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We're All Capitalist Now: The Importance, Nature, Provision and Regulation of Investor Education

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WE'RE ALL CAPITALISTS NOW: THE IMPORTANCE, NATURE, PROVISION AND REGULATION OF INVESTOR EDUCATION

James A. Fanto[†]

ABSTRACT

The Article studies investor education so as to evaluate and guide increasing educational efforts. It first discusses the conditions that have made investor education important in the United States. The Article then presents a theoretical framework that identifies three kinds of investor education—education about saving, investing and financial fraud. In considering the parties best competent to provide them, the Article suggests that families might accomplish each kind of investor education, with schools also offering, as many now do, general financial education. Consumer financial services and nonprofit firms, moreover, should conduct—and do, in fact, provide—saving and investing education as initial or “continuing” investor training. Federal and state regulators of financial services should, therefore, focus their tasks on educating consumers about financial fraud and abuse, persuading them to save, invest and use available educational products and services and on conveying basic saving and investing norms. As an application of the theoretical perspective, the Article analyzes the major investor educational initiatives of the Securities and Exchange Commission (“SEC”). The SEC should improve its

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educational efforts by redirecting them, in accordance with the Article's guidance, to concentrate on anti-fraud education, to reinforce the basic norms and to promote and facilitate private investor education.

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I. INTRODUCTION

Parents with young children may occasionally find themselves watching *Mary Poppins*.¹ At one point in that movie, the father, appropriately named Mr. Banks, takes his two young children, Jane and Michael, on an outing to his place of employment, a well-established British merchant bank in London, intending to counter the imagina-

¹ (Walt Disney 1964).

tive influence of Mary Poppins with a healthy dose of reality. Michael wants to spend his savings of two pence on a bag of bird feed sold by an old woman who sits on the steps of St. Paul's Cathedral. Mr. Banks disallows this wasteful spending and leads the two children into the bank, where the bank's partners, particularly its managing partner, the "elder Mr. Dawes" (played by Dick Van Dyke), confront them. Assisted by Mr. Banks, the partners give the children a musical lesson on saving and investing. Yet Michael's vocal refusal to follow their advice and invest his "tuppence" in the bank creates a panic among the bank's customers that results in a run on, and closure of, the bank and in the temporary loss of Mr. Banks' job.

The scene is a good introduction to the subject of this Article, investor education, for it portrays a flawed educational attempt. Without investor education there would likely be no investment in all of the productive ventures enumerated in the partners' song. The education must be properly conducted, however. The partners become so carried away with their love of finance that they scare² and bewilder Michael with incomprehensible terms, such as "self-amortizing notes." It is no surprise, then, that Michael refuses to part with his money, especially when, in a beautiful song, Mary Poppins has encouraged him to spend it on bird feed. If, as is the case here, education is poorly done, it not only discourages investing, but, given the "herd" behavior of existing investors, it disastrously undermines capital-raising.

Investor education is important in the United States today mainly because saving and investing activities are as common as finding a job or an apartment. Saving and investing are critical for survival in our society for those who, as children years ago, first watched *Mary Poppins*. Because investing has assumed a significance in their lives that it did not generally have for their parents,³ they must be educated in how to invest. Their financial future and retirement income mainly depend upon the success of their investments, for they can no longer rely on the Social Security "safety net" that is projected to run out of funds early in the next century. Their employers are less likely to provide guaranteed retirement benefits, but more often offer them contributions to a retirement fund to be invested at the individual employee's direction. To meet their retirement and other future needs, they must also save and invest outside retirement plans. Developments in financial services, which give ordinary consumers numerous saving and investing products that will enable them to assume their new responsibilities, also require education to ensure that an individ-

² His partners refer to the elderly Mr. Dawes as a "giant in the world of finance," but all Michael understands is that Dawes is a "giant."

³ See *infra* Part II(A).

ual will understand and choose knowledgeably among the many products to design an optimal portfolio.

This kind of education means more than merely supplying a consumer with information and is, therefore, radically different from the disclosure about investment products and the companies selling them that securities law has traditionally sought to provide.⁴ Rather, it involves an intellectual *formation*, which gives consumers the conceptual framework, intellectual skills and the language: in sum, the “culture” of saving and investing that will allow them to make sense of financial information and to function intelligently in the investment world. Investor education thus raises challenges and difficulties akin to those of other kinds of education, such as identifying the appropriate educational curriculum and instructors.⁵

Economists, consumer organizations, financial firms, government regulators and even Congress and the Executive Branch have all recognized the increasing significance of investor education and are actively designing and contributing to educational programs and materials. Economists have inspired much of the educational activity with their theoretical and empirical work, suggesting that investor education can increase consumers’ savings and improve their investing performance.⁶ Consumer groups have worked with state legislatures and state and federal agencies to institute saving and investing training even in grade schools.⁷ Consumer financial services firms, whether individually, in trade groups or in self-regulatory organizations (“SROs”),⁸ provide consumers with useful educational materials and services at little or no cost.⁹ Federal financial regulators, par-

⁴ See, e.g., HOMER KRIPKE, *THE SEC AND CORPORATE DISCLOSURE: REGULATION IN SEARCH OF A PURPOSE* 73 (1979) (“[I]n recent years the SEC has insisted that the purpose of securities disclosure is to supply information for investment decisions.”).

⁵ This analysis includes the basic question about the proper role of government in education. See, e.g., OLIVER HART ET AL., *THE PROPER SCOPE OF GOVERNMENT: THEORY AND AN APPLICATION TO PRISONS* 46-47 (National Bureau of Econ. Research Working Paper No. 5744, 1996) (discussing the pros and cons of voucher arrangements).

⁶ See, e.g., B. DOUGLAS BERNHEIM & DANIEL M. GARRETT, *THE DETERMINANTS AND CONSEQUENCES OF FINANCIAL EDUCATION IN THE WORKPLACE: EVIDENCE FROM A SURVEY OF HOUSEHOLDS* 19 (National Bureau of Econ. Research Working Paper No. 5667, 1996) (presenting empirical research on effects of workplace financial education); B. DOUGLAS BERNHEIM ET AL., *EDUCATION AND SAVING: THE LONG-TERM EFFECTS OF HIGH SCHOOL FINANCIAL CURRICULUM MANDATES* 3 (National Bureau of Econ. Research Working Paper No. 6085, 1997) (presenting empirical research on results of high school financial education); B. DOUGLAS BERNHEIM, *THE VANISHING NEST EGG: REFLECTIONS ON SAVING IN AMERICA* 3 (1991) [hereinafter BERNHEIM, *THE VANISHING NEST EGG*] (arguing that a public campaign designed to promote frugal behavior will exploit motives for saving).

⁷ See *infra* text accompanying note 122.

