

Dear Commissioner:

I respectfully submit this proposal for enhancing the regulatory framework governing Registered Investment Advisors (RIAs) to better serve retail investors through comprehensive disclosure, professional standards, and accountability measures. As equity markets evolve and become increasingly complex, we have an unprecedented opportunity to strengthen investor protection while elevating the professional standards of investment advisory services.

I write as the CEO of an investment data science firm dedicated to advancing investor protection, drawing on 45 years of market experience spanning multiple market cycles. This perspective has shown me both the tremendous value that skilled investment advisors provide to their clients and the critical importance of ensuring investors have complete, transparent information to make informed decisions about their financial futures. [See Exhibit I.]

My commitment to investor protection began in 2000 when I alerted the SEC to concerning financial reporting practices at major corporations like Cisco and GE. The subsequent market corrections, including Cisco's 83.3% decline from September 2000 to October 2002, reinforced my belief that transparency and rigorous disclosure standards are essential to market integrity and investor protection. [See Exhibits II, III, IV, and V.]

### **The Opportunity: Building a More Transparent and Professional Advisory Industry**

The investment advisory industry serves millions of Americans in achieving their financial goals. To strengthen this vital service and protect investors—particularly middle-income Americans and retirees—we propose ten concrete reforms that will enhance transparency, demonstrate advisor competence, and ensure clients receive the professional-level service they deserve.

These reforms leverage modern data science capabilities to provide investors with clear, actionable information while establishing professional standards that benefit both advisors and their clients.

### **Ten Positive Reforms to Strengthen Investor Protection**

#### **1. Clear Investment Risk Classification System**

**Current Standard:** Investment accounts are generally classified by broad investment objectives (growth, income, balanced) with limited standardization across firms. Risk assessment typically relies on general questionnaires about client preferences.

**Enhancement Opportunity:** Current classifications don't provide clear risk boundaries or consistent definitions. Clients often misunderstand their portfolio's actual risk level, and advisors have wide discretion in interpreting risk categories without standardized criteria.

**Proposed Solution:** Implement a standardized risk labeling system for all client accounts: Conservative, Moderate, Growth-Oriented, or Speculative. Each category would have specific allocation guidelines and require investments to meet defined risk criteria for that classification.

#### **Benefits:**

- Investors gain immediate clarity about their portfolio's risk level
- Advisors can demonstrate appropriate asset allocation decisions with clear standards

- Enhanced accountability through transparent, standardized risk categorization
- Reduced disputes through consistent industry-wide definitions

## 2. Personalized Risk Tolerance Documentation

**Current Standard:** Risk tolerance is typically assessed through general questionnaires asking about comfort with volatility and loss scenarios, often without specific numerical parameters or action protocols.

**Enhancement Opportunity:** Current assessments are subjective and don't establish clear loss thresholds or response procedures. When losses occur, clients often claim they weren't adequately informed about downside risks, while advisors point to general risk disclosures.

**Proposed Solution:** Require written acknowledgment of maximum acceptable losses for each client (e.g., 20%), with pre-agreed action plans if thresholds are approached. This would include specific triggers for portfolio review and potential defensive actions.

### Benefits:

- Clients make quantified, informed decisions about acceptable risk levels
- Advisors have clear guidance for portfolio management during volatile periods
- Reduced potential for disputes through documented, specific risk agreements
- Enhanced fiduciary protection through explicit client consent

## 3. Historical Context Education

**Current Standard:** Risk disclosures typically include general statements about market volatility and past performance not guaranteeing future results, without specific historical context about extended loss periods.

**Enhancement Opportunity:** Clients often have unrealistic expectations about market behavior, particularly regarding the duration and severity of market downturns. General risk warnings don't convey the reality of extended periods where equity investments may underperform or lose value.

**Proposed Solution:** Provide all clients with standardized educational materials showing historical market performance, including extended periods of negative returns and comparative performance of various asset classes during different market conditions (Exhibit VI shows NASDAQ performance 2000-2016 as an example).

