron. Her arms are crossed over her chest. The background is a blurred indoor setting, possibly a kitchen or a retail store, with warm lighting.

# Office of the Investor Advocate

OFFICE OF THE INVESTOR ADVOCATE

# REPORT ON OBJECTIVES

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FISCAL YEAR 2019

Section 4(g) of the Securities Exchange Act of 1934 (Exchange Act), 15 U.S.C. § 78d(g), requires the Investor Advocate to file two reports per year with the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives.<sup>1</sup> A Report on Objectives is due no later than June 30 of each year, and its purpose is to set forth the objectives of the Investor Advocate for the following fiscal year.<sup>2</sup> The instant report contains a summary of the Investor Advocate's primary objectives for Fiscal Year 2019, beginning October 1, 2018.

A Report on Activities is due no later than December 31 of each year, and it describes the activities of the Investor Advocate during the preceding fiscal year.<sup>3</sup> For Fiscal Year 2019, the activities and accomplishments of the Office will be reported not later than December 31, 2019.


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**Disclaimer:** Pursuant to Section 4(g)(6)(B)(iii) of the Exchange Act, 15 U.S.C. § 78d(g)(6)(B)(iii), this Report is provided directly to Congress without any prior review or comment from the Commission, any Commissioner, any other officer or employee of the Commission, or the Office of Management and Budget. Thus, the Report expresses solely the views of the Investor Advocate. It does not necessarily reflect the views of the Commission, the Commissioners, or staff of the Commission, and the Commission disclaims responsibility for the Report and all analyses, findings, and conclusions contained herein.

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# MESSAGE FROM THE INVESTOR ADVOCATE

 n behalf of the Office of the Investor Advocate, I am pleased to submit this Report on Objectives for Fiscal Year 2019.

During Fiscal Year 2019, we expect to continue our work in several areas in which the Commission and self-regulatory organizations are engaged in multi-year rulemakings or reform initiatives. We will continue to monitor activities and make recommendations related to public company disclosure, equity market structure, fixed income market reform, and various initiatives involving accounting and auditing standards.

In addition, new priorities will require our attention in Fiscal Year 2019. Among other issues that undoubtedly will arise during the course of the year, we expect to examine the impact on investors resulting from proposed changes in the standards of conduct for broker-dealers, updates to the rules governing transfer agents and exchange-traded funds, and enhancements to the disclosures made by mutual funds and variable annuities. These topics are discussed in greater detail in this Report.

We are also examining issues that may require legislative intervention. For example, we are concerned about a recent Supreme Court case, *Kokesh v. SEC*, in which the Court held that the equitable remedy of disgorgement is a “penalty” that is subject to a five-year statute of limitations. As described in this Report, the decision may limit the SEC’s ability to return money to investors who were defrauded by someone who successfully concealed the wrongdoing. We are considering possible approaches to help restore or enhance the SEC’s ability to recover such losses and, in accordance with the statutory mandate of this Office, we may propose to Congress legislation that would be appropriate to promote the interests of investors.



Similarly, as described in the Ombudsman Report below, we are troubled by the declining level of legal assistance for investors of limited means, particularly seniors. To address this shortfall, the SEC's Investor Advisory Committee has recommended that the Commission and FINRA utilize money from fines and penalties to provide grants to law schools that establish or maintain investor advocacy clinics. We agree with this recommen-

dation and may propose or support legislation as needed to achieve this goal.

As always, I would welcome the opportunity to answer questions or provide additional information to Members of Congress. It is a privilege to serve in this role.

Sincerely,

A handwritten signature in black ink, appearing to read "Rick Fleming". The signature is fluid and cursive, with a large initial "R" and a long, sweeping tail.

Rick A. Fleming  
Investor Advocate

# OBJECTIVES OF THE INVESTOR ADVOCATE

**A**s set forth in Exchange Act Section 4(g)(4), 15 U.S.C. § 78d(g)(4), the Investor Advocate is required to perform the following functions:

- (A) assist retail investors in resolving significant problems such investors may have with the Commission or with self-regulatory organizations (SROs);
- (B) identify areas in which investors would benefit from changes in the regulations of the Commission or the rules of SROs;
- (C) identify problems that investors have with financial service providers and investment products;
- (D) analyze the potential impact on investors of proposed regulations of the Commission and rules of SROs; and
- (E) to the extent practicable, propose to the Commission changes in the regulations or orders of the Commission and to Congress any legislative, administrative, or personnel changes that may be appropriate to mitigate problems identified and to promote the interests of investors.

## Assisting Retail Investors

Exchange Act Section 4(g)(4)(A) directs the Investor Advocate to assist retail investors in resolving significant problems such investors may have with the Commission or with SROs.<sup>4</sup> To help accomplish that objective, the Investor Advocate has appointed an Ombudsman to, among other

things, act as a liaison between the Commission and any retail investor in resolving problems that retail investors may have with the Commission or with SROs.<sup>5</sup> As required by statute, a semi-annual report from the Ombudsman is included within this Report on Objectives.<sup>6</sup>

## Identifying Areas in Which Investors Would Benefit from Regulatory Changes

Exchange Act Section 4(g)(4)(B) requires the Investor Advocate to identify areas in which investors would benefit from changes in the regulations of the Commission or the rules of SROs.<sup>7</sup> This is a broad mandate that authorizes the Investor Advocate to examine the entire regulatory scheme, including existing rules and regulations, to identify those areas that could be improved for the benefit of investors. For example, the Investor Advocate may look at the rules and regulations governing existing equity market structure to determine whether any regulatory changes would benefit investors. These and similar other concerns are discussed in greater detail below in the section entitled *Policy Agenda for Fiscal Year 2019*.

## Identifying Problems with Financial Service Providers and Investment Products

Exchange Act Section 4(g)(4)(C) requires the Investor Advocate to identify problems that investors have with financial service providers and investment products.<sup>8</sup> The Investor Advocate continues to monitor investor inquiries and complaints, SEC and SRO staff reports, enforcement actions, and other data to determine





which financial service providers and investment products may be problematic. As required by Exchange Act Section 4(g)(6), these problems will be described in the Reports on Activities to be filed in December of each year.

### **Analyzing the Potential Impact on Investors of Proposed Rules and Regulations**

Exchange Act Section 4(g)(4)(D) directs the Investor Advocate to analyze the potential impact on investors of proposed regulations of the Commission and proposed rules of SROs.<sup>9</sup> As required, in Fiscal Year 2019 the Office will review all significant rulemakings of the Commission and SROs, and we will communicate with investors and their representatives to determine the potential impact of proposed rules. In addition, we will study investor behavior and utilize a variety of research methods to examine the efficacy of policy proposals.

### **Proposing Appropriate Changes to the Commission and to Congress**

Exchange Act Section 4(g)(4)(E) provides that, to the extent practicable, the Investor Advocate

may propose to the Commission changes in the regulations or orders of the Commission and to Congress any legislative, administrative, or personnel changes that may be appropriate to mitigate problems identified and to promote the interests of investors.<sup>10</sup> As we study the issues in our *Policy Agenda for Fiscal Year 2019*, as set forth below, we will likely make recommendations to the Commission and Congress for changes that will promote the interests of investors.

### **Supporting the Investor Advisory Committee**

Exchange Act Section 39 establishes the Investor Advisory Committee (IAC or Committee).<sup>11</sup> As discussed in greater detail below in the section entitled *Summary of IAC Recommendations and SEC Responses*, the purpose of the Committee is to advise and consult with the Commission on regulatory priorities, issues impacting investors, initiatives to protect investors, and related matters. The Investor Advocate is a member of the IAC,<sup>12</sup> and the Office will continue to provide staff and operational support to the IAC during Fiscal Year 2019.

# POLICY AGENDA FOR FISCAL YEAR 2019

**A**s described above, the statutory mandate for the Office of the Investor Advocate is broad, and much of our time is consumed with the review of rulemakings that flow through the Commission and SROs. We monitor all rulemakings, but we prioritize certain issues so that we can develop expertise in those areas and maximize our impact for investors with the resources we have available. After discussions with numerous knowledgeable parties, both inside and outside the Commission, and after due consideration, the Investor Advocate has determined that the Office will focus upon the following issues during Fiscal Year 2019:

- Public Company Disclosure
- Equity Market Structure
- Fixed Income Market Reform
- Accounting and Auditing
- Standards of Conduct for Broker-Dealers and Investment Advisers
- Exchange-Traded Funds
- Enhanced Disclosure for Mutual Funds and Variable Annuities
- Transfer Agents
- Impact of *Kokesh v. SEC* on Enforcement Actions

Although other issues may arise that will require the attention of the Office, the foregoing issues will remain on our policy agenda for FY 2019.

## PUBLIC COMPANY DISCLOSURE

Disclosure obligations are at the very core of the laws governing the offer and sale of securities in the United States. When investors have access to all material information about potential investment opportunities, they are better equipped to make informed choices and are more willing to participate in the capital markets.

Since our inception in 2014, the Office of the Investor Advocate has supported efforts to update and modernize the SEC's disclosure requirements, and we will continue this work in Fiscal Year 2019. In our view, efforts to make disclosure more effective can result in "win-wins," whereby investors receive higher-quality information at a lower cost to the companies that must provide the disclosure. We will look for these types of opportunities, while remaining vigilant to guard against the reduction of disclosures that are important to investors.

The Commission's Regulatory Flexibility Act Agenda<sup>13</sup> includes several rulemaking projects pertaining to public company reporting and capital raises. Some are mandated by the Fixing America's Surface Transportation Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act. Others represent a continuation of a years-long Disclosure Effectiveness initiative, which is a more comprehensive effort to review and



modernize public company reporting requirements. Additionally, Chairman Jay Clayton has announced a priority of looking for ways to make it more attractive for growing businesses to join the ranks of public companies.<sup>14</sup>

In a previous report, we described the phenomenon of fewer initial public offerings, a trend which has engendered a policy debate regarding causes and appropriate regulatory responses.<sup>15</sup> In general, we believe it is appropriate for the Commission to encourage businesses to go through the transformation from a private company to a public reporting company because it is a process that produces stronger companies that better serve the interests of investors, particularly Main Street investors.<sup>16</sup> Better disclosure also leads to better-informed valuations and greater capital market efficiency overall.

Early efforts to advance that goal appear to be centered on reducing compliance burdens, due to a concern that costs borne by public companies, ranging from direct compliance costs to the consumption of management and employee attention, exceed those for comparable private companies.<sup>17</sup> Because these compliance burdens often involve issues related to disclosure obligations, current proposals tend to concentrate on those obligations.

The rulemaking projects underway include, among others:

- Considering changes to the rules in Regulation S-X related to requirements for financial statements for acquired businesses;<sup>18</sup>
- Considering additional changes to the rules in Regulation S-X to eliminate provisions thought to be redundant, overlapping, outdated, or superseded in light of other changes to Commission disclosure requirements, U.S. Generally Accepted Accounting Principles (GAAP), International Financial Reporting Standards, or technology developments;<sup>19</sup>
- Considering amendments to Regulation S-K to change exhibit filing requirements and the related process for confidential treatment requests and also to allow for flexibility in discussing historical periods in the Management’s Discussion and Analysis section, among other miscellaneous updates;<sup>20</sup>
- Mandating the use of a newer filing format called Inline XBRL, which may enhance the quality and reliability of the financial statement data that filers submit;<sup>21</sup>
- Considering updates to certain industry-specific disclosure requirements, such as those pertaining to financial services companies’ lending activities and loan portfolios<sup>22</sup> and to mining companies’ mineral properties;<sup>23</sup>
- Amending the “smaller reporting company” definition, which would expand the number of issuers eligible to provide scaled-back disclosures;<sup>24</sup> and
- Considering amendments to extend the “test the waters” provision of the Jumpstart Our Business Startups Act to companies that are not emerging growth companies, which would make it easier to assess interest in a potential public offering.<sup>25</sup>

For our part, we will continue to engage in investor outreach and share feedback internally with our Commission colleagues who are contemplating these and other reforms. In our investor outreach, we have been meeting with mainly buy-and-hold equity and debt investors, including individual investors as well as institutional portfolio managers and analysts—in other words, individuals who consume the information that public companies are required to disclose. We have asked them to tell us about how they make investment and voting decisions, what information they rely on to make those decisions, and where they get it. This outreach provides additional context for the input that the Commission has received in thousands of comment letters on its rulemaking projects. We also intend to coordinate our work where possible with the Office of the Advocate for Small Business Capital Formation, a soon-to-be-formed office with

a mission that will focus on small businesses and small business investors.

While these types of disclosure-based initiatives, if properly implemented to maintain investor access to material information, may be helpful in encouraging more private companies to go public, we continue to believe that a holistic approach is needed to create a healthy ecosystem for small public companies. As we have stated previously, this approach should include efforts to improve the liquidity in smaller company shares and other reforms to enhance the market structure for equity securities.<sup>26</sup>

### **EQUITY MARKET STRUCTURE**

As noted in our prior Reports on Objectives, the secondary trading market for U.S.-listed equities is dispersed and complex, and the Commission has been engaged in a multi-year effort to improve the environment for modern trading.<sup>27</sup>

Three years ago, the Commission proposed amending Regulation ATS to enhance the operational transparency of alternative trading system (ATS) venues that trade listed equity securities.<sup>28</sup> Greater information about the operation of these venues could allow sophisticated investors to better compare the trading venues and determine which venues and order routing products meet their trading needs. In addition, in July 2016, the Commission proposed rules that, for the first time, would require broker-dealers to disclose the handling of institutional orders to customers under existing Rule 606 of Regulation NMS.<sup>29</sup> This could provide certain customers with better information to evaluate the quality of execution for the orders they place with their brokers.

As required by our statutory mandate, our Office has evaluated the potential impact of these proposals on investors. We have encouraged the Commission to adopt the proposed changes to Rule 606 and, in September 2016, we submitted a comment letter to the Commission in support of the proposed amendments to Regulation ATS.<sup>30</sup>

In our letter, we suggested a modest expansion of certain aspects of the proposal in order to enhance the operational transparency of venues that trade fixed-income securities, including those that solely trade government securities.<sup>31</sup> We are pleased that the Chairman has indicated these two rules should be finalized soon, and we will continue to engage with the Commissioners and staff during that process.<sup>32</sup>

In addition to these rulemakings, in March 2018, the Commission proposed a rule to conduct a transaction fee pilot for NMS stocks.<sup>33</sup> The proposed rule would subject the stock exchanges to new temporary pricing restrictions across three test groups and thereby reduce or eliminate the use of so-called “maker-taker” fee-and-rebate pricing for transactions in those securities. In addition, the rule would require the exchanges to prepare and publicly post data.<sup>34</sup>

Originating with electronic trading venues in the late 1990s, early alternatives to registered exchanges competed by, among other things, charging low fees while offering fast and fully automated trading.<sup>35</sup> In response, exchanges began paying rebates for trading on their venues, which provided an additional incentive for traders to use a particular venue because it generated additional income beyond the spread between the bid and offer prices.<sup>36</sup> In part enshrined by Rule 610 of Regulation NMS, which sets a maximum access fee cap for “takers” on equity exchanges, this maker-taker fee model has been the subject of debate over the effects it may have on market structure, broker routing practices, and investor interests.<sup>37</sup> Some believe the maker-taker model is a competitive tool for exchanges and may, directly or indirectly, provide better prices for investors. Others believe that it exacerbates conflicts of interest for brokers who have a legal duty to seek best execution of their customers’ orders, contributes to market fragmentation and market complexity through the proliferation of new exchange order types, and undermines price transparency.<sup>38</sup>

Following the Commission's Equity Market Structure Advisory Committee's recommendation that the Commission establish a pilot program of this nature,<sup>39</sup> our Office encouraged the Commission to formally propose such a pilot. In Fiscal Year 2019, we will carefully consider whether the proposed elements of the pilot will provide the Commission with the most useful data for evaluating potential equity market structure reforms. Ultimately, we will consider whether lowering these fees and rebates on a permanent basis will improve market quality for investors.