⁸ A self-regulatory organization, or “SRO,” is the term of art for the organizations of securities market participants that, under the SEC’s supervision, regulate and discipline their members. See generally JAMES D. COX ET AL., *SECURITIES REGULATION: CASES AND MATERIALS* 18-20 (2d ed. 1997).

⁹ See *infra* Part III(B)(3).

ticularly the Securities and Exchange Commission ("SEC") and banking and pension regulators, have established and sponsored educational programs for investors, often using the new Internet technology, and have proposed and adopted regulations encouraging investor education.¹⁰ Most significantly, recent federal legislation makes investor education the goal of a national campaign by federal and state government officials (including the President) and interested private parties.¹¹

Despite these major government and financial industry activities, legal scholars have generally ignored investor education.¹² This Article evaluates and seeks to help guide these important educational efforts. Part II reviews in more detail the conditions that have made investor education important and inevitable in the United States. The inability of an aging "Baby Boom" generation to rely on Social Security programs for its retirement needs, the increasing use by employers of retirement plans that place investment decision-making upon employees and the major changes in consumer financial services are specific conditions evidencing the need for investor education. Part II also argues that the American cultural emphasis on individual responsibility determines that, short of a financial cataclysm, ordinary people expect to make their own saving and investing decisions, which makes any appreciable increase in government paternalism in Social Security or pension policy unlikely. Yet the same culture generates consumers' expectations that they should receive the training and tools to become capable saving and investing decision-makers, and thus ensures that investor education must accompany consumers' increased responsibilities. Part II contends that, given the cultural situation, improving investor education as soon as possible to respond to individuals' critical need for saving and investing training makes the most pragmatic and policy sense. It admits, however, that education is not *the* solution to the saving and investing crisis, but an important response to be used in conjunction with other solutions.

¹⁰ See *infra* Parts III(B)(4), IV(A).

¹¹ See *infra* Part III(B)(4)(a).

¹² A major exception is Professor Henry Hu of the University of Texas Law School, who insightfully discusses investor education when evaluating disclosure of investment products. See Henry T.C. Hu, *Illiteracy and Intervention: Wholesale Derivatives, Retail Mutual Funds, and the Matter of Asset Class*, 84 GEO. L.J. 2319, 2358-79 (1996) (observing that mutual fund disclosure includes a discussion of the attributes of the *class* of investments to which the fund belongs and thus leads to issues of investor education); see also Jeffrey N. Gordon, *Employees, Pensions, and the New Economic Order*, 97 COLUM. L. REV. 1519, 1565 n.148 (1997) (mentioning education in passing); cf. Gregory S. Alexander, *Pensions and Passivity*, LAW & CONTEMP. PROBS., Winter 1993, at 111, 130 (arguing that giving pension beneficiaries more decision-making may enhance individual responsibility); Deborah M. Weiss & Marc A. Sgaralino, *Prudent Risks for Anxious Workers*, 1996 WIS. L. REV. 1175, 1212-14 (advocating a "mild sort of paternalism" whereby employees can make investment choices among alternatives that are appropriately diversified to eliminate nonsystematic risk).

A serious inquiry on investor education requires a theoretical framework that establishes the kinds of investor education and the parties "best" suited to accomplish them. Part III identifies and examines three kinds of investor education: education about saving, investing and financial fraud. The first kind essentially involves acquiring an understanding of the need to defer present consumption to meet future goals (in Judge Posner's terms, to act responsibly towards one's future "selves"¹³), of the psychological impediments to saving optimally and of the best available means of achieving deferred consumption. The second kind of investor education basically concerns optimal wealth creation through investing. Because this subject is at the heart of finance, Part III relies upon finance theory to describe this kind of education, which includes training about securities markets, investment products, financial professionals, the language of finance, investing strategy and, again, psychological impediments to optimal investing. Investor education about financial fraud complements the other two kinds of investor education, because it teaches consumers to recognize and resist any fraud and abuse threatening them in the financial world.

Part III identifies the parties, or combination of parties, who should conduct each kind of education. It observes that families would best accomplish all investor education since they can inculcate individuals in the "culture of investing" from an early age. Because there is no assurance that every family can and will adequately perform this task, schools should complement family training by offering general saving and investing education. This education has, in fact, become part of the high school curriculum in many states and uses local and federal government, consumer organization and financial industry resources.¹⁴ Since not every state requires, or, in the near future, will likely require, this education and since, in any event, consumers need "continuing" investor education, this Part argues that financial services firms, as well as for-profit and nonprofit organizations in the financial information industry, should also conduct saving and investing education. They are appropriate education providers both because these kinds of education have become a commodity and because, as empirical evidence demonstrates, firms in the highly competitive consumer financial services market will supply educational services and products at low cost to attract and keep customers. Part III concludes that, in light of this market activity, federal and state regulators of financial services should accomplish two important educational tasks for which they are well suited: (i) to educate con-

¹³ See RICHARD A. POSNER, *AGING AND OLD AGE* 84 (1995) ("The idea that the individual can be modeled as a locus of competing selves (simultaneous or successive) is not new, but it remains esoteric and is disregarded in most economic analysis.") (footnote omitted).

¹⁴ See *infra* Part III(B)(2).

sumers on financial fraud and abuse (the third kind of investor education), including any abuse in private market educational efforts, and (ii) to persuade and encourage consumers to save, invest and use the investor education products and services of private firms, as well as to give them some basic tools and guidelines for these activities.¹⁵

As an application of this theoretical perspective, Part IV analyzes the major investor education initiatives of the SEC, one of the federal agencies most active in this area. It observes that, while the SEC's educational efforts have been useful, it could greatly improve them by redirecting its activities, in accordance with the Article's guidance, to concentrate on anti-fraud education and to encourage consumers to look to the education supplied by private firms, including nonprofit organizations. The SEC's Office of Investor Education and Assistance now educates consumers to guard against fraudulent and abusive practices in financial services. However, the Office's saving and investing education does not measure up to similar activities of private firms and should thus be redesigned to be part of a government campaign to encourage saving and investing, to provide consumers with a few easily-understandable rules and guidelines about these activities, and to publicize the firms' educational services. Part IV also finds that SEC initiatives to simplify securities disclosure and to design new disclosure formats for mutual funds exhibit a valuable partnership with the financial services industry. This partnership should allow consumers to receive basic information about investment products and companies in formats to which they can easily apply the saving and investing education that they receive from the financial firms. The SEC, however, should explicitly recognize the necessary relationship between the consumer-oriented disclosure and the firms' educational services, and take regulatory action to make firms link their disclosure documents to these services. Finally, the SEC should begin a sustained reflection on its role in investor education and heighten awareness of education's importance by issuing a "concept release" on investor education and inviting comment from all those involved and interested in the subject. Part V concludes by restating the need for a sustained reflection on investor education while circumstances are propitious—that is, while the stock market remains at record high levels.