### Benefits:

- Investors understand realistic market behavior and potential extended loss periods
- Better-informed investment decisions based on historical precedent rather than recent performance
- Reduced unrealistic return expectations and improved long-term investment discipline
- Enhanced informed consent through comprehensive historical context

## 4. Enforcement of Stated Investment Methods and Documentation Standards

**Current Standard:** Investment advisors must disclose their methods of analysis and investment strategies in Form ADV Part 2A, Item 8 ("Methods of Analysis, Investment Strategies and Risk of Loss"). However, there is limited oversight to ensure advisors actually follow their stated methodologies when making individual investment selections. Analysis of hundreds of Form ADVs reveals that Item 8 responses typically contain generalizations that provide little value for distinguishing one advisor from another beyond broad categories like "We buy ETFs, bond funds or individual securities." More concerning, comparison of Item 8 disclosures with actual portfolio holdings (using SEC filings and WhaleWisdom.com data) reveals significant gaps between stated practices and actual implementation. For example, advisors frequently claim to be "value investors" who avoid high P/E or P/S ratios, yet their top 50 holdings often show average P/E ratios of 35 and P/S ratios of 10—directly contradicting their written disclosures. [See Exhibit VII.]

**Enhancement Opportunity:** Many advisors list sophisticated analytical methods and disciplined investment strategies in their Form ADV filings but then select investments for client portfolios that don't align with their stated approaches. Current enforcement mechanisms don't require advisors to demonstrate how individual investment decisions follow their disclosed methods, creating a significant gap between stated practice and actual implementation.

**Proposed Solution:** Strengthen enforcement of Form ADV Item 8 disclosures by requiring advisors to maintain detailed documentation showing how each investment recommendation follows their stated methods and strategies:

**Documentation Requirements:**

- Written analysis demonstrating application of the specific analytical methods disclosed in Form ADV Part 2A to each stock in a client's portfolio
- 20 quarters of fundamental trend analysis consistent with stated investment approach
- Comprehensive financial condition assessment using disclosed evaluation criteria
- Detailed valuation analysis employing the specific methodologies claimed in regulatory filings
- Clear explanation of how each selection aligns with disclosed investment strategies

**Enforcement Mechanisms:**

- Regular audits comparing actual investment selections against stated methodologies
- Requirement to update Form ADV if actual practices differ from disclosed methods
- Enhanced penalties for material discrepancies between stated and actual practices
- Client notification requirements when investment approaches deviate from filed disclosures

**Benefits:**

- Ensures advisors actually employ the sophisticated methods they claim to use
- Provides accountability for stated investment expertise and analytical capabilities
- Creates transparency between disclosed practices and actual client service delivery
- Establishes meaningful consequences for misleading or inaccurate Form ADV disclosures

- Protects clients from advisors who claim expertise they don't actually employ
- Strengthens the integrity of the advisory registration and disclosure system

## 5. Enhanced Suitability Standards for Conservative Portfolios

**Current Standard:** Suitability rules focus primarily on matching investments to client risk tolerance and timeline, without specific criteria for what constitutes appropriate investments for conservative accounts.

**Enhancement Opportunity:** Conservative investors may unknowingly receive inappropriate investments simply because they align with stated risk tolerance. Current rules don't establish minimum financial quality standards for conservative portfolios, allowing speculative investments in contrast to client objectives.

**Proposed Solution:** Establish strong disclosure requirements for advisors to indicate to clients and prospective clients the financial criteria that they use to select investments in conservative accounts. For example, an advisor might select stocks based on criteria including, but not limited to, the following:

- Strong balance sheet fundamentals (positive tangible equity, reasonable leverage)
  - For example: positive earnings in 4 of the last 5 years
- Reasonable valuation based on conservative growth assumptions
- Demonstrated business stability and predictable cash flows

It is not my intention that the SEC mandate a specific standard to which advisor stock purchases should be held. Rather, I urge the SEC to require advisors to be detailed and specific in disclosing their analysis for each stock they purchase.

**Economic Value Documentation Requirements:** Advisors must provide written forecasts of future revenues and earnings for each equity investment, demonstrating how projected performance translates to shareholder value. Such analysis must focus on the two fundamental measures of economic value creation: tangible equity growth and growth in distributable cash from income (after accounting for reinvestment requirements to sustain operations and growth) relative to current market capitalization. This requirement ensures that conservative account recommendations are based on objective and quantifiable value creation rather than speculative price appreciation.