On April 23, 2018, the Division of Trading and Markets held an equity market structure roundtable discussion on liquidity in thinly-traded equity securities.<sup>40</sup> The discussion indicated that the Commission should continue to consider whether market structure changes could improve the liquidity in these small- and mid-cap stocks.<sup>41</sup> Although it was clear from the discussion that investors would benefit from improved liquidity in existing public companies, there was less agreement as to whether alternative market structures could attract additional companies to become publicly listed.

Following the roundtable, NASDAQ submitted a request for the Commission to suspend unlisted trading privileges during a one year pilot period for smaller companies with less than \$2 billion in market capitalization and fewer than 100,000 shares trading on an average day.<sup>42</sup> In effect, this would prevent other exchanges from trading this set of Nasdaq-listed securities. NASDAQ suggests that consolidating liquidity for smaller companies would promote economic and pricing efficiency and improve market quality, and could incentivize additional smaller companies to list on public markets.<sup>43</sup>

The Commission intends to hold two additional roundtables in the near future—one on participant access to markets and market data and another on regulatory approaches to addressing retail fraud.

We intend to consider the discussions around these important issues with an eye towards helping the Commission identify actionable recommendations that will benefit smaller public companies and their investors.

In addition to monitoring and evaluating rulemaking by the Commission during FY 2019, we will continue to examine the hundreds of rule proposals that are filed with the Commission by the SROs. Typically, a number of these filings involve market structure issues that impact investors. For example, IEX has recently proposed certain long-term listing standards,<sup>44</sup> and CBOE has proposed a secondary closing auction for NYSE and NASDAQ listed securities.<sup>45</sup> Where appropriate, we will make formal recommendations or utilize the comment process to ensure that the needs of investors are properly considered by the SROs and the Commission.

### **FIXED INCOME MARKET REFORM**

Since our inception, the Office of the Investor Advocate has included municipal market reform on its policy agenda each fiscal year.<sup>46</sup> During this time, significant and important reforms took place in the municipal securities market, including implementation of a best-execution rule, adoption of rules and guidance relating to mark-up disclosure and prevailing market price, and enhancements to the Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Market Access (EMMA) website.<sup>47</sup> During Fiscal Year 2019, we will continue to monitor the important work of the MSRB and SEC in overseeing the municipal securities markets, but we will also broaden our focus to fixed income market reform more generally.

Fixed income markets are typically segmented by sector according to the category of issuer such as corporate securities, mortgage related securities, asset-backed securities, federal agency securities, treasury securities, money market securities, and municipal securities.<sup>48</sup> As of the end of 2017, the value of outstanding debt securities in the U.S. was

approximately \$40.7 trillion, including nearly \$8.5 trillion of corporate securities,<sup>49</sup> \$9.3 trillion of mortgage related securities, \$1.5 trillion of asset-backed securities, \$2 trillion of federal agency securities, \$14.5 trillion of treasury securities, \$1 trillion of money market securities, and \$3.9 trillion of municipal market securities.<sup>50</sup> In Fiscal Year 2019, the Office will monitor these sectors of the fixed income market for issues that may directly or indirectly impact retail investors.

Holdings of fixed income securities typically include both individual and institutional investors.<sup>51</sup> Certain segments of the fixed income market have high rates of participation by individual investors, while others have higher participation by institutional investors.<sup>52</sup> Corporate and municipal securities, in particular, may be an important part of individual investors' investment and retirement strategies because they may produce regular income.<sup>53</sup>

In remarks at the Third Annual Conference on the Evolving Structure of the U.S. Treasury Market, SEC Chairman Jay Clayton stated, “[i]ndividual investors are key participants in the corporate and municipal debt markets, both directly as retail investors and indirectly through investment funds, such as pension funds and other pooled vehicles, including as insurance owners and beneficiaries.”<sup>54</sup> Recognizing the importance of these markets to retail investors, American companies, and the nation’s infrastructure, the Commission announced the formation of a Fixed Income Market Structure Advisory Committee (FIMSAC) on November 9, 2017.<sup>55</sup> This Committee, whose initial focus is on corporate bonds and municipal securities markets, will provide “advice to the Commission on the efficiency and resiliency of these markets and identify opportunities for regulatory improvements.”<sup>56</sup> Chairman Clayton has asked the Committee to help the Commission ensure that its regulatory approach reflects the realities of the current market and the needs of Main Street investors, as well as companies and state and local governments.<sup>57</sup>

FIMSAC held its inaugural meeting on January 11, 2018.<sup>58</sup> During this meeting, FIMSAC focused much of its time on bond market liquidity.<sup>59</sup> On April 9, 2018, FIMSAC held its second public meeting and discussed liquidity considerations for bond ETFs, retail investor disclosure and education, electronic trading in the retail market,<sup>60</sup> and block trade dissemination in municipal securities and corporate bonds.<sup>61</sup> Following this discussion, FIMSAC adopted a recommendation for a pilot program to study market implications of changing the reporting regime for block-size trades in corporate bonds by introducing a delay for larger trades.<sup>62</sup> In Fiscal Year 2019, the Office of the Investor Advocate will monitor the discussions and recommendations of FIMSAC.

Additionally, throughout Fiscal Year 2019, the Office will monitor, analyze, and review relevant Commission and SRO rulemakings and other activities relating to fixed income markets—with particular attention to amendments and rules impacting individual investors in municipal securities and corporate bond markets. For example, the Office will monitor attempts to deter abusive market practices that may present risk to investors, such as so-called “last look” or “pennying,” and the practice of “filtering” or “screening.”<sup>63</sup> During its quarterly meeting on April 25–26, 2018, the MSRB Board agreed to seek public comment on draft interpretive guidance for dealers that would clarify existing regulations on the practice of “pennying.”<sup>64</sup> As appropriate, the Office may provide public comment relating to this or other potentially problematic products or practices within the fixed income space.

## ACCOUNTING AND AUDITING

In a recent speech, SEC Chief Accountant Wesley Bricker emphasized the importance of maintaining the highest standards of general purpose financial reporting:

When formulating standards for general purpose financial reporting, the [Financial

Accounting Standards Board] (and the [International Accounting Standards Board]) do not seek to influence the outcome of investor capital allocation decisions or actions taken by management; rather, the boards design standards that provide better information to inform those decisions and actions. The alternative, whereby standards are designed to privilege certain special purpose objectives, economic activities, financial products, or market participants, could diminish confidence in the accuracy or quality of reported information, which could thereby impair capital formation, and in turn negatively impact economic activity.<sup>65</sup>

We concur. High-quality financial reporting is essential to investors in their investment and voting decisions. It is therefore important for the Office of the Investor Advocate to track accounting and auditing issues, to represent investors in the policymaking process, and to encourage investors themselves to express their views. As in past years, we will continue to follow developments at the Commission as well as the Financial Accounting Standards Board (FASB) and the Public Company Accounting Oversight Board (PCAOB).

At FASB, work is underway to facilitate successful implementation of the new credit loss standard (Current Expected Credit Losses or CECL), which the accounting standard-setter adopted in 2016 after a six-year, inclusive process.<sup>66</sup> FASB's Transition Resource Group<sup>67</sup> has been engaging with all stakeholders on implementation on the new standard, which will take effect in 2020.<sup>68</sup> The new standard is important to investors because it is expected to result in timelier reporting of credit losses and reduction of the information asymmetry between company management and investors.<sup>69</sup>

At the PCAOB, five new members have been appointed to the Board,<sup>70</sup> and it has announced that it is taking a fresh look at the organization and

its future direction. In preparing a new five-year strategic plan, the PCAOB has issued a survey to obtain the views of external parties, such as investors, auditors, preparers, audit committee members, and academics. We will engage with the PCAOB as it develops its new strategic plan, and we will monitor its implementation.

In international markets, we will pay attention to developments in international financial reporting standards (IFRS) and international auditing standards. These standards are important to U.S. investors because, as of the end of 2016, U.S. investors had invested \$9.9 trillion in equity and debt securities listed in non-U.S. jurisdictions.<sup>71</sup> Moreover, since 2007, the Commission has allowed foreign private issuers to report under IFRS without reconciling to U.S. GAAP.<sup>72</sup>

We were pleased to see the appointment in May 2018 of SEC Chief Accountant Wesley Bricker as a representative of the International Organization of Securities Commissions (IOSCO) to the Monitoring Group. As its name implies, the Monitoring Group is responsible for monitoring the overall governance of the international audit-related standard-setting process.

The question of an expectations gap regarding audits, though not new, has become a prominent theme recently in both the U.S. and the U.K. An expectations gap is the difference between what investors expect from the financial statements and independent audit, on the one hand, and what they actually communicate to investors. In June, Mr. Bricker discussed this topic within a speech he presented in London,<sup>73</sup> and the issue was raised at a June meeting of the PCAOB's Standing Advisory Group in the context of the new auditor reporting standard and its requirement to communicate critical audit matters (CAMS).<sup>74</sup> The topic of an expectations gap also has appeared recently in the press, including an article in the *Economist* under the title "Company audits: Great expectations gap."<sup>75</sup> In the coming fiscal year, we will pay

close attention to this issue, focusing on causes and potential solutions to narrow or close the expectation gap in ways that best protect investors.

### STANDARDS OF CONDUCT FOR BROKER-DEALERS AND INVESTMENT ADVISERS

On April 18, 2018, the Commission voted to propose a package of rulemakings and interpretations intended to improve the quality and transparency of relationships that retail investors have with investment advisers and broker-dealers while preserving access to different types of advice relationships and investment products.<sup>76</sup> Specifically, the regulatory package includes the following proposals: (1) a new rule called “Regulation Best Interest”; (2) an interpretation reaffirming and, in some cases, clarifying the Commission’s view of the fiduciary duty that investment advisers owe to their clients; and (3) a new short-form disclosure document called a customer or client relationship summary, as well as a restriction on the use of the terms “adviser” or “advisor” by certain broker-dealers and their associated persons as part of their firm names or professional titles.<sup>77</sup>

Proposed Regulation Best Interest would require a broker-dealer to act in the best interest of a retail customer when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer, without putting the financial or other interest of the broker-dealer ahead of the interests of the retail customer.<sup>78</sup> Under proposed Regulation Best Interest, a broker-dealer would discharge this duty by complying with each of the following three specific obligations.

- Disclosure obligation, which would require the broker-dealer to disclose to the retail customer the key facts about the relationship, including material conflicts of interest.
- Care obligation, which would require the broker-dealer, in making a recommendation, to exercise reasonable diligence, care, skill, and



prudence, to (i) understand the potential risks and rewards associated with the recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers; (ii) have a reasonable basis to believe that the recommendation is in the retail customer’s best interest; and (iii) have a reasonable basis to believe that a series of recommended transactions is not excessive and is in the retail customer’s best interest.

- Conflict of interest obligation, which would require the broker-dealer to establish, maintain, and enforce policies and procedures reasonably designed to identify and then, at a minimum, to disclose and mitigate (or eliminate), material conflicts of interest arising from financial incentives; and to at least disclose other material conflicts of interest.<sup>79</sup>

The proposed investment adviser interpretation would reaffirm and clarify certain aspects of the fiduciary duty that an investment adviser owes to its clients.<sup>80</sup> The aim of the proposed interpretation is to provide greater clarity to investment advisers and their clients regarding advisers’ legal obligations toward their clients.<sup>81</sup>



The proposed short-form disclosure document known as the customer or client relationship summary—Form CRS—would be a standardized disclosure of no more than four pages that would highlight key differences in the principal types of services offered by an investment adviser or broker-dealer, the legal standards of conduct that apply to each, the fees a client or customer might pay, and certain conflicts of interest that may exist.<sup>82</sup> This proposed rule, if adopted, would require investment advisers and broker-dealers, and their respective associated persons, to provide retail investors with a relationship summary.<sup>83</sup> Proposed Form CRS is intended to furnish retail investors with simple, easy-to-understand information about the nature of their relationship with their investment professional and would supplement other more detailed disclosures.<sup>84</sup>

The proposed restriction on certain broker-dealers and their associated persons from using the terms “adviser” or “advisor” as part of their name or title in communications with investors and prospective investors is meant to allay investor confusion regarding investment professionals’ registration status.<sup>85</sup> The new rule would require investment advisers and broker-dealers and their associated persons to be direct and clear about their registration status in communications with investors and prospective investors.

We are encouraged that the Commission has determined to address these long-standing issues, and we appreciate the willingness of Commissioners and staff to engage in active dialogue with us as the proposals were being developed. Nonetheless, while the resulting proposed rulemakings and interpretations reflect some of our views, they do not necessarily represent our strongest policy preferences. For instance, in addition to mitigating conflicts arising from financial incentives, we think that broker-dealers should be required to mitigate—not merely disclose—material conflicts involving situations in which the broker-dealer

cannot form a reasonable basis for believing that disclosure effectively addresses those conflicts. We also believe that the prohibition on labeling should not be limited to use of the terms “adviser” or “advisor,” but should instead be a principles-based restriction on the use of any label that would connote an ongoing relationship of trust with an investor. These are just two examples of the myriad issues that we are considering in connection with the proposed rulemakings. As this rulemaking process unfolds, we will continue to analyze developments in this area and promote the interests of retail investors at every opportunity.

On a separate but parallel track, we have been conducting investor testing generally on the nature of advice relationships.<sup>86</sup> For example, we have been researching, among other things, whether investors understand the distinctions among different types of investment professionals, how effectively investors navigate the market for financial advice, investor perceptions of financial conflicts of interest, and the types of conduct investors expect from an investment professional who is required to act in an investor’s best interest. We will also explore, through controlled experiments, the optimal length and content of the proposed Form CRS, as well as alternative disclosure methods such as video and web-based delivery. We hope to use the information obtained from our research efforts to help augment the Commission’s data-driven policymaking approach.

## EXCHANGE-TRADED FUNDS

Since the Commission approved the first exchange-traded fund (ETF) in 1992, the U.S. ETF market has grown to \$3.4 trillion in total net assets—and approximately 1,832 funds—at year-end 2017.<sup>87</sup> Currently, ETFs rely on exemptive orders from the Commission, which permit the funds to operate as investment companies under the Investment Company Act (subject to representations and conditions that have developed over time).

Because the Commission has granted more than 300 of these exemptive orders in the past quarter century, differences in representations and conditions have resulted, which has led to some variations in the regulatory structure for existing ETFs.<sup>88</sup> To address these and related issues, the Commission has determined to modernize the regulatory framework for ETFs to reflect its 26 years of experience in regulating these products. The objective is to create a consistent, transparent, and efficient regulatory framework for ETFs and to facilitate greater competition and innovation in the ETF space.

We support the Commission's efforts to permit ETFs that satisfy certain conditions to operate without the expense and delay of obtaining an exemptive order insofar as such efforts do not sacrifice investor protection. However, while we favor rulemaking that would cover "plain vanilla" ETFs and would promote full daily portfolio transparency and broad disclosure (e.g., historical information on premiums and discounts, bid-ask spread information), among other things, we will be taking a closer look at the treatment of leveraged and inverse ETFs and some of the more complex and less transparent products that have sought or obtained exemptive relief.

### **ENHANCED DISCLOSURE FOR FUNDS AND VARIABLE ANNUITIES**

On June 4, 2018, the Commission issued a request for comment to elicit the views of retail investors with respect to mutual funds, ETFs, and other pooled investment vehicles.<sup>89</sup> The purpose of the request for comment is to help the Commission learn how individual investors and other interested parties use disclosures by funds and how investors believe those disclosures could be improved to help investors make informed investment decisions. This would include investor feedback on the delivery, design, and content of fund disclosures.