¹⁵ The state and federal governments can, and should, do much to address the saving and investing crisis in the U.S., for example, by providing tax incentives to saving. *See generally* BERNHEIM, *THE VANISHING NEST EGG*, *supra* note 6, at 93-121 (discussing potential government policy options to increase rates of saving). This Article focuses, however, only on the government's role in investor education.

II. THE NEED FOR, AND CULTURAL INEVITABILITY OF, INVESTOR EDUCATION

A. *The Consequences of the Aging "Baby Boom" Generation*

Investor education has become important because individual wealth creation is critical, primarily on account of demographics.¹⁶ The numerous children born in the two decades following World War II (the "Baby Boom" generation)¹⁷ have increasing financial needs. As they begin to retire in 2010 with a longevity greater than that of their parents,¹⁸ they will require considerable financial resources. Many must now support their children's important, but expensive, education¹⁹ and may also have to take care of aging parents, who are living longer as well.²⁰ Since saving and investing performance can contribute to meeting these needs,²¹ a fundamental issue is whether individuals are intellectually, and even psychologically, equipped to save and invest optimally.²²

That Americans can not expect federal government programs to help them fully meet their retirement and other needs makes optimal individual saving and investing particularly acute. The primary gov-

¹⁶ See Peter F. Drucker, *The Future That Has Already Happened*, HARV. BUS. REV., Sept.-Oct. 1997, at 20 ("The dominant factor for business in the next two decades—absent war, pestilence, or collision with a comet—is not going to be economics or technology. It will be demographics.").

¹⁷ See Barry Bosworth, *What Economic Role for the Trust Funds?*, in SOCIAL SECURITY IN THE 21ST CENTURY 156, 156 (Eric R. Kingson & James H. Schulz eds., 1997) [hereinafter SOCIAL SECURITY] (defining the baby-boomers as those individuals born between 1945 and 1965).

¹⁸ See *id.* at 161 (citing statistics related to the increase in life-spans); see also GENERAL ACCOUNTING OFFICE, GAO/HEHS-97-81, RETIREMENT INCOME: IMPLICATIONS OF DEMOGRAPHIC TRENDS FOR SOCIAL SECURITY AND PENSION REFORM 17 (1997) [hereinafter GAO, RETIREMENT INCOME] (showing steady longevity increase since 1940 and projected increase in the future).

¹⁹ See STEVEN A. SASS, THE PROMISE OF PRIVATE PENSIONS: THE FIRST HUNDRED YEARS 250 (1997) (explaining how parents jeopardize their financial futures when they absorb their children's tuition costs). See generally JOHN E. CHUBB & TERRY M. MOE, POLITICS, MARKETS, AND AMERICA'S SCHOOLS 105-11 (1990) (observing that school success is largely determined by socioeconomic status of students' families); Simon Hakim et al., *Introduction*, in PRIVATIZING EDUCATION AND EDUCATIONAL CHOICE: CONCEPTS, PLANS, AND EXPERIENCES 4 (Simon Hakim et al. eds., 1994) (discussing expenses of public education).

²⁰ Cf. Marilyn Moon, *Are Social Security Benefits too High or too Low?*, in SOCIAL SECURITY, *supra* note 17, at 62, 71-72 (observing that the elderly's perceived improved well-being in relation to other age groups has generated a backlash).

²¹ Saving and investing also benefit investors indirectly by providing companies with sources of inexpensive capital. This capital helps firms successfully compete in global product and capital markets, and they can thus provide more jobs for investors and their children. See Michael C. Jensen, *The Modern Industrial Revolution, Exit, and the Failure of Internal Control Systems*, 48 J. FIN. 831, 850-52 (1993). An active investment market also requires a successful financial services industry. See, e.g., *The Americans Are Coming*, ECONOMIST, Apr. 15, 1995, at 23, 23-25.

²² Cf. Gordon, *supra* note 12, at 1534-36 (explaining that low growth in wages has placed additional importance on other forms of wealth creation, such as investing).

ernment social insurance program, Social Security (officially, the Old-Age, Survivors, and Disability Insurance ("OASDI") programs), was never intended to be the major source of retirement income for most people, but only a safety net for the lower-income elderly.²³ Yet the impending retirement of the "Baby Boomers" will create a deficit in funds available for OASDI payments and could even cast doubt on the continued viability of this minimum retirement amount.²⁴ Whatever solution to the projected funding deficit is adopted,²⁵ the publi-

²³ See Robert M. Ball & Thomas N. Bethell, *Bridging the Centuries: The Case for Traditional Social Security*, in SOCIAL SECURITY, *supra* note 17, at 259, 259-60 (describing the program as part of a three-pronged approach to retirement that also includes private pensions and personal savings); cf. Edward D. Berkowitz, *The Historical Development of Social Security in the United States*, in SOCIAL SECURITY, *supra* note 17, at 22, 24-25 (discussing early history of the Social Security program). In reality, Social Security payments provide most, and in some cases nearly all, of the income for the lower-income elderly. See GAO, RETIREMENT INCOME, *supra* note 18, at 24-26 (presenting statistics); Moon, *supra* note 20, at 66-67 (presenting percentages of income received from Social Security, which in the lowest-income families is more than 75%). This result is due to the redistributive nature of the program: individuals with low average earnings over their eligible working lives receive a greater percentage of these earnings as Social Security benefits than do individuals with higher average earnings. See EMPLOYEE BENEFIT RESEARCH INSTITUTE, FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS 20 (5th ed. 1997) [hereinafter FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS]. Individuals can obtain estimates about future benefits from the Social Security Administration, as well as from commercial and noncommercial services. See *id.* at 27; see, e.g., American Savings Education Council, *Ballpark Estimate* (visited Sept. 15, 1998) <<http://www.asec.org/ballpark.htm>> (providing rough estimates for different income levels).

²⁴ See Robert J. Myers, *Will Social Security Be There for Me?*, in SOCIAL SECURITY, *supra* note 17, at 208, 209-11 (summarizing various actuarial reports on date of future deficit in Social Security funds). OASDI is a pay-as-you-go program: present workers are taxed to pay for the benefits of current retirees. Social Security now collects more than it pays out and has generated a surplus that is invested in, and receives interest payments as, U.S. Treasury securities. Under current estimates, the Social Security surplus will rapidly fall in 2009 and disappear in 2012. The federal government will then have to begin repaying its loan from Social Security to make up the shortfall. Proceeds from this loan (also known as the Social Security trust funds) will be used up in 2029. See GAO, RETIREMENT INCOME, *supra* note 18, at 40-41.