### Benefits:

- Protects conservative investors from inappropriate speculative risk exposure
- Provides clear, objective guidelines for advisors managing low-risk portfolios
- Maintains investment flexibility while ensuring appropriate fundamental quality
- Reduces potential for unsuitable recommendations in conservative accounts

## 6. Valuation Analysis Documentation

**Current Standard:** Investment recommendations can be based on growth projections or valuation expansion expectations without requiring quantitative analysis or documentation of the assumptions underlying those projections.

**Enhancement Opportunity:** Advisors can recommend investments trading at extreme valuations without disclosing the mathematical requirements for positive returns or the probability of achieving necessary performance levels. Clients receive investments requiring unrealistic growth without understanding these requirements.

**Proposed Solution:** When recommending investments based on potential valuation expansion or requiring above-average growth, require written analysis including:

- **Specific performance metrics needed:** "This investment requires [X]% annual growth for 5 years to achieve positive returns"
- **Probability analysis:** "Based on fundamental analysis and historical precedent, the probability of achieving required performance is estimated at [X]%"
- **Historical context:** "This valuation level has historically been associated with [specific outcomes] in similar market conditions"
- **Clear classification:** "This recommendation represents [investment/speculation] based on current fundamental analysis"  
[See Exhibit VIII.]

**Benefits:**

- Demonstrates analytical basis for investment recommendations through quantified analysis
- Provides complete transparency about required performance and probability assessments
- Helps clients understand the mathematical requirements underlying investment selections
- Encourages thorough fundamental analysis and realistic return expectations

## **7. Professional Track Record Disclosure**

**Current Standard:** Investment advisors must provide general information about their business and services but are not required to provide detailed personal performance history or track records to prospective clients.

**Enhancement Opportunity:** Clients select advisors without access to comprehensive performance data, making it difficult to evaluate advisor competence. Unlike other professional services, investment advisory lacks standardized competence demonstration requirements.

**Proposed Solution:** Require all investment advisors to provide prospective clients with a comprehensive 10-year professional performance summary, including:

- Risk-adjusted returns across different market conditions
- Maximum drawdowns experienced in client portfolios
- Performance relative to appropriate benchmarks and passive alternatives
- Portfolio turnover rates and cost analysis
- Client retention statistics and reasons for departures

**Benefits:**

- Clients can evaluate advisor expertise based on actual, documented results

- Encourages advisors to maintain consistently high professional standards
- Provides transparency in advisor selection process comparable to other professions
- Creates competitive advantage for skilled advisors while protecting clients from underperformers

## **8. Clear Standards for Technical Analysis and Momentum-Based Investment Methods**

**Current Standard:** Investment advisors can employ technical analysis, momentum strategies, and trend-following methods without clear regulatory guidance on whether these approaches meet fiduciary duty standards, particularly for conservative accounts. There is no requirement to disclose the analytical limitations of these methods or their suitability for different client risk profiles.

**Enhancement Opportunity:** A significant percentage of investment advisors rely primarily on technical indicators—moving averages, RSI, momentum signals—to select investments without examining the underlying financial condition of companies. These advisors may purchase securities with no earnings history, minimal assets, or questionable business fundamentals solely because price momentum suggests potential appreciation. The SEC has not provided clear guidance on whether momentum-based selection methods alone constitute adequate analysis for fiduciary duty, particularly in conservative accounts.

**Proposed Solution:** Require the SEC to establish clear regulatory guidance distinguishing between investment analysis methods and their appropriateness for different account types:

### **Fundamental Analysis Requirements for Conservative Accounts:**

- Investments must be supported by analysis of financial condition, earnings history, and intrinsic value
- Technical analysis alone is insufficient for conservative account recommendations
- Momentum-based selections require additional fundamental justification for suitability

### **Enhanced Disclosure Requirements:**

- Advisors must clearly disclose what percentage of client portfolios consists of companies with no earnings history
- Required disclosure of how many holdings lack tangible equity or profitable operations
- Clear explanation of whether investment selections are based on fundamental analysis or price momentum
- Specific disclosure when assets derive value from market perception rather than income-producing operations

### **Analytical Method Classifications:**

- **Income-Producing Assets:** Securities backed by operational earnings, dividends, or demonstrable cash flows
- **Speculative Price-Based Positions:** Holdings selected primarily on technical indicators or momentum without fundamental support
- **Non-Productive Assets:** Investments that cannot generate operational income (used metaphorically to illustrate the principle)