Fund disclosures are important because millions of individuals invest in funds as a means of achieving their financial goals, such as saving for retirement

and funding their children's educations.<sup>90</sup> Indeed, an estimated 100 million Americans representing approximately 56.2 million households owned mutual funds as of mid-2017.<sup>91</sup> Given this level of investor participation in funds, it makes sense for the Commission to seek the input of Main Street investors on how they use, and how to improve, fund disclosures.

The Office of the Investor Advocate is heavily involved in efforts to understand investor behavior. As reported previously, in 2017 we launched an investor research and testing effort to examine potential ways to improve fund fee and expense disclosure. This investor testing research project, which is part of a larger testing initiative known as Policy Oriented Stakeholder and Investor Testing for Innovative and Effective Regulation (POSITIER) that encompasses several research streams, seeks to inform the rulemaking process with evidence obtained from surveys and other research methods. The fund fee and expense disclosure research stream explores, for example, topics such as the effectiveness of dollar-denominated fee and expense disclosure as compared to disclosure expressed in percentage terms, the utility of standardized cost disclosure generally, and ways to provide further context for the disclosure. This research effort is ongoing.

Our interest and involvement in fund disclosure extends to separate accounts that offer variable annuities.<sup>92</sup> Indeed, we have consistently advocated for enhanced disclosure concerning separate accounts that offer variable annuities. For example, three years ago, in our *Report on Objectives, Fiscal Year 2016* (published in June 2015), we indicated our strong support for "staff's efforts to address the problem of lengthy and complex disclosure" for variable annuities.<sup>93</sup> We continue to support the development of a summary prospectus for variable annuities that would disclose the key facts that investors need to know about the risks and costs, as well as the benefits, of their investment.<sup>94</sup>

According to the Commission’s agenda that was developed in accordance with the Regulatory Flexibility Act, Commission staff is considering such enhanced disclosure for separate accounts registered as unit investment trusts and offering variable annuities.<sup>95</sup> We remain convinced that the mutual fund summary prospectus could serve as a useful model for providing variable annuity disclosure,<sup>96</sup> and there appears to be support for this idea within the Commission. On March 19, 2018, for example, Commissioner Hester Peirce stated that the “Commission got off to a good start on revamping fund disclosures with its adoption of the mutual fund summary prospectus” and that a “similar variable annuity summary prospectus would be a valuable project.”<sup>97</sup> We look forward to working with Commission staff as they develop a proposal for enhanced disclosure for separate accounts registered as unit investment trusts and offering variable annuities.

## TRANSFER AGENTS

In recent years, Commission enforcement actions have focused on gatekeepers,<sup>98</sup> including cases against auditors, transfer agents, and attorneys. Transfer agents, in particular, play a critical role with respect to securities settlement. Transfer agents issue and cancel stock certificates to reflect changes in ownership, act as an intermediary for the company, and handle lost, destroyed, or stolen certificates, among other key functions.<sup>99</sup> Additionally, transfer agents play an important role in monitoring the restrictive legends and “stop transfer” orders that distinguish restricted securities from freely-tradable securities.<sup>100</sup> The failure of a transfer agent to promptly, accurately, and safely perform its duties can, among other things, hinder the successful completion of secondary trades, disenfranchise investors, and expose issuers, investors, securities intermediaries, and the securities markets as a whole to significant financial loss.<sup>101</sup>

Restricted securities are securities acquired in an unregistered, private sale from the issuing company or from an affiliate of the issuer.<sup>102</sup> Typically,

restricted securities bear a legend indicating that they cannot be resold legally unless there is an effective registration statement for their resale or there is an available exemption from registration for the resale.<sup>103</sup> Often, transfer agents are the party responsible for affixing, tracking, and removing restrictive legends from a security.<sup>104</sup>

Distribution of unregistered securities is particularly problematic in the microcap market,<sup>105</sup> where there may be limited publicly available information and increased risk for fraud.<sup>106</sup> Often, less sophisticated investors may be the victims of microcap fraud.<sup>107</sup> Given their responsibilities, transfer agents are well positioned to play important gatekeeper functions<sup>108</sup> in that they can potentially detect and prevent frauds involving unregistered microcap securities.<sup>109</sup>

The Commission first adopted transfer agent rules in 1977<sup>110</sup> and has rarely updated the rules since that time.<sup>111</sup> Transfer agents now perform a more diverse array of services and operate in a market structure that has changed significantly since 1977.<sup>112</sup> Recognizing the increasingly critical role of transfer agents and changing landscape, in December 2015, the Commission issued an advanced notice of rulemaking, together with a concept release requesting public comment on the Commission’s broader review of transfer agent regulation.<sup>113</sup> The concept release highlighted, among other things, a transfer agent’s particular role with respect to the issuance and transfer of restricted securities and removal of restrictive legends.<sup>114</sup> Modernization of transfer agent rules and more specificity around transfer agents’ responsibilities with respect to restricted securities could enhance investor protection and combat fraud and manipulation in the microcap market.<sup>115</sup>

In the coming fiscal year, we will examine issues relating to transfer agents, transfer agent rules, and the critical role transfer agents play as gatekeepers. We will consider whether proposed changes and modernization to transfer agent regulations are appropriate and would benefit the retail investor.

Based upon our findings, we will advocate for reforms as needed.

### IMPACT OF *KOKESH V. SEC* ON ENFORCEMENT ACTIONS

On June 5, 2017, the Supreme Court unanimously held that 28 U.S.C. § 2462,<sup>116</sup> which establishes a five-year statute of limitations period for “an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture,” bars the Commission from obtaining disgorgement in actions brought beyond the five-year statute of limitations.<sup>117</sup> The Court’s June 2017 holding in *Kokesh v. SEC* expanded on its 2013 ruling in *Gabelli v. SEC*, wherein the Supreme Court held that the Commission must bring enforcement actions seeking civil money penalties within five years of when the conduct occurred.<sup>118</sup>

In 2009, the Commission brought an action against Charles Kokesh alleging that he violated various securities laws by concealing the misappropriation of \$34.9 million from four business development companies from 1995 to 2009.<sup>119</sup> The Commission sought monetary civil penalties, disgorgement, and an injunction barring Mr. Kokesh from future violations.<sup>120</sup> Mr. Kokesh was found liable for various securities laws violations at a jury trial.<sup>121</sup> The District Court determined that with respect to the civil monetary penalties, 28 U.S.C. § 2462’s five-year statute of limitations precluded any penalties for misappropriation that occurred prior to the filing of the Commission’s complaint.<sup>122</sup> The District Court agreed with the Commission, however, that because disgorgement is not a “penalty” within the meaning of 28 U.S.C. § 2462, no limitation period applied to disgorgement.<sup>123</sup> Thereafter, the Court of Appeals for the Tenth Circuit affirmed, agreeing that disgorgement is not a penalty, and further finding that disgorgement is not a forfeiture.<sup>124</sup>

Following a circuit split<sup>125</sup> over whether 28 U.S.C. § 2462 applies to claims for disgorgement in SEC enforcement actions, the Supreme Court

granted certiorari to resolve the disagreement.<sup>126</sup> The Supreme Court unanimously held that disgorgement, as it is applied in SEC enforcement proceedings, operates as a penalty under 28 U.S.C. § 2462. Accordingly, any claim for disgorgement in an SEC enforcement action must be commenced within five years of the date the claim accrued.<sup>127</sup>

The *Kokesh* holding may have a far-reaching impact on SEC enforcement actions and the Commission’s ability to recover funds stolen from investors.<sup>128</sup> On May 16, 2018, the co-directors of the SEC’s Division of Enforcement, Stephanie Avakian and Steven Peikin (the Directors), testified before the House Committee on Financial Services, Subcommittee on Capital Markets, Securities, and Investment.<sup>129</sup> The Directors testified that the *Kokesh* decision already has had significant impact across many parts of the Division<sup>130</sup> because many securities frauds are complex and take significant time to uncover and investigate.<sup>131</sup> Moreover, some fraud schemes are well concealed and are not discovered until investors have been victimized over many years.<sup>132</sup> In such cases, *Kokesh* may severely limit the recovery available to harmed investors.<sup>133</sup> The Directors further expressed concern with “an outcome where some investors must shoulder additional losses—and the fraudulent actor is able to keep those ill-gotten gains—because those investors were tricked early in a scheme rather than later.”<sup>134</sup>

The overall impact of *Kokesh* remains to be seen. However, in the wake of *Kokesh*, the Division will need to work to bring cases as quickly as possible to have the best chance at recovery for harmed investors.<sup>135</sup> Moreover, as the Directors testified, some of the effects of *Kokesh* have already become clear. For example, in the *Kokesh* case alone, Mr. Kokesh kept more than 80 percent of the approximately \$35 million he fraudulently obtained from his firm’s advisory clients.<sup>136</sup> Due to the Court’s ruling, the harmed investors will not recover any of those funds.<sup>137</sup> In the year since the *Kokesh* decision, the Division of Enforcement has



had to forego over \$800 million of disgorgement in both litigated and settled actions.<sup>138</sup>

Shortly after the Court's ruling, former SEC Chair Mary Jo White and former SEC enforcement officials described the potential impacts of the *Kokesh* ruling on SEC enforcement actions.<sup>139</sup> According to those commentators, the decision could result in, among other things, reduced leverage for the SEC in settlement negotiations, fewer investigations involving aged conduct, earlier (and potentially less successful) staff requests for tolling agreements, and cascading effects on other sanctions such as injunctive relief or bars from serving as an officer or director.<sup>140</sup>

In our view, the Supreme Court's *Kokesh* holding has had, and will continue to have, troubling impacts on retail investors. The decision limits the Commission's ability to recover funds on behalf of harmed investors and potentially threatens the Commission's ability to protect investors through other sanctions. As Director Peikin testified, the Division of Enforcement is interested in working with legislators to fashion a proposal to address the impacts of *Kokesh*, or alternatively, to respond to any legislation that may come forward.<sup>141</sup> During FY 2019, the Office will work with the Division of Enforcement and others to explore possible solutions to the *Kokesh* decision.



# OMBUDSMAN'S REPORT

**A**s set forth in Exchange Act Section 4(g)(8), 15 U.S.C. § 78d(g)(8), the Ombudsman is required to: (i) act as a liaison between the Commission and any retail investor in resolving problems that retail investors may have with the Commission or with self-regulatory organizations (SROs); (ii) review and make recommendations regarding policies and procedures to encourage persons to present questions to the Investor Advocate regarding compliance with the securities laws; and (iii) establish safeguards to maintain the confidentiality of communications between investors and the Ombudsman.<sup>142</sup>

The Ombudsman is also required to “submit a semi-annual report to the Investor Advocate that describes the activities and evaluates the effectiveness of the Ombudsman during the preceding year” (Ombudsman’s Report).<sup>143</sup> The Ombudsman’s Report must be included in the semi-annual reports submitted by the Investor Advocate to Congress. To maintain reporting continuity, the Ombudsman’s Report included in the Investor Advocate’s June 30 Report on Objectives will describe the Ombudsman’s activities during the first six months of the current fiscal year and provide the Ombudsman objectives and outlook for the following full fiscal year. The Ombudsman’s Report included in the Investor Advocate’s December 31 Report on Activities will provide a look back on the Ombudsman’s activities during the full preceding fiscal year.

Accordingly, this report provides a look back on the Ombudsman’s activities for the six-month period of October 1, 2017, through March 31, 2018 (Reporting Period) and discusses the Ombudsman’s objectives and outlook for Fiscal Year 2019, beginning October 1, 2018.

## SERVICE BY THE NUMBERS

The Ombudsman<sup>144</sup> assists retail investors—sometimes referred to as individual investors or Main Street investors—and other persons with concerns or complaints about the SEC or SROs the SEC oversees. The assistance the Ombudsman provides includes, but is not limited to:



- listening to inquiries, concerns, complaints, and related issues;
- helping persons explore available SEC options and resources;
- clarifying certain SEC decisions, policies, and practices;
- taking objective measures to informally resolve matters that fall outside of the established resolution channels and procedures at the SEC; and
- acting as an alternate channel of communication between retail investors and the SEC.



In practice, individuals often seek the Ombudsman’s assistance as an initial point of contact to resolve their inquiries or as a subsequent or ongoing point of contact when they are dissatisfied with the outcome, rate of progress, or resolution. At times, individuals request the Ombudsman’s assistance with things the Ombudsman is not permitted to do. For example, they may expect the Ombudsman to participate in a formal investigation, play a role in a formal resolution process, or overturn a decision of a fact-finder or appellate body.

The Ombudsman maintains inquiry data records to: (i) identify and respond to problems raised by retail investors and others; (ii) track and analyze inquiry volume; (iii) categorize and report data, trends, and concerns; and (iv) provide data-driven support for recommendations presented by the Ombudsman to the Investor Advocate for review and consideration.

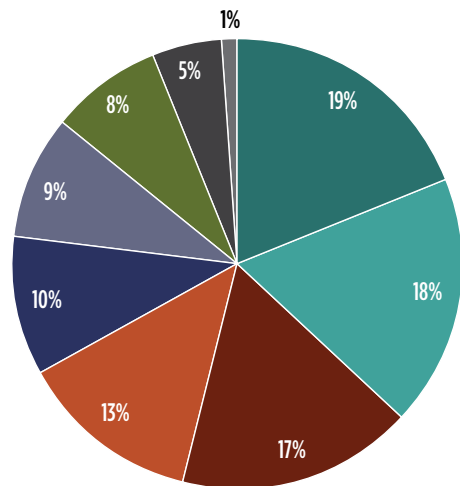
Inquiry volume is counted in terms of matters and contacts. The initial contact—a new, discrete inquiry received by or referred to the Ombudsman—is the contact that establishes the matter. When a matter is established, the Ombudsman reviews the facts, circumstances, and concerns raised, and assesses the staff engagement and resources that may be required to respond to, refer, or resolve the matter.

The matter established by the initial contact may generate subsequent contacts—related inquiries and communications to or from the Ombudsman staff deriving from the matter. Subsequent contacts often require further staff attention to answer additional questions, explain or clarify proposed resolution options, or respond to challenging or persistent communications from an investor. This system of counting matters and contacts helps the Ombudsman quickly assess volume and resource issues related to each matter.

### Data Across Primary Issue Categories

During the Reporting Period, retail investors, industry professionals, concerned citizens, and other interested persons contacted the Ombudsman for assistance on 102 new matters covering nine primary issue categories.

**Matters by Primary Issue Category**  
October 1, 2017–March 31, 2018

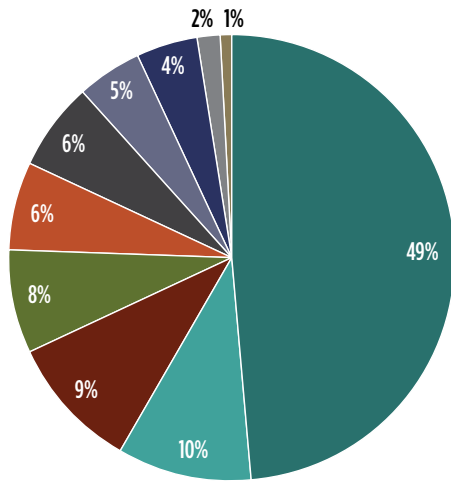


- Non-SEC / Other Matters (20)
- Allegations of Securities Law Violations / Fraud (19)
- SEC Questions / Complaints (17)
- Investment Products / Retirement Accounts (13)
- Securities Ownership (10)
- Company Disclosures and Information (9)
- Securities Laws / Rules / Regulations / Procedures (8)
- SEC Investigation / Litigation / Enforcement Actions (5)
- Atypical Matters (1)

In addition to the 102 new matters, we fielded 503 contacts during the Reporting Period, covering ten primary issue categories, for a total of 605 contacts. A portion of these contacts related to matters received prior to this Reporting Period. As expected, a small number of matters relating to issues outside of the SEC’s purview yielded a disproportionate number of contacts due to persistent investor communications and the submission of additional documents and communications to support the

allegations raised in those matters. The chart that follows displays the distribution of the 605 contacts by primary issue category.