²⁵ There is an ongoing national debate on the future design of Social Security. See generally Christopher Georges, *Social-Security 'Privatization' Effort Makes Headway*, WALL ST. J., June 22, 1998, at A24 (summarizing reform movements); see, e.g., GAO, RETIREMENT INCOME, *supra* note 18, at 29-41 (listing possible solutions, such as reducing initial benefits, raising retirement age, reducing cost-of-living adjustments, means-testing benefits, increasing income taxes on Social Security benefits, increasing payroll taxes, etc.); GENERAL ACCOUNTING OFFICE, GAO/AIMD/HEHS-98-74, SOCIAL SECURITY FINANCING: IMPLICATIONS OF GOVERNMENT STOCK INVESTING FOR THE TRUST FUND, THE FEDERAL BUDGET, AND THE ECONOMY 4-6 (1998) (discussing implications of shifting Social Security trust funds from government securities to stocks); NATIONAL COMM'N ON RETIREMENT POLICY, THE 21ST CENTURY RETIREMENT SECURITY PLAN 2 (1998) (summarizing its reform recommendations); Bosworth, *supra* note 17, at 164-75 (recommending that baby-boomers increase funding through higher taxes, that Social Security trust funds be removed from the federal government's budget, and that the program invest its funds in instruments other than Treasury securities); Myers, *supra* note 24, at 212-14 (describing possible solutions to the deficit problem, including increasing payroll taxes); see also RICHARD DISNEY, CAN WE AFFORD TO GROW OLDER? A PERSPECTIVE ON THE ECONOMICS OF AGING 8-9, 104 (1996) (pointing out that "pay-as-you-go" social insurance systems are premised on the unrealistic promises and assumptions that "current and future generations could maintain positive real rates of return on contributions so long as both the growth of real earnings and the growth of the population remained positive," and that there has not been the necessary population growth in America). Proposals that would change the pay-as-

cized funding problems of Social Security have caused ordinary Americans and policy-makers alike to realize that an individual must rely primarily on two other means of generating income for retirement and other future needs that primarily depend upon individual effort: pensions and individual savings.²⁶

Investor education is also required to inform the decision-maker how to participate in a retirement plan. Since the late nineteenth century, many employees have traditionally looked to their employers for retirement income,²⁷ and favorable tax treatment of pensions has encouraged employer-sponsored plans.²⁸ Yet the kinds of retirement

you-go system to individualized Social Security accounts invested in accordance with account holders' directions would further emphasize individual investing and thus investor education. See generally Gary Burtless & Barry Bosworth, *Privatizing Social Security: The Troubling Trade-Offs* (visited Sept. 15, 1998) <<http://www.brook.edu/es/policy/polbrf14.htm>>.

²⁶ See, e.g., Virginia P. Reno & Robert B. Friedland, *Strong Support But Low Confidence*, in SOCIAL SECURITY, *supra* note 17, at 178, 186-87 (discussing Americans' recent loss of confidence in Social Security and increasing dependence upon personal investments); Dallas L. Salisbury, *Public Attitudes on Social Security: The UFO Fallacy*, EMPLOYEE BENEFIT RES. INST. NOTES, March 1998, at 1, 1-3 (reviewing survey data suggesting Americans' concerns about the viability of Social Security and confusion about the program's funding problems); cf. Alan Murray, *Boomers May Not Like Social Security 'Return,'* WALL ST. J., Jan. 12, 1998, at A1 (referring to Heritage Foundation study showing declining rates of return for Social Security for younger, affluent taxpayers). Popular and scholarly doubts have also increased about the ability of federal and state governments to provide such an important service as education. See generally MILTON FRIEDMAN & ROSE FRIEDMAN, *FREE TO CHOOSE* 141 (1981) (discussing lack of confidence in public education); Jonathan B. Cleveland, *School Choice: American Elementary and Secondary Education Enter the "Adapt or Die" Environment of a Competitive Marketplace*, 29 CLEV. MARSHALL L. REV. 77, 82-85 (1995) (summarizing studies that evidence the poor academic performance of American students);

²⁷ See SASS, *supra* note 19, at 227-28 (summarizing early history of pensions designed by large businesses to attract and keep employees trained for specialized positions); see also GAO, *RETIREMENT INCOME*, *supra* note 18, at 43 (noting that 45-47% of employees in the private sector are covered by pensions, a number that remained constant from 1970 through 1993, the last date for which data is available). The economic literature explains how employee retirement benefits fit into labor management: employers use these benefits to attract and retain employees (e.g., by requiring lengths of service for the "vesting" of benefits and increasing benefits with seniority). See generally E. PHILIP DAVIS, *PENSION FUNDS: RETIREMENT-INCOME SECURITY, AND CAPITAL MARKETS: AN INTERNATIONAL PERSPECTIVE* 57 (1995) (discussing the attraction of pension funds to employees); JOHN H. LANGBEIN & BRUCE A. WOLK, *PENSION AND EMPLOYEE BENEFIT LAW* 5-16 (2d ed. 1995) (discussing history of U.S. pension plans with reference to WILLIAM C. GREENOUGH & FRANCIS P. KING, *PENSION PLANS AND PUBLIC POLICY* 27-47 (1976)).

²⁸ While taxation regarding private pension plans is complex, the tax advantages can be generally summarized as follows: "(1) within limits, employer contributions are deductible as a business expense, (2) contributions are not counted as income to participants (and therefore not subject to federal income tax) until paid in the form of benefits, and (3) investment earnings, including capital gains, are not taxed until distribution." Kelly Olsen & Jack VanDerhei, *Defined Contribution Plan Dominance Grows Across Sectors and Employer Sizes, While Mega Defined Benefit Plans Remain Strong: Where We Are and Where We Are Going*, EMPLOYEE BENEFIT RES. INST. SPECIAL REP. SR-33/ISSUE BRIEF NO. 190, Oct. 1997, at 5 n.12; see also LANGBEIN & WOLK, *supra* note 27, at 149-51; Deborah M. Weiss, *Paternalistic Pension Policy: Psychological Evidence and Economic Theory*, 58 U. CHI. L. REV. 1275, 1280-85 (1991) (noting that the tax exemption for employer-sponsored plans is the largest tax preference in the Internal Revenue Code).

plans employers are more frequently offering to their employees actually place responsibility on an individual employee to save and invest funds for retirement and other future financial needs.²⁹ In recent years, employers have perceptively shifted to offering employees "defined contribution,"³⁰ rather than "defined benefit,"³¹ pension plans. In a defined contribution plan, an employer establishes individual accounts for employees and, depending upon the kind of the plan, the employers, the employees or both make contributions to the accounts within statutorily prescribed limits.³² For many plans, an employee specifies the investment of account funds in a number of investment options permitted under the plan.³³ Upon retirement, the employee

²⁹ See SASS, *supra* note 19, at 243 (describing these plans as essentially thrift savings plans, not pension plans); Weiss & Sgaraglino, *supra* note 12, at 1177 ("The average American worker is increasingly asked to bear the risks of his own financial decisions.").