**Mandatory Client Notifications:**

- "This recommendation is based on price momentum analysis without regard to company financial condition"
- "X% of your portfolio consists of companies with no established earnings history"
- "This investment selection method focuses on market trends rather than fundamental business analysis"

**Benefits:**

- Provides clear regulatory guidance on fiduciary standards for different analytical methods
- Ensures clients understand the analytical basis (or lack thereof) for their investments
- Distinguishes between fundamental investment analysis and speculative momentum trading
- Protects conservative investors from inappropriate technical-analysis-only strategies
- Requires advisors to clearly articulate their investment philosophy and methods
- Establishes accountability for investment selection methodology in fiduciary accounts

**9. Enhanced Disclosure for Non-Income-Producing Investments**

**Current Standard:** Investment advisors are not required to disclose what percentage of client portfolios consists of companies that produce no income for shareholders or have minimal earnings insufficient to support meaningful dividend distributions.

**Enhancement Opportunity:** Many investors, particularly those in conservative accounts, are unaware that significant portions of their portfolios may be invested in companies with no current earnings or earnings so minimal that even 100% distribution would generate negligible returns. Clients lack clear information about the income-producing capacity of their holdings relative to their stated investment objectives.

**Proposed Solution:** Require advisors to provide comprehensive disclosure regarding the income-producing characteristics of client portfolios:

**Income Production Disclosure Requirements:**

- Clear disclosure of what percentage of the portfolio consists of companies with no earnings history
- Specific analysis of holdings whose current earnings, if distributed entirely as dividends, would generate less than 3% annual return based on market capitalization
- Written explanation of the timeline and probability for non-earning companies to achieve meaningful income distribution capacity
- Comparative analysis showing potential returns from current holdings versus investment-grade income-producing alternatives

**Client Education Requirements:**

- Simple, understandable language explaining the income-producing capacity of each major holding

- Clear disclosure when investments are selected for potential price appreciation rather than income generation
- Explanation of the risk profile difference between speculative growth positions and income-producing alternatives

#### **Benefits:**

- Provides transparency about the actual income-generating potential of client investments
- Helps clients understand whether their portfolios align with stated income or conservative objectives
- Reduces potential misunderstanding about investment characteristics and expected returns
- Enables informed decision-making about speculative versus income-producing strategies

### **10. Mandatory Consideration and Disclosure of Investment-Grade Bond Alternatives**

**Current Standard:** Investment advisors are not required to consider or present investment-grade bond alternatives when recommending equity investments for conservative clients, despite the significant difference in advisory fees between stock and bond portfolios.

**Enhancement Opportunity:** A substantial conflict of interest exists where advisors can generate 4-5 times higher fees by recommending stock portfolios versus bond funds, even when bond investments may better serve conservative clients' objectives for capital preservation and steady returns. Many clients, particularly seniors, are unaware that high-quality bonds might better meet their needs for safety and income.

**Proposed Solution:** Establish affirmative duties for advisors when recommending equity investments for conservative accounts:

#### **Mandatory Bond Alternative Analysis:**

- Required written analysis comparing proposed equity investments with appropriate investment-grade bond alternatives
- Specific disclosure of fee differences between recommended equity strategies and bond alternatives
- Documentation explaining why equity selection is more suitable than bonds for the client's stated objectives
- For senior clients especially, clear justification of why speculative equity positions serve capital preservation goals better than high-quality, short-to-intermediate-term bonds

#### **Conflict Resolution Requirements:**

- Explicit disclosure of advisory fee differences between equity and bond recommendations
- Written client acknowledgment that they understand bond alternatives and fee implications



- Affirmative client consent when choosing higher-fee equity strategies over potentially more suitable bond alternatives
- Regular review requirements to reassess equity versus bond suitability as client circumstances change

### **Conservative Account Protections:**

- For clients with capital preservation objectives, advisors must demonstrate why equity investments with minimal income-producing capacity are preferable to investment-grade bonds
- Required disclosure when equity recommendations involve companies with earnings insufficient to support a 5% distribution relative to market capitalization
- Clear explanation of probability assessments for speculative positions achieving client objectives versus bond alternatives

### **Benefits:**

- Resolves advisor compensation conflicts in favor of client suitability
- Ensures conservative clients understand all appropriate investment alternatives
- Protects seniors and risk-averse investors from inappropriate equity exposure driven by fee considerations
- Creates accountability for equity recommendations when safer alternatives may better serve client needs
- Enhances fiduciary duty compliance by requiring consideration and disclosure to the client of **all** suitable investment options

### **Case Study: The Need for Enhanced Disclosure**

Consider NVIDIA's current \$4+ trillion market capitalization. For investors to achieve 50% returns, the company would need to reach \$6 trillion—unprecedented in market history. Statistical analysis suggests greater probability of reversion toward \$1-2 trillion valuation than continued expansion to \$5-7 trillion. [See Exhibit X.]