**Contacts by Primary Issue Category**  
October 1, 2017–March 31, 2018



- Non-SEC / Other Matters (295)
- Allegations of Securities Law Violations / Fraud (59)
- SEC Questions / Complaints (58)
- Securities Laws / Rules / Regulations / Procedures (46)
- Investment Products / Retirement Accounts (39)
- SEC Investigation / Litigation / Enforcement Actions (38)
- Company Disclosures and Information (28)
- Securities Ownership (27)
- Atypical Matters (11)
- FINRA Arbitration / Rules / Procedures (4)

### How the Numbers Inform our Efforts

The Ombudsman tracks matter and contact data to maintain a comprehensive view of the allocation of staff resources and to identify matters and contacts that significantly alter workflow volumes, call for the realignment of Ombudsman staff assignments, or require added staff support to manage effectively. The data also informs resource allocation considerations related to proposed program development, training, and outreach efforts. By tracking the distribution of matters and contacts across primary issue categories, the data helps the Ombudsman identify potential areas of concern or interest and enables the Ombudsman to act as an early warning system to alert agency leaders about the number and

potential impact of particular issues and concerns raised by retail investors and others.

### SERVICE BEHIND THE NUMBERS

While the matter and contact data quantifies the volume and categories of inquiries the Ombudsman receives, the data does not capture the full value of the service the Ombudsman provides to the investing public. Among the most common situations in which investors present their problems and concerns to the Ombudsman are those in which the investors are unfamiliar with the existing channels established to resolve the particular concerns they raise, unsure which resolution channel to use or how to initiate the process, and unable to get the specific outcome they want through the resolution channels available. In these situations, investors generally assume the outcome they want is a viable option and expect that the Ombudsman is permitted to do whatever is necessary to reach that outcome.

Investors who are unfamiliar with or unsure of the available resolution channels usually will thoughtfully consider the advantages and disadvantages of the resolution options the Ombudsman presents, and establish their expectations based upon the potential outcome each option offers. For these investors, the Ombudsman serves a valuable resource function, but the investor retains responsibility for choosing how to proceed based on the resources the Ombudsman presents. On the other hand, investors who believe they are entitled to a particular result and want the Ombudsman to provide it can be challenging to assist, as they typically conclude that any outcome, other than the particular outcome they want, is unacceptable.

The vignettes that follow are provided to give a sense of the variety of issues we address. Together, they offer a closer look at the how the Ombudsman staff's time, effort, and commitment provide meaningful, personalized service to investors, and illustrate the value of the day-to-day work more effectively than the data alone.

**A retail investor who invested a considerable amount of money** in an initial coin offering (ICO) reached out to the Ombudsman after reading a press release about the SEC halting the ICO. The investor wanted help understanding the next steps in the SEC process and recovering his investment. The Ombudsman staff contacted the investor, discussed the salient aspects of the press release, answered his general questions about ICOs, and directed the investor to the appropriate Division of Enforcement resources for submitting a complaint to the agency.

**An investor who previously corresponded with the SEC** many times regarding his stock ownership made an additional submission to the Commission. The investor reached out to the Ombudsman because he allegedly had not received any response from the agency. The Ombudsman staff followed up with the appropriate staff in an SEC regional office and confirmed that the regional office staff had indeed contacted the investor. In this instance, the investor was simply dissatisfied that his previous correspondence did not result in the particular outcome he desired, and he wanted the Ombudsman to help him force a specific result.

**A retail investor contacted the Ombudsman** after attempting to submit a complaint to the Division of Enforcement about a fraudulent cryptocurrency. The investor was concerned that her complaint had not been received by the SEC and was referred to the Ombudsman after calling the general SEC phone number. The Ombudsman staff discussed the investor's concerns with her and made sure that her complaint was properly submitted so that SEC staff focused on cryptocurrency matters were made aware of the possibly fraudulent activity the investor wanted to report.

**The daughter of an elderly retail investor reached out to the Ombudsman** after learning that a broker may have squandered her mother's sizable investment. The daughter discovered the broker had been investigated and charged by the SEC and wanted information on how to receive any funds recovered from the broker. Her attempts to reach the broker had, up to that point, been unsuccessful. The Ombudsman responded to her concerns and directed her to the SEC Office of Investor Education and Advocacy for additional assistance. The daughter thanked the Ombudsman, and subsequently was able to reach the broker directly. While the daughter felt she had the situation under control, the Ombudsman encouraged her to contact the SEC should she have additional questions or concerns in the future.

**Several non-U.S. investors reached out to the Ombudsman** with questions about SEC endorsement letters, solicitation documents, and other communications containing the SEC seal. After reviewing the details and the documents provided by the investors, the Ombudsman strongly believed that the investors were contacted by individuals engaged in advance fee frauds, common fraudulent schemes directed at non-U.S. investors by entities falsely claiming to be registered or affiliated with the SEC. These types of scams generally involve requests that investors pay a fee in advance to conduct or close a proposed transaction. After the investor pays the fee, the soliciting person or entity typically breaks off contact, the proposed transaction does not take place, and the investor is never paid and never recovers the fees paid in advance. The Ombudsman advised each of these investors to not send money or personal information in response to the solicitations, and to submit their information to the Division of Enforcement. The Ombudsman also directed the investors to information on government impersonators and advance fee fraud scams available on [www.sec.gov](http://www.sec.gov).

Our interactions with investors provide invaluable insight into the information investors rely upon and the assistance they want when making financial decisions. When investors raise questions or complaints that point to the need for more information or additional explanations to assist their understanding of a particular product or process, we attempt to provide personalized, straightforward service to investors by liaising with the appropriate persons and entities, by providing the information necessary to help investors better understand the solutions the SEC can provide, and by empowering and equipping investors to make well-informed investment decisions.

### Communications with Investors

During the Reporting Period, the Ombudsman continued to work extensively with the SEC's Office of Information Technology (OIT) and a technology contractor to refine data and functionality requirements for the Ombudsman Matter Management System (OMMS), an electronic platform for tracking, analyzing, and reporting matter and contact information while ensuring all necessary data management, confidentiality, and reporting requirements are met. The OMMS Form, a web-based form permitting the submission of inquiries directly to the Ombudsman, was made available to the public in September 2017 via the [www.sec.gov/ombudsman](http://www.sec.gov/ombudsman) webpage. The OMMS Form guides the user through a series of questions specifically tailored to elicit information concerning matters within the scope of the Ombudsman's function. In addition, the OMMS Form allows users to electronically upload and submit other questions, concerns, information, and documents for review. The OMMS Form is instructive and user-friendly, and is also compatible for use on mobile devices.

After the launch of the OMMS Form to the public, the Ombudsman began meeting with the SEC's Office of Public Affairs (OPA) to discuss ways to better market the OMMS Form. During these meetings, OPA also made recommendations for improving the OMMS Form user experience. These recommendations enhanced the look and feel of the OMMS Form and were implemented seamlessly, with no disruptions to OMMS Form access.

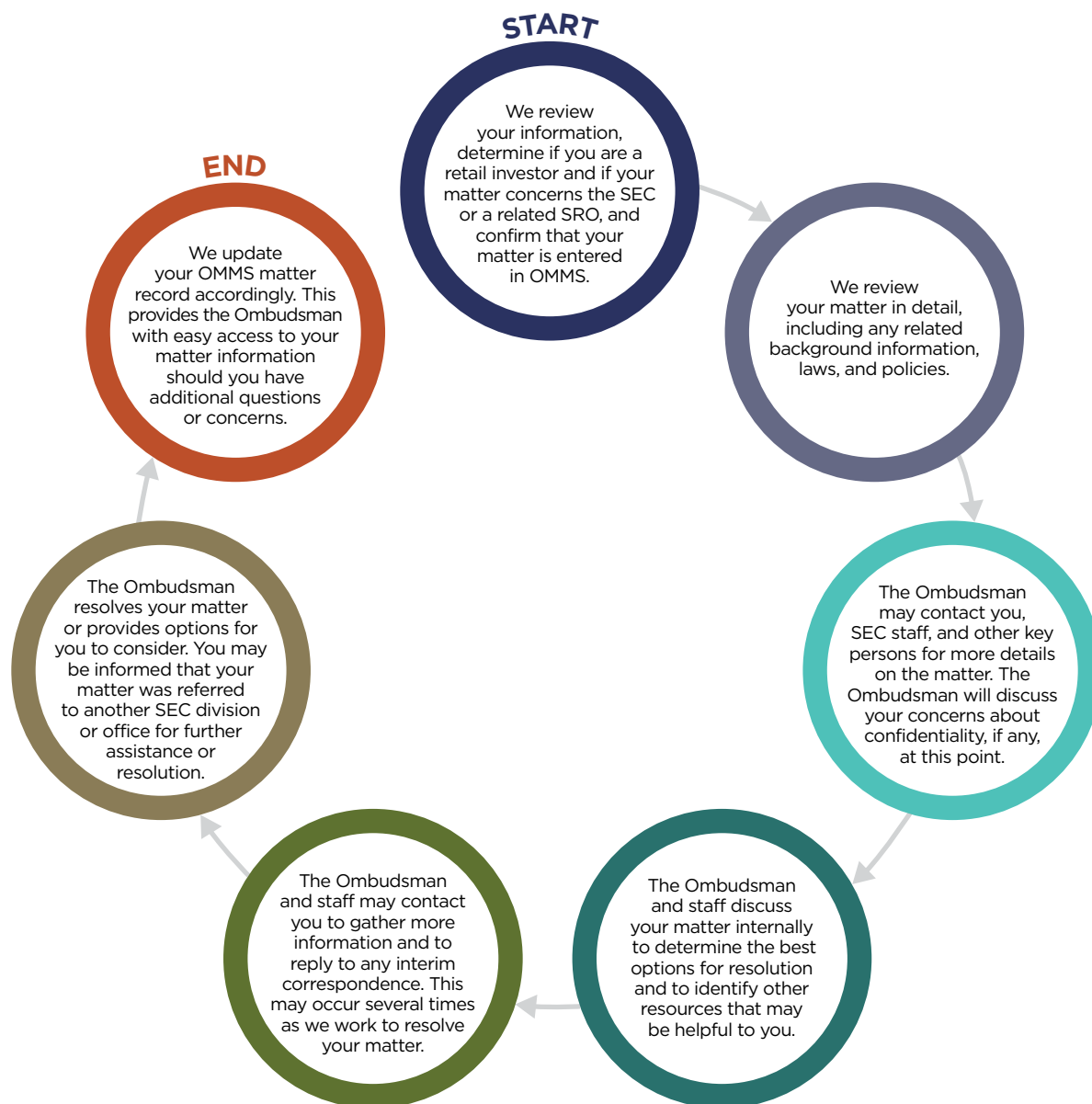
For the Ombudsman, OMMS makes it much easier to review and respond to all emails, voicemails, and other correspondence, and to analyze data, compare issues, and customize reports for a deeper dive into the issues raised. The Ombudsman also reviews matter and contact data on a frequent basis to remain aware of any issues or trends impacting the volume or types of inquiries received. When complicated or sensitive issues are raised, the Ombudsman either handles the inquiry directly or works closely with staff to determine what the next steps should be.

To respond to inquiries effectively and efficiently, the Ombudsman monitors the volume of inquiries and the staff resources devoted to addressing the particular concerns raised. The Ombudsman tracks:

- all inquiries received by, or referred to, the Ombudsman;
- all related correspondence and communications to and from Ombudsman staff;
- staff engagement and resources utilized to respond to inquiries; and,
- inquiry status from receipt to referral or resolution.

The diagram on the following page highlights the standard lifecycle of what happens when investors or other interested persons contact the Ombudsman for assistance.

## What Happens When You Contact the Ombudsman



During FY 2018, the full first fiscal year using OMMS functionality, the Ombudsman and staff will closely monitor questions and suggestions relating to the OMMS Form and will continue to work to enhance the user experience. The Ombudsman is also working with OPA to create a stronger public presence on the web, in social

media, and with investor-focused groups, so that retail investors and others are better informed about the role of the Ombudsman and the resources the Ombudsman provides. For any persons who do not wish, or are unable, to use the OMMS Form, they may still contact the Ombudsman by email, telephone, fax, and mail.

## STANDARDS OF PRACTICE

Similar to ombudsmen at other federal agencies, the Ombudsman follows three core standards of practice:

CONFIDENTIALITY	IMPARTIALITY	INDEPENDENCE
<p>The Ombudsman has established safeguards to protect confidentiality, including the use of OMMS, a separate email address, dedicated telephone and fax lines, and secure file storage. The Ombudsman generally treats matters as confidential, and takes reasonable steps to maintain the confidentiality of communications. The Ombudsman also attempts to address matters without sharing information outside of the Ombudsman staff, unless given permission to do so. However, the Ombudsman may need to contact other SEC divisions or offices, SROs, entities, and/or individuals and share information without permission under certain circumstances including, but not limited to: a threat of imminent risk or serious harm; assertions, complaints, or information relating to violations of the securities laws; allegations of government fraud, waste, or abuse; or if otherwise required by law.</p>	<p>The Ombudsman does not represent or act as an advocate for any individual or entity, and does not take sides on any issues brought to her attention. The Ombudsman maintains a neutral position, considers the interests and concerns of all involved parties, and works to resolve questions and complaints by clarifying issues and procedures, facilitating discussions, and identifying options and resources.</p>	<p>By statute, the Ombudsman reports directly to the Investor Advocate, who reports directly to the Chairman of the SEC. However, the Office of the Investor Advocate and the Ombudsman are designed to remain somewhat independent from the rest of the SEC. Through the Congressional reports filed every six months by the Investor Advocate, the Ombudsman reports directly to Congress without any prior review or comment by the Commission or other Commission staff.</p>

## INVESTOR PROTECTION AND THE RETAIL INVESTOR

The SEC’s mission is to “protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.”<sup>145</sup> At the center of many complaints the Ombudsman receives is a misunderstanding about the SEC’s relationship and obligations to investors because of the “protect investors” language in the SEC mission statement. In these situations, investors frequently assume the purpose for SEC investigations and enforcement actions is to protect investors by getting their money back. As a result, investors often request that the Ombudsman take actions that the Ombudsman is not authorized to take, including:

- deciding the facts in a dispute that the investor has with the Commission or an SRO, or in a dispute before an SRO, such as an arbitration or mediation;
- intervening on behalf of, or representing the interest of, an investor in a formal dispute or investigation process;
- providing advice on how the federal securities laws may impact their particular investments or legal options; or
- changing formal outcomes, including decisions about whether to investigate an allegation of wrongdoing, settle an enforcement action, or create a Fair Fund.



At times, SEC investigations and enforcement actions may align with the personal interests of harmed investors; however, the SEC does not pursue investigations and enforcement actions solely to represent an investor's individual legal interests or to recover money a particular investor may have lost. The Investor Advocate explained it this way in a recent speech:<sup>146</sup>

The SEC, itself, continually reminds investors of its constraints in advocating for their individual interests. Consider how many times every day an investor is told by the SEC staff that we cannot give them legal advice or represent their individual interests. For good reasons, nearly every SEC Investor Alert and hotline phone call includes a disclaimer to the effect that the reader or caller should consult with an attorney who specializes in securities law. In fact, I have personally communicated this to investors many times over the course of my career. When I was a state regulator, I frequently cautioned investors that they should retain private counsel, because even though the interests of victims were generally aligned with the interests of the [state], those interests could diverge—for example, it might be in the best interest of the state to take away a license, which may decrease the likelihood that a victim would be repaid.