³⁰ See Olsen & VanDerhei, *supra* note 28, at 3 (pointing out that "[d]uring 1975-1993, the number of workers participating in a private [defined contribution] plan increased from 12 million to 44 million, while [defined benefit] plan participants remained roughly steady at 33-40 million"); *id.* at 22, 31 (observing that the greatest decrease in defined benefits plans occurred in small plans (with 10-24 active participants) and was partly attributable to the loss of favorable tax treatment for these plans acting as tax shelters for highly-paid persons and that the number of large defined pension plans has remained stable); see also GENERAL ACCOUNTING OFFICE, GAO/GGD-97-1, PRIVATE PENSIONS: MOST EMPLOYERS THAT OFFER PENSIONS USE DEFINED CONTRIBUTION PLANS 4-9 (1996) (presenting statistics of growth in defined contribution plans); Olivia S. Mitchell et al., *Introduction: Assessing the Challenges to the Pension System, in POSITIONING PENSIONS FOR THE TWENTY-FIRST CENTURY 1, 2-5* (Michael S. Gordon et al. eds., 1997) [hereinafter POSITIONING PENSIONS] (explaining shift to defined contribution plans).

³¹ Under a defined benefit plan, an employer provides an employee with a pension calculated in accordance with some set formula (e.g., based upon years of service and a percentage of pay). See generally FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS, *supra* note 23, at 69-70. Defined benefit plans use different formulae: some pay a flat-dollar amount for each eligible year of service, others use a percentage of pay for each eligible year or a percentage of career-average pay and still others calculate benefits as a percentage of average pay in the final employment years. See LANGBEIN & WOLK, *supra* note 27, at 44.

³² See FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS, *supra* note 23, at 57-59, 70-72; LANGBEIN & WOLK, *supra* note 27, at 46-52 (describing kinds of defined contribution plans); see also GENERAL ACCOUNTING OFFICE, GAO/GGD-98-23, PRIVATE PENSIONS: PLAN FEATURES PROVIDED BY EMPLOYERS THAT SPONSOR ONLY DEFINED CONTRIBUTION PLANS 11-18 (1997) [hereinafter GAO, PLAN FEATURES] (describing contribution features of a subset of defined contribution plans). A well-known defined contribution plan is that pursuant to Section 401(k) of the Internal Revenue Code, in which an employee can defer, on a pre-tax basis, a portion of her compensation as a contribution to an individual retirement account and receive a matching contribution from an employer (generally, a percentage of an employee's earnings), at the employer's option. See FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS, *supra* note 23, at 96-97 (summarizing "nondiscrimination" rules under which plans lose their favorable tax treatment if they do not have adequate participation of "nonhighly compensated" employees vs. "highly compensated" employees).

³³ See LANGBEIN & WOLK, *supra* note 27, at 741-42; GAO, PLAN FEATURES, *supra* note 32, at 21-23 (presenting data on employer-directed, as opposed to participant-directed, plans). Section 404(c) of the Employee Retirement Security Act of 1974 ("ERISA"), 29 U.S.C. § 1104(c) (1974), authorizes an employer to provide a defined contribution individual account plan. The Department of Labor's regulations, see 29 C.F.R. § 2550.404c-1(b)(1)(ii), (b)(3) (1997), provide that, in such plans, an employer must offer an employee a minimum of three diversified investment alternatives with different risk and return characteristics. See generally Vickie L. Bajtelsmit & Jack L. VanDerhei, *Risk Aversion and Pension Investment Choices, in POSITIONING PENSIONS, supra* note 30, at 45, 50-56 (discussing investment decision-making by

receives the proceeds of the account's investment performance.³⁴ Although defined benefit plans protect employees better against some retirement risks,³⁵ employers prefer the defined contribution plans for numerous reasons, particularly because they are less costly to administer.³⁶

Americans can satisfy their retirement and other needs through the classic third method—saving outside of Social Security and employer-sponsored pensions.³⁷ In this method, saving and investing responsibility falls almost exclusively upon an individual, which again raises the issue of education. Since government incentives to encourage saving have been, at best, mixed,³⁸ individuals should not

employees in defined contribution plans). *But see* Weiss & Sgaraglino, *supra* note 12, at 1196-97 (explaining that the Section 404(c) regulations do not require complete diversification in the finance sense of diversification within and across asset types).

³⁴ See generally FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS, *supra* note 23, at 70-71 (explaining that the benefit payable at retirement reflects employer and employee contributions and investment gains or losses).

³⁵ See Olsen & VanDerhei, *supra* note 28, at 7-8 (referring to discussion of risks in Zvi Bodie, *Pensions As Retirement Income Insurance*, J. ECON. LIT., March 1990, at 28-49). *But see* Gordon, *supra* note 12, at 1539-40 (observing that employers providing defined benefit plans captured most of the growth in invested plan assets from 1980 to 1995, since their pension obligations to employees were fixed). Other risks facing retirees include the risk that a retiree will have insufficient assets to maintain a pre-retirement standard of living and that an employer/plan sponsor will become bankrupt.

³⁶ The costs of defined benefit plans include not only the actuarial help to calculate the employer contributions needed to provide the agreed-upon benefits for retirees, but also the premium paid to a government retirement insurance fund (the Pension Benefit Guaranty Corporation) to protect employees of companies that fail to fund their pension liabilities. See Olsen & VanDerhei, *supra* note 28, at 13-14 (discussing costs); see also Ball & Bethell, *supra* note 23, at 259, 289 n.1 (attributing the decline of defined benefit plans to employer cost savings); Haim A. Mozes, *The Role of Taxes in the Shift in Emphasis from Defined Benefit Plans to Defined Contribution Plans 1* (Dec. 1997) (unpublished manuscript, on file with author) (associating declining use of defined contribution plans with decreased corporate tax rates after 1986). *But see* RICHARD A. IPPOLITO, PENSION PLANS AND EMPLOYEE PERFORMANCE: EVIDENCE, ANALYSIS, AND POLICY 85-89 (1997) (arguing that the decline of defined benefit plans owes much to the popularity of Section 401(k) plans). Yet the cost issue does not uniformly support defined contribution plans (e.g., new workers may not accrue any benefits under defined benefit plans, which is a cost advantage for these plans from an employer's perspective). Defined benefit plans, like Social Security, are "pay-as-you-go" in nature and thus favor older workers at the expense of younger workers and may thus lead employers in industries where new or younger employees are more productive to abandon such plans. See DISNEY, *supra* note 25, at 110-21 (explaining how, in defined benefit plans, older workers benefit at the expense of others, as they are given early retirement, which typically requires more contributions from younger workers). Defined contribution plans might simply be more suitable in a labor environment where highly-educated employees "rent" their services to many companies over their working lives, which means that they could not take full advantage of defined benefit plans that require several years for vesting. See SASS, *supra* note 19, at 240-41.