**Current disclosure:** General statements about market volatility and growth stock risks provide insufficient guidance for investors to properly assess investments requiring unprecedented market performance. For instance, NVIDIA's current \$4 trillion market capitalization would require extraordinary and historically unprecedented value creation to justify positive returns, particularly when compared to the reliable income streams available from AA-rated bonds. Objective financial analysis suggests significant downside risk potential, yet current disclosure standards do not require advisors to present this mathematical reality or comparative risk assessment to clients. Enhanced disclosure requirements would ensure investors receive comprehensive analysis of valuation risks and alternative investment options, enabling properly informed decision-making.

**Enhanced disclosure would include:** Specific analysis of required performance metrics, probability assessments based on historical precedent, and clear risk-reward scenarios

This example illustrates how enhanced disclosure standards would provide investors with the comprehensive information needed to make truly informed decisions.

## **Benefits for the Entire Investment Ecosystem**

### **For Investors:**

- Additional transparency in investment decision-making
- Professional-level documentation and analysis
- Clear understanding of risks and potential outcomes

### **For Investment Advisors:**

- Clear professional standards and expectations
  - Encouragement of the use of technology to enhance client performance
  - Differentiation through demonstrated competence
- [See Exhibit XI.]

### **For the Industry:**

- Enhanced credibility and public trust
- Reduced regulatory uncertainty
- Alignment with other professional service standards

### **For Markets:**

- Improved price discovery through better-informed participants
- Reduced systemic risk from misinformed investment decisions
- Enhanced overall market integrity

## **The Path Forward**

With advanced analytical tools now available and successful regulatory precedents established, the Commission has an opportunity to implement reforms that will:

1. **Enhance investor protection** through comprehensive disclosure
2. **Elevate professional standards** within the investment advisory industry
3. **Strengthen market integrity** through better-informed participant decisions
4. **Demonstrate regulatory leadership** in adapting to modern market conditions

## **Conclusion and Next Steps**

The investment advisory industry plays a crucial role in helping Americans achieve their financial goals. These proposed reforms will strengthen that role by ensuring investors have access to comprehensive, transparent information while encouraging the highest professional standards among investment advisors.

We respectfully urge the Commission to:

- **Initiate a formal rulemaking process** to consider these enhanced disclosure and professional standards
- **Engage industry stakeholders** in developing practical implementation guidelines

- **Leverage modern technology** to make comprehensive disclosure both practical and cost-effective

I am prepared to provide detailed validation data, implementation examples, and expert testimony to support this initiative. Together, we can build an investment advisory industry that truly serves the best interests of American investors through transparency, competence, and accountability.

Sincerely,

**Raymond Mullaney**

Founder and CEO

Equity Risk Sciences, Inc.

## List of Supporting Exhibits (Attached as Separate Documents)

Exhibit	Title
Exhibit I	Career Overview of Raymond Mullaney
Exhibit II	Letter from SEC Counsel Susan Mathews (Oct 5, 2000)
Exhibit III	Barron's Article by Dr. Abraham Briloff
Exhibit IV	Cisco/GE Price Collapse Timeline
Exhibit V	Merrill Lynch: Global Research Review (August 2000)
Exhibit VI	NASDAQ Returns From 2000 to 2020
Exhibit VII	The 5 Core Causes of Stock Decline and How Advisors Must Disclose Their Risk Management Approach
Exhibit VIII	Historic Price Collapses of Leading Stocks: MSFT, AMZN (1999–2010)
Exhibit IX	25 Years of Predictive Power: A 25-Year Comparative Quantitative Study of ERS's Loss Indicator™ (LI™) and 4 Dimensions of Risk™ (4D™)
Exhibit X	NVIDIA Valuation Analysis - Evidence of Systematic Investor Protection Failure
Exhibit XI	Questions of Fact About BUY Stock Ratings from Investment Analysts