In addition, investors have remedies that may not be available to regulators, the most important of which is the ability to seek full restitution of their losses instead of merely disgorging the bad actor's ill-gotten gains. Resource constraints can also make regulators pick and choose among cases, which means that the government may decline to pursue many viable cases. In short, our regulatory framework assumes that investors themselves will serve an important role in policing the markets.

What, then, can the Ombudsman do for investors who have been harmed by violations of the federal securities laws? The Ombudsman routinely explains to investors that they have the ability to protect their interests and preserve their legal rights in ways that the Ombudsman cannot. For example, an investor can file an arbitration complaint with FINRA to address a broker dispute, or hire private legal counsel to advise the investor on the best ways to protect the investor's rights or reach a particular outcome. Investors who do not have the means to hire legal counsel may want to request representation through no-cost legal clinics sponsored by various law schools. While the Ombudsman staff cannot represent the interests of investors in private disputes, we do serve these investors by providing information that will assist them in making choices for themselves. The Ombudsman is always available to answer questions, identify options and resources to address concerns, and to explore informal, objective steps to address issues that may fall outside of the SEC's existing inquiry and complaint processes.

### Monitoring Areas of Interest for Retail Investors

The Office of the Investor Advocate is required to analyze the potential impact on investors of proposed regulations of the Commission and the rules of SROs. In addition, we are required to identify areas in which investors would benefit from changes to existing rules and regulations. The Ombudsman assists the Investor Advocate in this important mission by monitoring policy matters at the SEC and SROs, particularly those that involve rules or processes that are related to issues brought to our attention through the Ombudsman's direct interaction with investors. The updates that follow include information about some of the policy topics of particular concern to the Ombudsman.

### *FINRA Expungement of Customer Dispute Information*

As discussed in the *Report on Activities, Fiscal Year 2017*, the Ombudsman has a strong interest

in the information contained in the Central Registration Depository (CRD), especially because the information is valuable to regulators, firms, and investors.<sup>147</sup> Similarly, FINRA has stated that it has an interest in “protecting the integrity of the CRD system and the information contained in it.”<sup>148</sup>

During the Reporting Period, FINRA issued a notice proposing amendments to several of its rules related to the expungement of customer complaints and dispute information from CRD (the Notice).<sup>149</sup> Some of the rule changes proposed in the Notice include: (1) creating a limitations period for brokers and firms to request expungement from FINRA; (2) establishing an “Expanded Expungement Roster” of attorney arbitrators with specialized experience; (3) requiring arbitrator panels to unanimously agree to award expungement; (4) potentially increasing the fees that brokers or firms must pay when requesting expungement; and (5) requiring the arbitrator panel to unanimously find that the case has no investor protection or regulatory value.<sup>150</sup>

Through the Notice, FINRA seeks to address weaknesses in the expungement process related to settled cases, particularly, “the practice of brokers continually being granted expungement of their disciplinary histories from industry databases.”<sup>151</sup> FINRA also seeks to reduce the expungement rate by, for example, making hearings less one-sided, having hearings presided over by more experienced arbitrators, and adding potential procedural and cost hurdles.

On February 15, 2018, the Investor Advocate and Ombudsman responded to the Notice by submitting a comment letter to FINRA noting our support for some proposals, objections to other proposals, and recommendations to better protect retail investors.<sup>152</sup> One of the proposals we supported was that the three-person arbitrator panel must unanimously find that at least one Rule 2080 prong is present to award expungement.<sup>153</sup> In our view, this requirement will encourage brokers to seek expungement only when the complaint is

meritless, and will provide greater assurance that only meritless complaints are expunged. We also supported the proposal to codify two of the five rights of investors contained in FINRA’s Expanded Expungement Guidance relating to participating in expungement hearings—the right of investors to participate in expungement hearings, and the right to participate via telephone if the investor chooses. Moreover, we recommended that all five rights be codified.<sup>154</sup> Other proposals we supported were that, for arbitrations not decided on the merits, any expungement request related to the case would be heard by a panel of arbitrators from the Expungement Arbitrator Roster, and for simplified arbitration cases, expungement requests must be filed after the arbitration is concluded.<sup>155</sup>

The Investor Advocate and Ombudsman also noted concerns about several proposals and gaps in FINRA’s expungement framework. One concern related to the proposal that an arbitration panel that believes that expungement is appropriate must find that the customer dispute information has no investor protection or regulatory value. While we appreciated the intent, we were concerned that the terms “investor protection” and “regulatory value” were vague and could be interpreted differently and inconsistently by arbitrators. We were especially concerned about the term “regulatory value” because arbitrators are not regulators and are not guided by regulatory concerns. As a result, we recommended that FINRA define these terms, as well as provide a framework for how these terms should be interpreted and applied by arbitrators.

FINRA stated in the Notice that its staff had been working with NASAA on “various expungement issues, including potential amendments to the existing regulatory review process.”<sup>156</sup> As CRD is co-owned by FINRA and NASAA, both are stakeholders in the integrity of CRD and in the expungement process. In our comment letter, we encouraged FINRA to give further consideration to an issue that NASAA brought to the attention of the FINRA Dispute Resolution Task Force

(the Task Force);<sup>157</sup> namely, to consider establishing a procedure for providing pre-notice to state regulators during an ongoing arbitration or establish a standardized protocol for informing states when FINRA waives its role as a party.<sup>158</sup> In closing the comment letter, we commended FINRA for proposing procedural changes that should benefit retail investors, but reiterated our concerns about other proposals.<sup>159</sup> We encouraged FINRA to review the proposal comments and consult with NASAA, and once that was completed, we encouraged FINRA to propose the amended rules to the SEC for approval.

### Funding for New and Existing Investor Advocacy Clinics

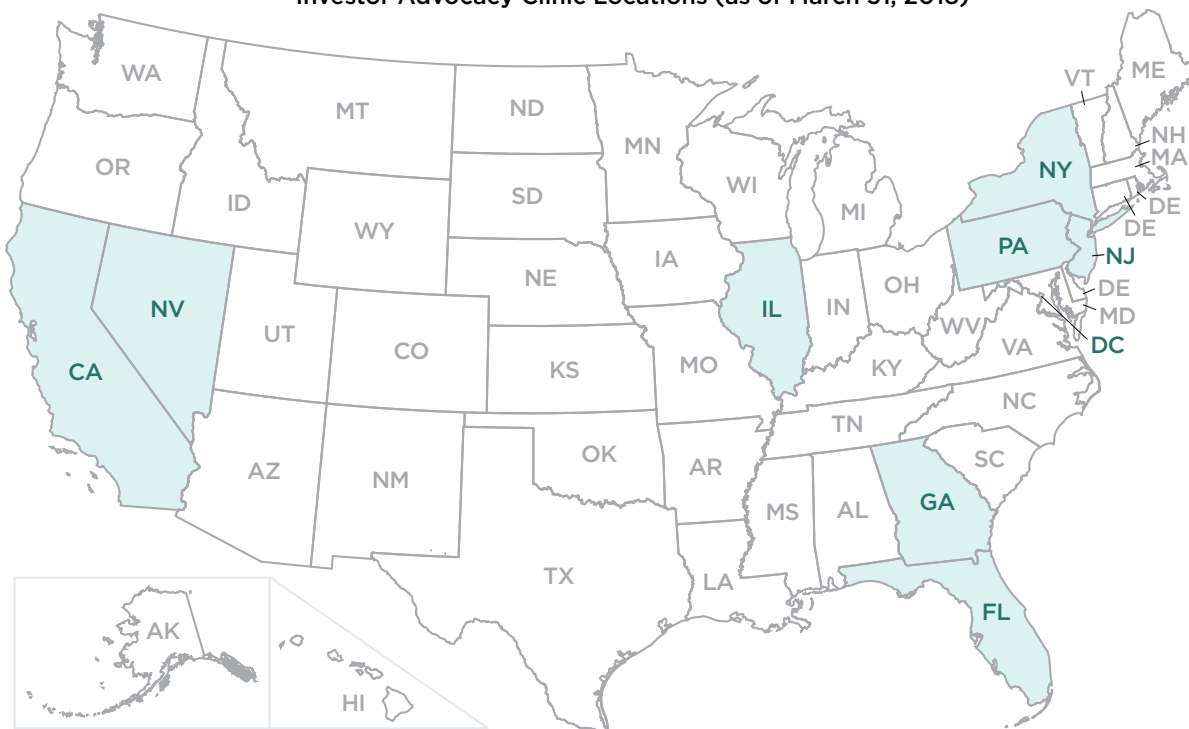
#### Availability of Investor Advocacy Clinics

Arbitration is the forum most used to resolve disputes between retail investors and brokers.<sup>160</sup> However, retail investors with small claim amounts often cannot obtain legal assistance or retain counsel to represent them in arbitration

proceedings.<sup>161</sup> In response, in 1997, then SEC Chairman Arthur Levitt announced the start of two pilot securities arbitration clinics that provided no cost legal services to help these retail investors.<sup>162</sup> Over time, other securities arbitration clinics were established and sustained through funding from portions of securities fraud enforcement case awards<sup>163</sup> and from state securities commissions.<sup>164</sup> As discussed in the *Report on Objectives, Fiscal Year 2018*,<sup>165</sup> from 2009 through 2012, the FINRA Investor Education Foundation (the Foundation) also provided grants of \$250,000 each to eight law schools as start-up funding to establish investor advocacy clinics.<sup>166</sup>

At the peak, 24 investor advocacy clinics existed across the country, most located in the Northeast. There are only 17 clinics in operation today.<sup>167</sup> Since 2012, no Foundation funds have been awarded to clinics, leading to a perception that the Foundation has a policy not to fund new or ongoing clinic operations.<sup>168</sup> While the start-up grants were sufficient for those clinics that were

Investor Advocacy Clinic Locations (as of March 31, 2018)



able to secure additional sustaining funds, as external funding options have dwindled, some clinics have been forced to close, leaving a void for advocacy and access to justice for retail investors across the majority of the country.<sup>169</sup>

Investor advocacy clinics present a unique opportunity to educate and help protect retail investors with smaller claims. As the investors interact directly with clinic faculty and law students, an obvious advantage is that the investors—often seniors and persons with limited access to technology—have the benefit of personalized service, either in person or by phone, while avoiding miscommunications, the need for computer access, and unwanted or unsuitable sales tactics. The Task Force noted that while it was not inclined to second guess the Foundation’s policy of limiting funding to “new or expanded projects with reasonable prospects for post-grant sustainability,”<sup>170</sup> continued funding of investor advocacy clinics would be an appropriate use of FINRA fines and penalties.<sup>171</sup> The Ombudsman agrees with the Task Force that funding investor advocacy clinics would be an appropriate use of FINRA fines and penalties, as these clinics offer an invaluable service by providing legal advice and representation to retail investors who need it most.

### *The Important Services Provided by Investor Advocacy Clinics*

Many retail investors lack the familiarity and sophistication to navigate the securities arbitration process without legal representation.<sup>172</sup> As expressed to then SEC Chairman Levitt during town hall meetings more than 20 years ago, small investors often did not pursue their claims due to difficulties in obtaining legal representation, and intimidation and unfamiliarity with the arbitration process.<sup>173</sup> To help small investors “who have nowhere else to turn,” the SEC launched a pilot securities arbitration clinic program in 1997.<sup>174</sup> The clinics were designed to help small investors receive “high quality legal representation and assistance, while at the same time providing law students with a valuable learning experience.”<sup>175</sup>

Investor advocacy clinics have evolved over the years. Not only do clinics provide legal advice and representation during the arbitration process, they help many more retail investors by providing investor education, counseling, outreach services, and presentations—in person, online, and through printed resources. These efforts keep retail investors informed of important issues and help them avoid becoming victims of frauds and scams. Clinics also draft and submit formal comment letters to the SEC, FINRA, and other securities industry organizations to draw attention to issues affecting retail investors, providing a voice and platform for the concerns of retail investors to be heard and examined.

The Ombudsman, working directly with the Investor Advocate and staff, renewed the SEC’s commitment and outreach to investor advocacy clinics by developing and implementing the Law School Clinic Outreach Program (LSCOP),<sup>176</sup> discussed in more detail below. To date, the Ombudsman and key Office of the Investor Advocate counsel have visited 16 of the 17 law school clinics currently in operation across the country.<sup>177</sup> Through insights gained from their personalized, direct interactions with retail investors, these clinics have provided the Ombudsman and Investor Advocate vital information and feedback on problematic products and practices, as well as suggestions for enhancing the SEC’s outreach to retail investors.<sup>178</sup>

### *Recommendation of the SEC Investor Advisory Committee*

As noted by the SEC Investor Advisory Committee (the IAC or the Committee) in a recent recommendation to the Commission,<sup>179</sup> “[l]aw school and investor advocacy clinics fill a crucial gap for retail investors by providing high quality legal advice and representation to investors with small claims, that otherwise, would have no access to representation. The Committee is concerned that due to the lack of external funding available to existing investor advocacy clinics, clinics will be forced to further

curtail services or close their doors, leaving small investors with nowhere to turn. Moreover, the Committee recognizes that law school investor advocacy clinics play an important role in the protection of retail investors through their education and advocacy efforts.”<sup>180</sup> For these reasons, the IAC made a formal recommendation to the SEC to improve funding sources for investor advocacy clinics. In the short term, the IAC recommended the SEC work with FINRA to provide continued funding to existing clinics, and work with NASAA and the broader legal community to identify potential state and local funding sources. In addition, for the long term, the IAC encouraged the SEC to request legislation from Congress to consider “permanently funding investor advocacy clinics, possibly through a matching grant program through the SEC Investor Protection Fund.”<sup>181</sup>

The Committee believes the investor advocacy clinics serve an important function in providing retail investors access to protection, education, and advocacy, and therefore, clinics should have a defined and reliable source of funding.

The Committee believes the SEC Investor Protection Fund is the appropriate source of funding to advance investor education initiatives to help investors protect themselves against securities fraud or other violations of securities laws. The SEC Investor Protection Fund as enacted provides funding for the SEC’s whistleblower award program and the employee suggestion program of the SEC’s Office of Inspector General. It is funded by monetary sanctions collected by the Commission through judicial and administrative actions against securities laws violators. Money deposited into the fund is designated after harmed retail investors receive payment. Since the Investor Protection Fund’s creation the balance has remained

over \$300,000,000 in each fiscal year report from 2011–2017. As such, the SEC Investor Protection Fund is the ideal funding source for investor advocacy clinics. Moreover, investor advocacy clinics directly align with the Congressional intent of the SEC Investor Protection Fund to educate and protect retail investors.<sup>182</sup>

### *Recommendation of the Clinic Directors*

In response to FINRA’s request for comment on its investor education initiatives,<sup>183</sup> 13 investor advocacy clinic directors raised similar concerns about the establishment and support of clinics, and made recommendations for funding clinics in a June 19, 2017, letter to FINRA:

Because FINRA’s investor protection mission and the live-client representation and educational functions of law school securities arbitration clinics align so closely, we respectfully request that FINRA’s investor education engagement initiatives include creating a funding model that sustains and grows clinics. This request is not without precedent. For example, in its 2015 report, the FINRA Dispute Resolution Taskforce wrote that it “believes that an appropriate use of FINRA fines and penalties would be funding of law school arbitration clinics and recommends FINRA consideration.” Moreover, funds may be available for this purpose from both FINRA and the FINRA Investor Education Foundation. The FINRA Investor Education Foundation’s 2015 Form 990 indicates net assets exceeding \$74 million. In that year, FINRA awarded \$50 million to the Foundation. FINRA’s 2015 annual report also noted that its “financial position remains strong and highly liquid with approximately \$2.3 billion of total assets, including \$2.0 billion of cash and investments,

and approximately \$1.5 billion in equity.” Successful models for funding of law school clinics already exist. As one example, addressing similar needs in the context of unrepresented taxpayers, the IRS Office of the Taxpayer Advocate created a successful low income taxpayer clinic (LITC) grant program in 1999. In its first year, that program “awarded grants totaling less than \$1.5 million to 34 entities located in 18 states and the District of Columbia.” Almost 20 years later, in 2016, the program has grown to fund “138 entities located in 49 states and the District of Columbia.” To ensure sustainability of LITCs, the program requires that law schools match grants dollar for dollar up to a maximum grant of \$100,000. A similar program for securities arbitration clinics would ensure the longevity of existing clinics and create capacity for new clinics in high need areas.<sup>184</sup>

#### *Ombudsman’s Support of the IAC and Clinic Directors’ Recommendations*

On behalf of retail investors, particularly the most vulnerable and those residing in the more than 40 states and U.S. territories where no investor advocacy clinics are located, the Ombudsman fully supports the recommendations made by both the IAC and the clinic directors to financially support and expand the critical services performed by the existing investor advocacy clinics, and to create additional funding pathways for new clinics to be established at law schools throughout the country.