³⁷ See Ball & Bethell, *supra* note 23.

³⁸ See BERNHEIM, THE VANISHING NEST EGG, *supra* note 6, at 107-08, 116-17 (describing how low capital gains tax rates and favorable tax treatment of home mortgage deductions encourage consumption, rather than saving). By contrast, the favorable tax treatment of the Individual Retirement Account or "IRA" encourages saving. See FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS, *supra* note 23, at 163-71 (describing how an employee (as well as his or her spouse) not covered by a pension plan at work can make a deductible IRA contribu-

shoulder all of the blame for the low national saving rate.³⁹ Yet because individuals must rely at least partly upon income from their savings for their future needs, their present saving rate and their decisions about how to invest the saved funds are critical for their future.

Finally, as a result of the enormous changes in consumer financial services during the past several decades, financial firms offer ordinary people numerous investment products and options, which may enable people to better assume the new burdens of saving and investing and may even help cause an increased use of defined contribution plans. However, these products require financial literacy so that an individual will understand and choose knowledgeably among the many kinds of securities when designing an optimal portfolio. Individuals' investment options are not, as once was the case, merely savings deposits or a few insurance products with a saving component; brokerage services and most financial products are no longer limited to the wealthy. Because of technological developments and competition in financial services, individuals with modest financial resources can now purchase sophisticated investment products and services.⁴⁰ Most importantly, the investment company or asset management industry, which provides consumers with professional

tion). The Taxpayer Relief Act of 1997 substantially modified IRAs and established a "Roth IRA" (named after a Senate sponsor) where, depending upon an income qualification, an individual can make a nondeductible contribution to an IRA account and where accumulated earnings and distributions are not taxed, provided that funds remain in the account for a minimum period. See generally Paul Yakoboski & Bill Pierron, *IRAs: It's a Whole New Ballgame*, EMPLOYEE BENEFIT RES. INST. NOTES, Sept. 1997, at 1, 1-4. The new law facilitates (i.e., assesses no tax penalty on) withdrawals from all IRAs for special consumption purposes, such as education and first-time home purchase, which could undermine the saving incentive aspect. See, e.g., R. Glenn Hubbard & Jonathan S. Skinner, *Assessing the Effectiveness of Saving Incentives*, J. ECON. PERSP., Fall 1996, at 73, 73-90 (reviewing debate over the value and costs of saving incentives). But see James M. Poterba et al., *How Retirement Saving Programs Increase Saving*, J. ECON. PERSP., Fall 1996, at 91, 111 (concluding, on the basis of empirical data, that tax-favored accounts (IRAs and 401(k)s) do, in fact, increase saving, and do not involve a shift of savings from other investment vehicles); Eric M. Engen & William G. Gale, *Debt, Taxes, and the Effects of 401(k) Plans on Household Wealth Accumulation 28-29* (May 1997) (unpublished manuscript, on file with author) (questioning whether eligibility for 401(k) plans has in fact increased participants' wealth).

³⁹ See generally BERNHEIM, *THE VANISHING NEST EGG*, *supra* note 6, at 5-35 (describing the decline in the U.S. saving rate since 1973, the poor saving rate in comparison to those in other developed countries, and refuting arguments that such decline is illusory). See also CHRISTOPHER CONTE, *THE NATIONAL SUMMIT ON RETIREMENT SAVINGS: AGENDA BACKGROUND MATERIALS 10-11* (1998) (presenting data on contemporary saving rates); Arthur B. Kennickell et al., *Family Finances in the U.S.: Recent Evidence from the Survey of Consumer Finances*, 83 FED. RESERVE BULL. 1, 1 (Jan. 1997) (same).

⁴⁰ Cf. ROY C. SMITH & INGO WALTER, *GLOBAL BANKING 189* (1997) (describing how new technology enables financial services companies to provide their services and investments in a cost efficient manner). See generally David M. Bartholomew & Dena L. Murphy, *The Internet and Securities Regulation: What's Next?*, 25 SEC. REG. L.J. 177, 177-79 (1997) (providing a review of the effects of the internet on securities regulation); Robert A. Robertson, *Personal Investing in Cyberspace and the Federal Securities Laws*, 23 SEC. REG. L.J. 347, 362-74 (1996) (discussing benefits to investors of technology advances).

money management, has grown tremendously in the past two decades,⁴¹ and gives consumers a bewildering array of investment choices.

B. The Culture of Individual Responsibility and Education

Therefore, developments in Social Security, pensions, saving and consumer financial services all emphasize individual saving and investing responsibility and decision-making, and *could* support the need for investor education. However, different, more paternalistic, solutions to the saving and investing crisis are imaginable and may even be preferable, particularly if one is doubtful that most people could be trained to bear this responsibility. A government agency, for example, could mandate the amount an individual should save and the appropriate investment of the savings. In fact, government paternalism is manifest in Social Security and pension law, for Social Security forces individuals to put aside money for retirement (and dictates the investment of these "trust funds"), and pension and tax law generally favor pension plans that remove decision-making from employees.⁴² Although economists debate the advantages and purposes of paternalism in retirement programs, common sense suggests that it beneficially addresses the failure of individuals, for a number of understandable psychological reasons, to plan adequately for their future consumption.⁴³ A powerful argument for paternalistic pension policies is that, according to the psychological and behavioral literature, and data, people often do not act rationally in their saving and investing activities.⁴⁴

⁴¹ See Investment Company Institute, *1998 Mutual Fund Fact Book* (visited Aug. 15, 1998) <http://www.ici.org/facts.figures/factbook98_toc.html> [hereinafter *1998 Mutual Fund Fact Book*] (presenting charts illustrating such growth); see also Ingo Walter, *Global Competition and Market Access in the Securities Industry*, in INTERNATIONAL FINANCIAL MARKETS: HARMONIZATION VERSUS COMPETITION 84, 92-94 (Claude E. Barfield ed., 1996) [hereinafter INTERNATIONAL FINANCIAL MARKETS] (describing growth of investment companies and pension funds); *All Aboard*, ECONOMIST, Oct. 25, 1997, at 5, 5-10 [hereinafter *All Aboard*] (describing tremendous fund growth); *Wall Street: Giants Go Hunting*, ECONOMIST, Feb. 8, 1997, at 81, 81 (documenting investment banks' acquisitions as a way of increasing access to retail investors).

⁴² See generally Weiss, *supra* note 28, at 1279-85 (explaining that the largest tax subsidy goes to employer-sponsored pension plans where employee participation is mandatory).

⁴³ See *id.* at 1285-97 (surveying the debate among economists over paternalism); *id.* at 1297-1311 (discussing human behavior that justifies paternalism in pension policy); see also Alexander, *supra* note 12, at 134-39 (reviewing arguments justifying paternalism).

⁴⁴ See B. Douglas Bernheim et al., *What Accounts for the Variation in Retirement Wealth Among U.S. Households?* 34-35 (Sept. 1997) (unpublished draft, on file with author) (concluding that the life-cycle model of consumption can not explain data about individuals' consumption pre- and post-retirement, because individuals are often surprised by their decline in income following retirement); Gordon, *supra* note 12, at 1557-59 (discussing loss aversion and salience as psychological barriers to making high levels of equity investments); Richard H. Thaler, *Psychology and Savings Policies*, 84 AM. ECON. REV. 186, 186 (May 1994) (arguing that psychological factors cause investors to fail to perform optimal life-cycle investing). See

Constraints in American culture, however, significantly limit paternalism because the culture favors, promotes and thus determines a preference for individual responsibility and decision-making. Short of a financial cataclysm, these constraints make unlikely any appreciable increase in government paternalism in Social Security and pension policy that would significantly limit this preference. (This does not mean that there will, and should, not be significant government intervention in the saving and investing crisis that is paternalistic in nature.⁴⁵) The same culture that foregrounds individual responsibility also assumes that individuals should be educated to accept this burden. It thus ensures that investor education will inevitably accompany the new saving and investing tasks placed on Americans, particularly since these activities have become a part of ordinary life. Because investor education is, therefore, a cultural "given," scholars should consider ways of improving it, instead of focusing most of their attention on more paternalistic saving and investing policies.

It is assumed here that culture instills in each individual methods of motivating and understanding their own behavior and also that of others, while not placing them in a mental straightjacket.⁴⁶ What may be drawn from this assumption is that in American culture, individuals look to, and expect to rely upon, their own efforts for many achievements, including saving and investing success. Individuals expect that much of their financial well-being should flow from these savings and investment efforts. Because it is cultural, the "ideology" of self-help animates both the wealthy and those with limited financial resources.⁴⁷ The social- and self-understandings that the ideology generates are powerful, and thus constraining, because they have been

generally Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1477-78 (1998) (discussing data calling into question rationality of economic actors); Cass R. Sunstein, *The Future of Law and Economics: Looking Forward: Behavioral Analysis of Law*, 64 U. CHI. L. REV. 1175, 1179-92 (1997) (outlining psychological factors that can affect rationality).

⁴⁵ See, e.g., Weiss & Sgaraglino, *supra* note 12, at 1207-09 (proposing safe harbor rules for small pension plans to encourage proper diversification of pension assets).

⁴⁶ "Culture" does not explain all behavior, attitudes or viewpoints in a country, for within any given culture there are innumerable subcultures, often at odds with the dominant culture. Yet, just as nearly every human practice is to a degree conventional and made up of shared goals, routines, and procedures, so also do citizens share certain common viewpoints. See generally STANLEY FISH, *PROFESSIONAL CORRECTNESS: LITERARY STUDIES AND POLITICAL CHANGE* 82 (1995) ("Each effort only makes sense in relation to the traditions, goals, obligatory routines, and normative procedures that comprise its history and are the content of its distinctiveness . . ."); CLIFFORD GEERTZ, *THE INTERPRETATION OF CULTURES: SELECTED ESSAYS* 89 (1973) ("[culture] denotes an historically transmitted pattern of meanings embodied in symbols, a system of inherited conceptions expressed in symbolic forms by means of which men communicate, perpetuate, and develop their knowledge about and attitudes toward life.").

⁴⁷ See, e.g., FRIEDMAN & FRIEDMAN, *supra* note 26, at xv (expressing this ideology). But see ROBERT H. BORK, *SLOUCHING TOWARDS GOMORRAH: MODERN LIBERALISM AND AMERICAN DECLINE* 66-82 (1996) (arguing that current societal pressures undermine the traditional cultural emphasis upon individual responsibility).

formed in history and by earlier common experiences.⁴⁸ Yet the past alone does not determine the American cultural preference for individual responsibility, for the present reinforces it in countless ways.⁴⁹

The shared perspectives of this culture that emphasize individual responsibility do not leave individuals unaided. Rather, within the culture, individuals accept a burden as an appropriate *individual* task only if they receive a minimum of collective support and training to develop their respective talents, and to recognize and make use of opportunities, in the human activity in question.⁵⁰ The culture thus ensures that education inevitably accompanies individual growth and responsibility. Under its central and traditional justifications, education “forms” or “empowers” men and women so that they can function responsibly in our society. However, the “constraining” side of education should not be ignored. In instructing individuals how best to accomplish a given activity, education creates and reinforces the collective understanding that the activity is an individual, as opposed to social, undertaking and helps to limit the ways in which individuals engage in the activity.⁵¹

A culture that places responsibility on individuals and educates them to bear it should similarly affect Americans’ understanding of saving and investing. Yet something more is needed for these activities to fall into the familiar cultural pattern. Saving and investing must become everyday activities, similar to learning how to find a job

⁴⁸ See, e.g., MARK J. ROE, STRONG MANAGERS, WEAK OWNERS: THE POLITICAL ROOTS OF AMERICAN CORPORATE FINANCE 29-31 (1994) (citing American experiences of self-reliance and resistance to centralized government and financial power as formative elements in an American “way of thinking”); see also LOUIS D. BRANDEIS, OTHER PEOPLE’S MONEY AND HOW THE BANKERS USE IT 163 (1914) (expressing characteristic American academic hostility towards centers of financial and economic power). See generally Mark J. Roe, *Chaos and Evolution in Law and Economics*, 109 HARV. L. REV. 641, 643-44 (1996) (suggesting that certain behavior and practices are “path dependent,” or determined by historical circumstances).

⁴⁹ See, e.g., Donald C. Langevoort, *Selling Hope, Selling Risk: Some Lessons for Law from Behavioral Economics About Stockbrokers and Sophisticated Customers*, 84 CAL. L. REV. 627, 681-84 (1996) (discussing cases that impose a duty upon individuals to read information on investments that has been given to them).

⁵⁰ Cf. CHUBB & MOE, *supra* note 19, at 3-4 (discussing “scientific” progressive justification for bureaucratic control of schools); FRIEDMAN & FRIEDMAN, *supra* note 26, at 144 (“Mostly, [the establishment of the school system in the United States] simply reflected the importance that was attached by the community to the ideal of equality of opportunity.”); Cleveland, *supra* note 26, at 85-88 (noting that universal elementary and secondary education in the U.S. was the product of the Progressive Era); Lee E. Teitelbaum, *Family History and Family Law*, 1985 WIS. L. REV. 1135, 1152 (discussing influence of the Enlightenment theory upon provision and methods of education in the U.S.).