As the clinic directors noted in their letter to FINRA, successful models for funding clinics already exist. As the IAC noted in its recommendation, the SEC Investor Protection Fund is an appropriate source of funding to advance investor education initiatives to help investors protect themselves against securities fraud or other violations of securities laws, as the purpose and work of the clinics directly align

with the congressional intent of the SEC Investor Protection Fund. Furthermore, the SEC Investor Protection Fund is not subject to fluctuations due to congressional budget appropriations, thereby ensuring that the clinics have a predictable and dependable source of funding.

The Ombudsman agrees that one effective solution would be for the SEC to request legislation from Congress to permanently fund investor advocacy clinics, and that the SEC Investor Protection Fund is a suitable funding source. The Ombudsman also agrees that funds from FINRA and its Foundation would be appropriate to fund investor advocacy clinics. The Ombudsman is confident that, should FINRA resume funding for investor advocacy clinics, and should the SEC request legislation from Congress to fund investor advocacy clinics through the SEC Investor Protection Fund, the Ombudsman could utilize the framework of the successful LITC grant program as a starting point and tailor an investor advocacy clinic grant program to best serve the needs and work of these clinics. The SEC and Congress can be assured that the Ombudsman, with dedicated staff, would develop a comprehensive program to monitor and audit the designation and effectiveness of grant awards to ensure that the work and services of the clinics can be tracked accordingly, and most importantly, that the needs of retail investors who rely upon these clinics the most are met.

#### **LAW SCHOOL CLINIC OUTREACH PROGRAM**

During the Reporting Period, the Office continued the broad rollout of the Law School Clinic Outreach Program (LSCOP or the Program). As discussed in prior reports,<sup>185</sup> the Ombudsman, working directly with the Investor Advocate and other staff, developed LSCOP to connect with law schools with investor protection, securities law, and investor-focused clinics that align with our Office’s statutory mandate and core functions, and to benefit law student clinic participants and the investing public.



In October 2017, the Ombudsman and the Office hosted clinic directors and students from five law schools at SEC Headquarters. This visit coincided with the October 12, 2017, public meeting of the IAC. During that meeting, the IAC discussed the work of law school clinics and invited two clinic directors and a law student to submit prepared remarks to the Committee and provide an overview of clinic advocacy efforts on behalf of retail investors.<sup>186</sup> In addition to attending and presenting at the IAC meeting, clinic directors and students had the opportunity to meet and engage in interactive discussions with Chairman Clayton, Commissioner Stein, Commissioner Piwowar, Division of Investment Management Director Dalia Blass, Division of Enforcement Associate Director Melissa Hodgman, and other senior staff. The law school clinic discussion and subsequent meetings generated great dialogue about the work of law school clinics and the challenges clinics face, including ongoing funding challenges.

Shortly thereafter, the Ombudsman and Office staff had the opportunity to observe in-person an Investor Education Roadshow in Teaneck, New Jersey, sponsored by Seton Hall University School of Law's Investor Advocacy Project. This was the Office's first opportunity to observe first-hand clinic investor education and outreach. The Office appreciated the opportunity to gain a better understanding of direct clinic outreach efforts, and was impressed by the clinic-led presentation and information session.

The Ombudsman and Office staff also conducted on-site visits to the University of Miami School of Law Investor Rights Clinic and UNLV's William S. Boyd School of Law Investor Protection Clinic during this Reporting Period, engaging with clinic faculty and students in the classroom setting. Prior to visiting the University of Miami School of Law Investor Rights Clinic, the Ombudsman and Office staff submitted discussion topics and questions to the clinic director. As in prior visits, the clinic students raised extremely insightful questions and

provided feedback aimed at ameliorating common problems experienced by the clinic clients.

In January 2018, UNLV William S. Boyd School of Law's Investor Protection Clinic opened its doors, becoming the seventeenth investor advocacy clinic currently active in the United States.<sup>187</sup> The Ombudsman and Office staff visited the new clinic, engaged with clinic faculty and students, and shared more about the work of our Office, the Program, and how the clinic and the Office may work together moving forward. Additionally, the Ombudsman and staff were able to solicit perspectives and policy feedback on retail investor concerns.

In March 2018, the Ombudsman and the Office coordinated an in-person visit for approximately 26 clinic faculty and students, representing seven different law schools, at SEC Headquarters. Clinic faculty and students attended the public IAC meeting and met with Chairman Clayton, Commissioner Stein, Commissioner Piwowar, Commissioner Peirce, and other senior staff. The in-person visit provided clinic faculty and students the opportunity to discuss the potential impact of SEC policy considerations on their clients directly with SEC Commissioners and senior staff. Moreover, during the March 2018 public meeting of the IAC, the IAC voted to approve a recommendation, "Financial Support for Law School Clinics that Support Investors,"<sup>188</sup> addressing the ongoing funding concerns clinics face and have highlighted to the Office throughout the Program's existence.

Additionally, throughout the Reporting Period, a number of law schools and faculty expressed interest in starting investor advocacy clinics at their institutions. To that end, although our Office does not assist law schools with establishing clinics, the Ombudsman has acted as a liaison, providing appropriate resources and connections related to establishing investor advocacy clinics to law school faculty and administrators.

## OBJECTIVES AND OUTLOOK

During the Reporting Period, retail investors continued to raise questions and complaints that highlighted a fundamental lack of understanding about how the SEC protects investors. As noted in the *Report on Activities, Fiscal Year 2017*, the Ombudsman will continue to examine the various ways the SEC communicates with the investing public to identify areas for improvement. The Ombudsman will continue to work with SEC divisions and offices to identify places where our messaging to retail investors—particularly as that messaging relates to the SEC’s mission, authority, and efforts to protect investors—should be refined and improved.

To this end, the Ombudsman worked with OPA during this fiscal year to improve the look and feel of the OMMS Form and to revamp the [www.sec.gov/ombudsman](http://www.sec.gov/ombudsman) webpage to update the content, improve messaging, and simplify navigation. The updated webpage should be available to the public before the end of this fiscal year.

To focus our efforts and staff resources properly, the Ombudsman will continue to track matter and

contact data, identify trends, and conduct detailed research and analysis. With the use of OMMS for the entire 2018 Fiscal Year, the Ombudsman anticipates OMMS will help identify additional areas of concern to investors and permit more targeted research and analysis.

Finally, the Ombudsman looks to Fiscal Year 2019 as an opportunity to establish more extensive channels of communication with retail investors, including through working with law school clinics and other organizations focused on retail investor concerns. Clinic faculty and students participating in our Program remain eager to identify areas in which retail investors could potentially benefit from rulemaking and policy changes, and to offer feedback and practical solutions. The Ombudsman will continue to seek opportunities to solicit perspectives, feedback, and formal comments on SEC rulemakings and policy and retail investor concerns from the clinic faculty and students. Most importantly, the Ombudsman will continue to foster an environment for the voices of retail investors to be heard and considered as a vital part of the work of the Office.



Tracey L. McNeil  
Ombudsman



# SUMMARY OF INVESTOR ADVISORY COMMITTEE RECOMMENDATIONS AND SEC RESPONSES

Congress established the Investor Advisory Committee (IAC) to advise and consult with the Commission on regulatory priorities, initiatives to protect investor interests, initiatives to promote investor confidence and the integrity of the securities marketplace, and other issues.<sup>189</sup> The Committee is composed of the Investor Advocate, a representative of state securities commissions, a representative of the interests of senior citizens, and not fewer than 10 or more than 20 members appointed by the Commission to represent the interests of various types of individual and institutional investors.<sup>190</sup>

Exchange Act Section 39 authorizes the Committee to submit findings and recommendations for review and consideration by the Commission.<sup>191</sup> The statute also requires the SEC “promptly” to issue a public statement assessing each finding or recommendation of the Committee and disclosing the action, if any, the Commission intends to take with respect to the finding or recommendation.<sup>192</sup> While

the Commission must respond to the IAC’s recommendations, it is under no obligation to agree with or act upon the recommendations.<sup>193</sup>

In each of our reports to Congress, the Office of the Investor Advocate summarizes the IAC recommendations and the SEC’s responses to them.<sup>194</sup> In the past, the Commission has taken action that was responsive to the IAC’s recommendations related to crowdfunding,<sup>195</sup> a shortened trade settlement cycle,<sup>196</sup> and increasing the number investment adviser examinations.<sup>197</sup> This report covers all other recommendations the IAC has made since its inception. For more detailed summaries, please see our earlier reports to Congress.

The Commission may be pursuing initiatives that are responsive to IAC recommendations but have not yet been made public. Commission staff—including the staff of this Office—are prohibited from disclosing nonpublic information.<sup>198</sup> Therefore, any such initiatives are not reflected in this Report.



Topic	Date	IAC Recommendation	SEC Response
Financial Support for Law School Clinics that Support Investors <sup>199</sup>	March 8, 2018	Explore ways to improve external funding sources to the law school investor advocacy clinics. Work with FINRA, NASAA, and other potential partners, and request legislation from Congress to consider permanent funding.	Pending.
Dual Class and Other Entrenching Governance Structures in Public Companies <sup>200</sup>	March 8, 2018	The SEC Division of Corporation Finance should scrutinize disclosure documents filed by companies with dual class and other entrenching governance structures and develop a pilot program to monitor shareholder disputes and to determine if enhanced disclosure requirements are necessary.	Pending.
Promotion of Electronic Delivery and Development of a Summary Disclosure Document for Delivery of Investment Company Shareholder Reports <sup>201</sup>	Dec. 7, 2017	Explore methods to encourage a transition to electronic delivery that respect investor preferences and that increase the likelihood that investors will see and read important disclosure documents, and explore development of a summary disclosure document for annual shareholder reports that incorporates key information from the report along with prominent notice regarding how to obtain a copy of the full report.	On June 4, 2018, the SEC adopted new rule 30e-3 under the Investment Company Act, which allows registered investment companies to deliver shareholder reports by making such reports accessible at a website address specified in a written notice to investors, <sup>202</sup> unless an investor expresses a preference for delivery of printed shareholder reports. Within the notice of availability of the shareholder report, an investment company is permitted to provide additional information, including content from the shareholder report that the fund considers helpful to investors. <sup>203</sup>
Enhance Information for Bond Market Investors <sup>204</sup>	June 7, 2016	Provide post-trade price transparency, including markups or markdowns, in municipal, corporate and agency bonds and, over the longer term, provide pre-trade price transparency as well.	On November 17, 2016, the SEC approved new FINRA and MSRB rules requiring disclosure of mark-ups and markdowns on most municipal and corporate bond transactions, calculated from the bond's prevailing market price. <sup>205</sup> The rules became effective on May 14, 2018. <sup>206</sup> In November 2017, the SEC announced the formation of its Fixed Income Market Structure Advisory Committee, which began meeting in January 2018. <sup>207</sup>

Topic	Date	IAC Recommendation	SEC Response
Mutual Fund Cost Disclosure <sup>208</sup>	April 14, 2016	Enhance investors' understanding of mutual fund costs and the impact of those costs on total accumulations over time. Provide standardized disclosure of actual dollar costs on customer account statements.	On June 4, 2018, the SEC issued a request for comment seeking input from individual investors and other interested parties on how to enhance the delivery, design, and content of fund disclosures, including shareholder reports and prospectuses. <sup>209</sup> The request for comment solicits investor feedback on, among other things, fund fees and expenses, and includes questions related to the IAC recommendation (e.g., dollar vs. percentage disclosure, disclosure within account statements, etc.). <sup>210</sup>
Empowering Elders and Other Investors: Background Checks <sup>211</sup>	July 16, 2015	Develop a disciplinary database to allow easy searches to determine whether a person or firm has been sanctioned for securities law violations. Reduce the complexity of background searches.	On May 2, 2018, the SEC launched a new online search tool that enables investors to research whether the person trying to sell them investments has a judgment or order entered against them in an enforcement action. The new tool is called SEC Action Lookup for Individuals (SALI). <sup>212</sup>
Accredited Investor Definition <sup>213</sup>	Oct. 9, 2014	Consider enabling individuals to qualify as accredited investors based on their financial sophistication.	On December 18, 2015, the SEC issued a staff report that discussed, among other alternatives, using sophistication as an element of the accredited investor definition.
Impartiality in the Disclosure of Preliminary Voting Results <sup>214</sup>	Oct. 9, 2014	Ensure impartiality in the disclosure of preliminary voting results.	Pending.
Decimalization and Tick Sizes <sup>215</sup>	Jan. 31, 2014	Oppose any test or pilot programs to increase the minimum quoting and trading increments ("tick sizes") in the securities markets.	A 2-year pilot program began in October 2016 and is set to expire on Oct. 2, 2018. FINRA and the exchanges have a deadline of July 3, 2018, to submit a joint assessment of the impact of the Tick Pilot.



Topic	Date	IAC Recommendation	SEC Response
Broker-Dealer Fiduciary Duty <sup>216</sup>	Nov. 22, 2013	Establish a fiduciary duty for broker-dealers when they provide personalized investment advice to retail investors.	On April 18, 2018, the SEC voted to propose Regulation Best Interest, under which a broker-dealer would be required to act in the best interest of a retail customer when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer. The SEC is seeking public comments for 90 days. <sup>217</sup>
Universal Proxy Ballots <sup>218</sup>	July 25, 2013	Allow universal ballots in connection with short slate director nominations.	On October 26, 2016, the SEC proposed amendments to the proxy rules to require parties in a contested election to use universal proxy cards that would include the names of all board of director nominees. <sup>219</sup>
Data Tagging <sup>220</sup>	July 25, 2013	Promote the use of machine-readable data tagging formats for data filed with the SEC.	The SEC has addressed data tagging in a number of final and proposed rules. <sup>221</sup> On April 20, 2018, the SEC Staff issued updated FAQs on IFRS Taxonomy.
Target Date Mutual Funds <sup>222</sup>	April 11, 2013	Revise an SEC proposed rule on target date retirement fund names and marketing, and develop a glide path illustration based on a measure of fund risk.	On April 3, 2014, the Commission reopened the comment period on the proposed rule in order to seek public comment on the IAC's recommendations to adopt a risk-based glide path illustration and the methodology to be used for measuring risk. <sup>223</sup> The comment period closed on June 9, 2014.
General Solicitation and Advertising <sup>224</sup>	Oct. 12, 2012	Strengthen investor protections and enhance regulators' ability to police the private placement market.	The SEC adopted final general solicitation and advertising rules on July 10, 2013, and also proposed a related rule to enhance its ability to monitor the market following lifting of the ban. That proposal, which relates to most of the IAC recommendations, is pending. <sup>225</sup>

## End Notes

- 1 Exchange Act § 4(g)(6), 15 U.S.C. § 78d(g)(6).
- 2 Exchange Act § 4(g)(6)(A)(i), 15 U.S.C. § 78d(g)(6)(A)(i).
- 3 Exchange Act § 4(g)(6)(B)(i), 15 U.S.C. § 78d(g)(6)(B)(i).
- 4 Exchange Act § 4(g)(4)(A), 15 U.S.C. § 78d(g)(4)(A).
- 5 Exchange Act § 4(g)(8)(A), 15 U.S.C. § 78d(g)(8)(A).
- 6 Exchange Act § 4(g)(8)(D), 15 U.S.C. § 78d(g)(8)(D).
- 7 Exchange Act § 4(g)(4)(B), 15 U.S.C. § 78d(g)(4)(B).
- 8 Exchange Act § 4(g)(4)(C), 15 U.S.C. § 78d(g)(4)(C).
- 9 Exchange Act § 4(g)(4)(D), 15 U.S.C. § 78d(g)(4)(D).
- 10 Exchange Act § 4(g)(4)(E), 15 U.S.C. § 78d(g)(4)(E).
- 11 Exchange Act § 39, 15 U.S.C. § 78pp.
- 12 Exchange Act § 39(b)(1)(A), 15 U.S.C. § 78pp(b)(1)(A).
- 13 See Regulatory Flexibility Agenda, Securities Act Release No. 10424, Exchange Act Release No. 81839, Investment Company Act Release No. 32857, 83 Fed. Reg. 2,022 (Jan. 12, 2018); SEC, “Spring 2018 Unified Agenda of Regulatory and Deregulatory Actions,” <https://www.reginfo.gov/public/do/eAgendaMain>. The Current Agenda for the Securities and Exchange Commission lists the rulemakings that Chairman Jay Clayton “actually intends and realistically expects to accomplish over the coming year.” See *Examining the SEC’s Agenda, Operations and Budget: Hearing Before the H. Comm. on Financial Services*, 115th Cong. (2017) (testimony of Jay Clayton, Chairman, SEC), <https://www.sec.gov/news/testimony/testimony-examining-secs-agenda-operation-and-budget> [hereinafter Clayton Testimony on Examining the SEC’s Agenda, Operation, and Budget]. The “Current Long Term Actions” lists rulemaking projects with a less certain timetable.
- 14 See Clayton Testimony on Examining the SEC’s Agenda, Operation, and Budget, *supra* note 13.
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- 30 See Comment Letter, Rick A. Fleming, Investor Advocate, SEC, RE: File No. S7-23-15, Regulation of NMS Stock Alternative Trading Systems (Sept. 9, 2016), <https://www.sec.gov/about/offices/investoradv/investor-advocate-comment-letter-regulation-ats.pdf>.
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- 62 See FIMSAC Preliminary Recommendation, *supra* note 61; see also FIMSAC April Webcast, *supra* note 60.
- 63 Typically, a municipal bond dealer places a retail client's bid-wanted out to the market and compiles the bids received to determine the winning bid. In "pennying" or as it may also be called, "last-look," the dealer, rather than execute a trade with the highest bidder, will nominally exceed the high bid to the client and buy the bond for the dealer's own trading account. The MSRB has expressed concern that it can be harmful to investors over the long-term if the practice discourages broad market participation in the bidding process and renders the market less efficient. Filtering (or screening) is the practice where a dealer may use automated tools available on an alternate trading system to screen out bids and offers received from certain dealers or where a selling dealer may direct a broker's broker to limit the audience for a bid-wanted. According to the MSRB, policies and procedures should be in place to govern when and how to: reasonably use filters; periodically review any established filters; and consider lifting them upon request. See Letter from Lynnette Kelly, Exec. Dir., MSRB, to Rick A. Fleming, Investor Advocate, SEC, RE: *Response to SEC Request Highlighting*



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- 66 FINANCIAL ACCOUNTING STANDARDS BOARD, MEASUREMENT OF CREDIT LOSSES ON FINANCIAL INSTRUMENTS 249-84 (2016), [https://www.fasb.org/jsp/FASB/Document\\_C/DocumentPage?cid=1176168232528&acceptedDisclaimer=true](https://www.fasb.org/jsp/FASB/Document_C/DocumentPage?cid=1176168232528&acceptedDisclaimer=true).
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- 68 *Id.* at 5. For public business entities that are SEC filers, the new standard will become effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Thus, for a calendar-year company, it would be effective January 1, 2020.
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- 114 *Transfer Agent Concept Release*, *supra* note 101, at 81,981.
- 115 *See id.* at 81,982.
- 116 The statute in full reads, “[e]xcept as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon.” 28 U.S.C. § 2462.
- 117 *Kokesh v. SEC*, 137 S. Ct. 1635, 1645 (2017).
- 118 *See Gabelli v. SEC*, 568 U.S. 442, 454 (2013).
- 119 *Kokesh*, 137 S. Ct. at 1641.
- 120 *Id.*
- 121 *Id.*
- 122 *Id.*
- 123 *Id.*
- 124 *Kokesh v. SEC*, 834 F.3d 1158, 1164-67 (2016).
- 125 In holding that disgorgement is not a penalty, the Tenth Circuit expressly disagreed with a June 2016 opinion by the Eleventh Circuit in *SEC v. Graham* that declaratory relief and disgorgement are a penalty and forfeiture respectively under the plain meaning of 28 U.S.C. § 2463. *SEC v. Graham*, 823 F.3d 1357, 1364 (2016). *See also* Mary Jo White et al., *What Kokesh V. SEC Means for Enforcement Actions*, LAW360 (June 8, 2017, 4:54 pm ET) <https://www.law360.com/articles/932661/what-kokesh-v-sec-means-for-enforcement-actions>.
- 126 *See Kokesh*, 137 S. Ct. at 1641.
- 127 *See id.* at 1645.
- 128 *Oversight of the U.S. Securities and Exchange Commission’s Division of Enforcement: Hearing Before the H. Comm. on Fin. Servs., Subcomm. on Capital Mkts., Secs., and Inv.*, 115th Cong., at 8 (2018), <https://financialservices.house.gov/uploadedfiles/hhrg-115-ba00-wstate-savakianspeikin-20180516.pdf> (testimony of Stephanie Avakian and Steven Peikin, Co-Directors, Division of Enforcement, SEC).
- 129 *Id.* at 1.
- 130 *Id.* at 8.
- 131 *Id.*
- 132 *Id.*
- 133 *Id.*
- 134 *Id.*
- 135 *See id.*
- 136 *Id.*
- 137 *Id.*
- 138 *Oversight of the U.S. Securities and Exchange Commission’s Division of Enforcement: Hearing Before the H. Comm. on Fin. Servs., Subcomm. on Capital Mkts., Secs., and Inv.*, 115th Cong. (2018), <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403383> (testimony of Stephanie Avakian and Steven Peikin, Co-Directors, Division of Enforcement, SEC) (webcast of verbal testimony).
- 139 White et al., *supra* note 125.
- 140 *Id.*
- 141 *Oversight of the U.S. Securities and Exchange Commission’s Division of Enforcement: Hearing Before the H. Comm. on Fin. Servs., Subcomm. on Capital Mkts., Secs., and Inv.*, 115th Cong. (2018), <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403383> (testimony of Stephanie Avakian and Steven Peikin, Co-Directors, Division of Enforcement, SEC) (webcast of verbal testimony).
- 142 Exchange Act § 4(g)(8)(B), 15 U.S.C. § 78d(g)(8)(B).
- 143 Exchange Act § 4(g)(8)(D), 15 U.S.C. § 78d(g)(8)(D).
- 144 As used in this report, the term “Ombudsman” may refer to the Ombudsman, or to the Ombudsman and Office of the Investor Advocate staff and contractors directly supporting the ombudsman function.
- 145 *What We Do*, SEC, <https://www.sec.gov/Article/whatwedo.html> (last modified June 10, 2013).
- 146 Rick Fleming, Investor Advocate, SEC, *PLI’s The SEC Speaks in 2018, Mandatory Arbitration: An Illusory Remedy for Public Company Shareholders* (Feb. 24, 2018), <https://www.sec.gov/news/speech/fleming-sec-speaks-mandatory-arbitration>.
- 147 SEC, Office of the Investor Advocate, *Report on Activities, Fiscal Year 2017* at 27-31 (Dec. 20, 2017),

- <https://www.sec.gov/advocate/reportspubs/annual-reports/sec-investor-advocate-report-on-activities-2017.pdf> [hereinafter *Report on Activities, Fiscal Year 2017*].
- 148 *Royal Alliance Associates v. Liebhaber*, 206 Cal. Rptr. 3d 805, 814 (Cal. Ct. App. 2016).
- 149 See generally FINRA, Reg. Notice 17-42, Expungement of Customer Disp. Info. (Dec. 2017), <http://www.finra.org/industry/notices/17-42> [hereinafter Notice 17-42]. Some of the data in CRD serves as the source data for BrokerCheck. Both systems are maintained by FINRA.
- 150 *Id.*
- 151 Antoinette Gartrell, *FINRA to Address Expungement Issues, Arbitration Chief Says*, BLOOMBERG BNA (Mar. 21, 2016), <http://www.bna.com/finra-address-expungement-n57982068766> (quoting statements from Richard Berry, Executive Vice-President and Director, FINRA Dispute Resolution).
- 152 See generally Comment Letter, Rick A. Fleming, Investor Advocate and Tracey L. McNeil, Ombudsman, SEC, RE: Regulatory Notice 17-42 (Feb. 15, 2018) [hereinafter Comment Letter RE: Notice 17-42], [http://www.finra.org/sites/default/files/notice\\_comment\\_file\\_ref/17-42\\_SEC\\_comment.pdf](http://www.finra.org/sites/default/files/notice_comment_file_ref/17-42_SEC_comment.pdf).
- 153 *Id.* at 6. Under FINRA Rule 2080(b)(1), the arbitrator panel must find that: (A) the claim, allegation or information is factually impossible or clearly erroneous; (B) the registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or (C) the claim, allegation or information is false.
- 154 See *id.* at 5-6. The five rights are: (1) Allow the customer and their counsel to appear at the expungement hearing; (2) Allow the customer to testify (telephonically, in person, or other method) at the expungement hearing; (3) Allow counsel for the customer or a *pro se* customer to introduce documents and evidence at the expungement hearing; (4) Allow counsel for the customer or a *pro se* customer to cross-examine the broker and other witnesses called by the party seeking expungement; and (5) Allow counsel for the customer or a *pro se* customer to present opening and closing arguments if the panel allows any party to present such arguments. Only items (1) and (2) would be codified under the proposal.
- 155 *Id.* at 6-7.
- 156 Notice 17-42, *supra* note 149, at 1.
- 157 Comment Letter, William Beatty, President, NASAA, RE: NASAA Comments on Expungement of Matters from the Central Registration Depository (CRD) at 7 (Aug. 31, 2015), <http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2011/07/NASAA-Expungement-Letter-enclosure.pdf>.
- 158 Comment Letter RE: Notice 17-42, *supra* note 152, at 4-5.
- 159 *Id.* at 9.
- 160 Jill Gross, *The Improbable Birth and Conceivable Death of the Securities Arbitration Clinic*, 15 *Cardozo J. Conflict Resol.* 597, 598 (2014).
- 161 See FINRA, FINAL REP. AND RECOMMENDATIONS OF THE FINRA DISP. RESOL. TASK FORCE 52 (Dec. 16, 2015), <https://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf> [hereinafter FINAL REPORT].
- 162 SEC, Press Release, SEC Announces Pilot Securities Arbitration Clinic to Help Small Investors—Levitt Responds to Concerns Voiced at Town Meetings, 97-101 (Nov. 12, 1997), <https://www.sec.gov/news/press/pressarchive/1997/97-101.txt>.
- 163 OFFICE OF THE NEW YORK STATE ATTORNEY GENERAL, Press Release, *Former Telecom Executive Agrees to Turn Over IPO Profits* (Dec. 4, 2003), <https://ag.ny.gov/press-release/former-telecom-executive-agrees-turn-over-ipo-profits>.
- 164 UNIV. OF PITTSBURGH, Press Release, *Pitt Law School to Open Securities Arbitration Clinic* (May 2, 2011), <http://www.news.pitt.edu/news/pitt-law-school-open-securities-arbitration-clinic>.
- 165 See *Report on Objectives, Fiscal Year 2018, supra* note 15, at 23-24.
- 166 See FINRA INVESTOR EDUCATION FOUNDATION, Press Release, *FINRA Foundation Announces \$1 Million in Grants to Fund Securities Advocacy Clinics* (Jan. 28, 2010), <http://www.finra.org/newsroom/2010/finra-foundation-announces-1-million-grants-fund-securities-advocacy-clinics>; see also Gross, *supra* note 160, at 603 (“As a result of these [FINRA] grants, clinics opened at other law schools such as Florida International University, Howard University, Suffolk University, and Pepperdine in 2009; at Seton Hall University and University of Miami in 2010; and at Georgia State and Michigan State University in 2012.”). As formal clinic names vary, for purposes of this Report, all securities law, securities arbitration, and investor protection-focused clinics referenced herein are referred to as investor advocacy clinics or clinics.
- 167 From 1997 to 2012, clinics were established at the following sixteen law schools (listed in order of founding year): Pace University Law School, Fordham Law School, Brooklyn Law School, Buffalo Law School, Duquesne School of Law, University of San Francisco School of Law, Albany Law School, Cardozo Law School, Syracuse University College of Law, St. John’s University School of Law, Touro Law Center, New York Law School, Northwestern University School of Law, Hofstra School of Law, Cornell University School of Law, and University of Pittsburgh School of Law. From 2009 to 2012, clinics were opened at an additional eight law school using Foundation start up grants: Florida International University School of Law, Howard University School of Law, Suffolk University School of Law, Pepperdine

- University School of Law, Seton Hall University School of Law, University of Miami School of Law, Georgia State University School of Law, and Michigan State University School of Law. Gross, *supra* note 160, at 602-03. UNLV William S. Boyd School of Law formally opened its clinic in the spring semester of 2018.
- 168 Gross, *supra* note 160, at 619.
- 169 There are currently seventeen clinics in operation: eight located in New York (Brooklyn, Cardozo, Cornell, Fordham, New York Law School, Pace, St. John's, and Syracuse), two in California (Pepperdine and University of San Francisco), and one each in the District of Columbia (Howard), Florida (University of Miami), Georgia (Georgia State), Illinois (Northwestern), Nevada (UNLV), New Jersey (Seton Hall), and Pennsylvania (University of Pittsburgh). Clinic programs at the following law schools have closed: Albany Law School, Buffalo Law School, Duquesne School of Law, Florida International University College of Law, Hofstra School of Law, Michigan State University School of Law, and Suffolk University School of Law.
- 170 FINAL REPORT, *supra* note 161, at 52.
- 171 *Id.*
- 172 Gross, *supra* note 160, at 599.
- 173 *See id.* at 601.
- 174 SEC, Press Release, SEC Announces Pilot Securities Arbitration Clinic to Help Small Investors—Levitt Responds to Concerns Voiced at Town Meetings, 97-101 (Nov. 12, 1997), <https://www.sec.gov/news/press/pressarchive/1997/97-101.txt> (quoting Chairman Levitt).
- 175 *Id.*
- 176 The Ombudsman listed the LSCOP as part of the fiscal year 2017 Outreach and Engagement. *See Report on Objectives, Fiscal Year 2017*, *supra* note 46, at 26.
- 177 As of February 2018, securities arbitration and investor advocacy clinics exist at the following sixteen law schools: Benjamin N. Cardozo School of Law, Cornell Law School, Fordham University School of Law, Georgia State University College of Law, Howard University School of Law, New York Law School, Northwestern Pritzker School of Law, Pace University Elisabeth Haub School of Law, Pepperdine University School of Law, Seton Hall University School of Law, St. John's University School of Law, Syracuse University College of Law, University of Miami School of Law, University of Pittsburgh School of Law, University of San Francisco School of Law, and UNLV William S. Boyd School of Law. *See PACE INVESTOR RIGHTS CLINIC, INVESTOR'S GUIDE TO SECURITIES INDUSTRY DISPUTES, HOW TO PREVENT AND RESOLVE DISPUTES WITH YOUR BROKER 10* (Jill I. Gross & Elissa Germaine eds., 2017). UNLV William S. Boyd School of Law formally opened its clinic in the spring semester of 2018 after the publication of the Investor's Guide. Brooklyn Law School maintains an investor advocacy clinic with a unique structure—it is unclear if the clinic is currently active.
- 178 *See generally* Meeting with Elissa Germaine, Dir., and Jill Gross, Dir., Pace Univ. Sch. of Law, Investor Rights Clinic, in White Plains, N.Y. (Oct. 19, 2016); Meeting with Teresa J. Verges, Dir., and Scott A. Eichhorn, Supervising Attorney, Univ. of Miami Sch. of Law, Investor Rights Clinic, in Coral Gables, Fla. (Oct. 20, 2016); Meeting with David White, Founding Dir., Seton Hall Univ. Sch. of Law, Investor Advocacy Project, in Washington, D.C. (Aug. 2, 2017); Meeting with Howard S. Meyers, Instructor, New York Law School, New York Law School Legal Serv.'s, Inc., Sec. Arbitration Clinic, in New York, N.Y. (Aug. 7, 2017); Meeting with Christine Lazaro, Director, Francis "Jay" Facciolo, Assistant Dir., Ann Goldweber, Dir. of Clinical Legal Education, and Michael A. Simons, Dean, St. John's Univ. School of Law, St. Vincent De Paul Legal Program, Inc., Sec. Arbitration Clinic, in Queens, N.Y. (Aug. 7, 2017); Meeting with Alice L. Stewart, Univ. of Pittsburgh School of Law, The Sec. Arbitration Clinic, in Pittsburgh, Pa. (Aug. 8, 2017); Meeting with J. Samuel Tenenbaum, Dir., and Colleen J. Balek, Atty., Northwestern Pritzker School of Law, Bluhm Legal Clinic, Investor Protection Clinic, in Chicago, Ill. (Aug. 9, 2017); Meeting with Nicole Iannarone, Dir. and Assistant Clinical Professor, Georgia State Univ. College of Law, Investor Advocacy Clinic, in Atlanta, Ga. (Aug. 10, 2017); Meeting with Bruce Sanders, Supervising Attorney, and Cheryl Nichols, Associate Professor of Law, Howard University School of Law, Investor Justice and Education Clinic, in Washington, D.C. (Aug. 24, 2017); Meeting with Gary Pieples, Dir., Syracuse Univ. College of Law, Sec. Arbitration and Consumer Law Clinic, in Syracuse, N.Y. (Aug. 28, 2017); Meeting with William A. Jacobson, Dir., Cornell Univ. School of Law, Sec. Law Clinic, in Ithaca, N.Y. (Aug. 29, 2017); Meeting with Elizabeth Goldman, Dir., Yeshiva Univ., Benjamin N. Cardozo School of Law, Cardozo Sec. Arbitration Clinic, in New York, N.Y. (Sept. 14, 2017); *Report on Activities, Fiscal Year 2017*, *supra* note 147, at 32-34.
- 179 SEC, *Recommendation of the Investor Advisory Committee: Financial Support for Law School Clinics that Support Investors* (Mar. 8, 2018), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/law-clinics-recommendation.pdf> [hereinafter *Recommendation of the Investor Advisory Committee: Financial Support for Law School Clinics that Support Investors*].
- 180 *Id.*
- 181 *Id.*
- 182 *Id.* at 7-8. The Investor Protection Fund "shall be available to the Commission, without further appropriation or fiscal year limitation, for the following purposes: (A) Paying awards to whistleblowers as

- provided in subsection (a). (B) Funding investor education initiatives designed to help investors protect themselves against securities fraud or other violations of the securities laws, or the rules and regulations thereunder.” H.R. REP. NO. 111-687 (2009).
- 183 See FINRA, Special Notice: Engagement Initiative, (Mar. 21, 2017), [http://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Special-Notice-032117.pdf](http://www.finra.org/sites/default/files/notice_doc_file_ref/Special-Notice-032117.pdf).
- 184 Comment Letter, CENTER FOR CLINICAL PROGRAMS, RE: FINRA Special Notice: Engagement Initiative Dated March 21, 2017 at 8 (June 19, 2017), [https://www.finra.org/sites/default/files/notice\\_comment\\_file\\_ref/SN-32117\\_GSU\\_comment.pdf](https://www.finra.org/sites/default/files/notice_comment_file_ref/SN-32117_GSU_comment.pdf).
- 185 *Report on Objectives, Fiscal Year 2018*, *supra* note 15, at 24; *Report on Activities, Fiscal Year 2017*, *supra* note 147, at 32-34.
- 186 Prepared Remarks of Nicole Iannarone, Assistant Clinical Professor and Director, Investor Advocacy Clinic, Georgia State University College of Law (Oct. 12, 2017) <https://www.sec.gov/spotlight/investor-advisory-committee-2012/nicole-iannarone-remarks-iac-101217.pdf>; Prepared Remarks of Qudsia Shafiq, Student Attorney, Investor Advocacy Clinic, Georgia State University College of Law (Oct. 12, 2017) <https://www.sec.gov/spotlight/investor-advisory-committee-2012/qudsia-shafiq-remarks-iac-101217.pdf>; Prepared Remarks of David M. White, Director, Investor Advocacy Project, Seton Hall University School of Law (Oct. 12, 2017) <https://www.sec.gov/spotlight/investor-advisory-committee-2012/david-white-remarks-iac-101217.pdf>. The Investor Advocate, the Ombudsman, and the Office are extremely appreciative of the time and effort extended by the clinics to help us further understand and address important issues faced by retail investors, particularly those with smaller claims and lack of access to legal representation and resources.
- 187 Currently, securities arbitration and investor advocacy clinics exist at the following sixteen law schools: Benjamin N. Cardozo School of Law, Cornell Law School, Fordham University School of Law, Georgia State University College of Law, Howard University School of Law, New York Law School, Northwestern Pritzker School of Law, Pace University Elisabeth Haub School of Law, Pepperdine University School of Law, Seton Hall University School of Law, St. John’s University School of Law, Syracuse University College of Law, University of Miami School of Law, University of Pittsburgh School of Law, University of San Francisco School of Law, and UNLV William S. Boyd School of Law.
- 188 *Recommendation of the Investor Advisory Committee: Financial Support for Law School Clinics that Support Investors*, *supra* note 179.
- 189 Exchange Act § 39(a), 15 U.S.C. § 78pp(a).
- 190 *Id.*
- 191 Exchange Act § 39(a)(2)(B), 15 U.S.C. § 78pp(a)(2)(B).
- 192 Exchange Act § 39(g), 15 U.S.C. § 78pp(g).
- 193 Exchange Act § 39(h), 15 U.S.C. § 78pp(h).
- 194 According to Exchange Act § 4(g)(6)(B)(ii), 15 U.S.C. § 78d(g)(6)(B)(ii), a Report on Activities must include several enumerated items, and it may include “any other information, as determined appropriate by the Investor Advocate.” Exchange Act § 4(g)(6)(B)(ii), 15 U.S.C. § 78d(g)(6)(B)(ii).
- 195 SEC, *Recommendation of the Investor Advisory Committee: Crowdfunding Regulations* (Apr. 10, 2014), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/investment-adviser-crowdfunding-recommendation.pdf>; SEC, Final Rule, Crowdfunding, Securities Act Release No. 9974, 80 FR 71,387 (Nov. 16, 2015); see *Report on Objectives, Fiscal Year 2017*, *supra* note 46 for an analysis of how the final rules correspond with the IAC recommendations.
- 196 SEC, *Recommendation of the Investor Advisory Committee: Shortening the Trade Settlement Cycle in U.S. Financial Markets* (Feb. 12, 2015), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/settlement-cycle-recommendation-final.pdf>. See also SEC, Press Release, SEC Adopts T+2 Settlement Cycle for Securities Transactions, 2017-68 (Mar. 22, 2017), <https://www.sec.gov/news/press-release/2017-68-0>; Securities Transaction Settlement Cycle, Exchange Act Release No. 80295, 82 Fed. Reg. 15,564 (Mar. 29, 2017).
- 197 See SEC, *Recommendation of the Investor Advisory Committee: Legislation to Fund Investment Adviser Examinations* (Nov. 22, 2013), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/investment-adviser-examinations-recommendation-2013.pdf>.
- 198 17 C.F.R. §§ 200.735-3(b)(2)(i), 230.122 (2014); Exchange Act § 24(b), 15 U.S.C. § 78x; 5 U.S.C. § 552a(i)(1); SECR18-2, Section 8.5 (Nonpublic Information) (July 31, 2005).
- 199 *Recommendation of the Investor Advisory Committee: Financial Support for Law School Clinics that Support Investors*, *supra* note 179.
- 200 SEC, *Recommendation of the Investor Advisory Committee: Dual Class and Other Entrenching Governance Structures in Public Companies* (Mar. 8, 2018), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-on-dual-class-shares.pdf>.
- 201 SEC, *Recommendation of the Investor Advisory Committee: Regarding Promotion of Electronic Delivery and Development of a Summary Disclosure Document for Delivery of Investment Company Shareholder Reports* (Dec. 7, 2017), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-promotion-of-electronic-delivery-and-development.pdf>.



- 202 Optional Internet Availability of Investment Company Shareholder Reports, Securities Act Release No. 10506, Exchange Act Release No. 83380, Investment Company Act Release No. 33115 (June 5, 2018).
- 203 *Id.*
- 204 SEC, *Recommendation of the Investor Advisory Committee to Enhance Information for Bond Market Investors* (June 7, 2016), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-enhance-information-bond-market-investors-060716.pdf>. See also MSRB, Regulatory Notice 2016-28, New Disclosure Requirements Under MSRB Rule G-15 and Prevailing Market Price Guidance Pursuant to Rule G-30 Effective May 14, 2018 (Nov. 29, 2016) <http://www.msrb.org/~media/Files/Regulatory-Notices/Announcements/2016-28.ashx> [hereinafter MSRB Notice 2016-28]; FINRA, Regulatory Notice 17-08, Pricing Disclosure in the Fixed Income Markets (Feb. 2017), [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-17-08.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-08.pdf) [hereinafter FINRA Notice 17-08].
- 205 Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, Relating to FINRA Rule 2232 (Customer Confirmations) To Require Members to Disclose Additional Pricing Information on Retail Customer Confirmations Relating to Transactions in Certain Fixed Income Securities, Exchange Act Release No. 79346, 81 Fed. Reg. 84,659 (Nov. 23, 2016); Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, to MSRB Rules G-15 and G-30 To Require Disclosure of Mark-Ups and Mark-Downs to Retail Customers on Certain Principal Transactions and To Provide Guidance on Prevailing Market Price, Exchange Act Release No. 79347, 81 Fed. Reg. 84,637 (Nov. 23, 2016).
- 206 FINRA Notice 17-08, *supra* note 204, at 1; MSRB Notice 2016-28, *supra* note 204, at 1.
- 207 SEC Announces Formation and First Members of Fixed Income Market Structure Advisory Committee, *supra* note 55.
- 208 SEC, *Recommendation of the Investor Advisory Committee Regarding Mutual Fund Cost Disclosure* (Apr. 14, 2016), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-mf-fee-disclosure-041916.pdf>.
- 209 Request for Comment on Fund Retail Investor Experience and Disclosure, Securities Act Release No. 10503, Exchange Act Release No. 83376, Investment Company Act Release No. 33113, 83 Fed. Reg. 26,891 (June 11, 2018).
- 210 *Id.*
- 211 SEC, *Recommendation of the Investor Advisory Committee: Empowering Elders and Other Investors Re: Background Checks in the Financial Markets* (July 16, 2015), [https://www.sec.gov/spotlight/investor-advisory-committee-2012/final\\_iac\\_backgroundcheck\\_recommendation\\_071615.pdf](https://www.sec.gov/spotlight/investor-advisory-committee-2012/final_iac_backgroundcheck_recommendation_071615.pdf).
- 212 SEC, Press Release, SEC Launches Additional Investor Protection Search Tool, 2018-78 (May 2, 2018), <https://www.sec.gov/news/press-release/2018-78>.
- 213 See SEC, *Recommendation of the Investor Advisory Committee: Accredited Investor Definition* (Oct. 9, 2014), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/investment-advisor-accredited-definition.pdf>.
- 214 See SEC, *Recommendation of the Investor Advisory Committee: Impartiality in the Disclosure of Preliminary Voting Results* (Oct. 9, 2014), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/impartiality-disclosure-prelim-voting-results.pdf>.
- 215 See SEC, *Recommendation of the Investor Advisory Committee Decimalization and Tick Sizes* (Jan. 31, 2014), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/investment-adviser-decimalization-recommendation.pdf>.
- 216 See SEC, *Recommendation of the Investor Advisory Committee: Broker-Dealer Fiduciary Duty* (Nov. 22, 2013), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/fiduciary-duty-recommendation-2013.pdf>.
- 217 Regulation Best Interest, *supra* note 78, at 21,574.
- 218 See SEC, *Recommendations of the Investor Advisory Committee: Regarding SEC Rulemaking to Explore Universal Proxy Ballots* (July 25, 2013), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/universal-proxy-recommendation-072613.pdf>.
- 219 See Universal Proxy, Exchange Act Release No. 79164, Investment Company Act Release No. 32339, 81 Fed. Reg. 79,122 (proposed Nov. 10, 2016).
- 220 SEC, *Recommendations of the Investor Advisory Committee Regarding the SEC and the Need for the Cost Effective Retrieval of Information by Investors* (July 25, 2013), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/data-tagging-resolution-72513.pdf>.
- 221 See the Office of the Investor Advocate's Report on Activities for Fiscal Year 2016 for a list of rulemakings that require data tagging. See SEC, Office of the Investor Advocate, *Report on Activities, Fiscal Year 2016* at 53-55, <https://www.sec.gov/advocate/reportspubs/annual-reports/sec-investor-advocate-report-on-activities-2016.pdf>.

- 222 SEC, *Recommendation of the Investor Advisory Committee: Target Date Mutual Funds* (Apr. 11, 2013), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac-recommendation-target-date-fund.pdf>.
- 223 Investment Company Advertising: Target Date Retirement Fund Names and Marketing, Securities Act Release No. 9570, Exchange Act Release No. 71861, Investment Company Act Release No. 31004, 79 Fed. Reg. 19,564 (proposed Apr. 9, 2014).
- 224 SEC, *Recommendations of the Investor Advisory Committee Regarding SEC Rulemaking to Lift the Ban on General Solicitation and Advertising in Rule 506 Offerings: Efficiently Balancing Investor Protection, Capital Formation and Market Integrity* (2012), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac-general-solicitation-advertising-recommendations.pdf>.
- 225 Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, Securities Act Release No. 9415, Exchange Act Release No. 69959, Investment Advisers Act Release No. 3624, 78 Fed. Reg. 44,771 (July 24, 2013). Disqualification of Felons and Other “Bad Actors” from Rule 506 Offerings, Securities Act Release No. 9414, 78 Fed. Reg. 44,729 (July 24, 2013). Amendments to Regulation D, Form D and Rule 156, Securities Act Release No. 9416, Exchange Act Release No. 69960, Investment Company Act Release No. 30595, 78 Fed. Reg. 44,806 (proposed July 24, 2013).





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