⁵¹ On the constraining side of education see, e.g., MICHEL FOUCAULT, DISCIPLINE AND PUNISH: THE BIRTH OF THE PRISON 184-92 (1979) which criticizes traditional Enlightenment justifications of education). Like all educators, those engaged in investor education must be sensitive to, and constantly question, the limitations placed upon students through education. See James A. Fanto, *Investor Education, Securities Disclosure and the Creation and Enforcement of Corporate Governance and Firm Norms*, 48 CATH. U. L. REV. (Forthcoming 1998) (manuscript at 18-20, on file with author) (discussing limiting or “reifying” aspect of education).

or housing, that nearly all members of society must undertake, and that are thus critical to one's individual and social development, survival and advancement. For all the reasons discussed earlier, particularly the transformations in retirement plans and consumer financial services, personal saving and investing have achieved this commonplace status. Individuals thus expect to depend upon their own efforts and saving and investing decisions and also feel *entitled* to investor education.

In fact, the very nature of American capitalism has made individual investing an ordinary activity, which inevitably leads to investor education. Unlike capitalism in other countries, American capitalism has always been characterized by capital market financing in which companies primarily raise funds on securities markets from dispersed investors, not privately from large financial intermediaries.⁵² In recent times, these capital markets have experienced tremendous growth because an increased number of ordinary individuals are participating in them, again often through defined contribution retirement plans.⁵³ This capitalism simply cannot grow, or exist at its present level, unless the consumer capital providers know how to participate in these markets, whether as direct investors or through collective investment vehicles, such as mutual funds.⁵⁴

Indeed, another aspect of American culture—a longstanding “Main Street” hostility to, suspicion of, and yet irresistible attraction to the dominant market capitalism typified by Wall Street—reinforces individuals' expectations of receiving investor education so that they can participate in a “game” where the deck has often been stacked against them. Historically, many ordinary citizens, politicians and intellectuals disliked Wall Street because, in their view, Wall Street

⁵² See, e.g., ROE, *supra* note 48, at 3-8; see also Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 748-73 (1997) (surveying corporate financing and governance systems).

⁵³ See NEW YORK STOCK EXCHANGE, *FACT BOOK FOR THE YEAR 1997 57-59* (1998) [hereinafter *FACT BOOK*] (discussing growth of individual stock ownership in America and observing that one in three adults owns stock directly or indirectly); Edward Wyatt, *Share of Wealth in Stock Holdings Hits 50-Year High*, N.Y. TIMES, Feb. 11, 1998, at A1 (observing that Americans have more of their funds invested in the stock market than in other assets); cf. Bartholomew & Murphy, *supra* note 40, at 177-78 (noting growth in the amount that individuals invest through the Internet).

⁵⁴ Indeed, investor education is becoming important in other countries that are moving from bank-centered capitalism to market capitalism because consumers need to be taught to save and invest if capital markets in these countries are to grow. See, e.g., AUSTRALIAN SECURITIES COMM'N & FINANCIAL PLANNING ASSOCIATION OF AUSTRALIA LTD., *DON'T KISS YOUR MONEY GOODBYE: HOW TO CHOOSE A FINANCIAL ADVISOR* (1997); SEC, *First-Ever Hemisphere-Wide Investor Education Campaign Planned* (visited Sept. 15, 1998) <<http://www.sec.gov/news/press/97-111>> (on file with author) (discussing investor education campaign to be coordinated by financial regulators throughout the Americas). This Article is part of a larger research agenda that also examines investor education outside the United States.

professionals took advantage of investors and misused their money.⁵⁵ The financial power of the investment community also potentially undermined individual initiative since financial institutions dominated many economic activities and thus eliminated areas for individual economic expression and activity.⁵⁶ Yet this suspicion of Wall Street was always coupled with an attraction to investing, the possible investment gains and to the successful investors in ways often akin to the love and hatred of gambling and gamblers.⁵⁷ From these additional cultural perspectives, investor education should correct the "educational" asymmetry between ordinary investors and Wall Street professionals to ensure that these investors could at least play the potentially valuable investing "game" better.

While it is not easy to gather empirical evidence about a concept as elusive as culture and while such evidence is not critical to establish the above argument, available data support the conclusions drawn from this general overview of American culture. For example, data suggests that Americans desire personal responsibility in investing and value investor education to improve their investing performance. Empirical studies have examined (and continue to examine) individual investing attitudes and behavior, particularly in retirement plans, with the goal of developing policies that increase personal saving activity and produce optimal investing behavior. The studies uniformly show that individuals want to control, or at least to be significantly involved in, investment decisions. Furthermore, investors want to feel that their efforts matter in their financial future.⁵⁸ More impor-

⁵⁵ See ROE, *supra* note 48, at 31-32 (discussing Populist hostility to Wall Street); JOEL SELIGMAN, *THE TRANSFORMATION OF WALL STREET: A HISTORY OF THE SECURITIES AND EXCHANGE COMMISSION AND MODERN CORPORATE FINANCE 19-38* (1982) (discussing political responses to the 1929 stock market crash); Stuart Banner, *What Causes New Securities Regulation? 300 Years of Evidence*, 75 WASH. U. L.Q. 849, 850-51 (1997) (describing popular Anglo-American hostility to speculators). *But see* YANKELOVICH PARTNERS INC., 1997 ANNUAL SIA INVESTOR SURVEY: INVESTORS' ATTITUDES TOWARDS THE SECURITIES INDUSTRY 5 (1997) (showing that, in an investor survey prepared for the Securities Industry Association, 64% of investors surveyed have a favorable view of the securities industry).

⁵⁶ See BRANDEIS, *supra* note 48, at 1-27 (positing a classic statement of hostility towards Wall Street).

⁵⁷ See ROBERT J. SHILLER, *MARKET VOLATILITY* 59 (1989) ("Investing in speculative assets clearly shares with gambling the element of play . . . The satisfaction afforded by gambling is related to the individual's ego involvement in the activity; and thus individual investors must themselves play to achieve satisfaction, and most do not rely on others for decisions."). Even business law scholars show much respect for "great" investors. *See, e.g., The Essays of Warren Buffett: Lessons for Corporate America*, 19 CARDOZO L. REV. 1 (1997) (symposium on this famous investor with a collection of his essays and contributions by over 20 well-known scholars).

⁵⁸ *See, e.g.,* CONTE, *supra* note 39, at 8-9 (citing results of U.S. Department of Labor's survey of focus groups); Arthur B. Kennickell et al., *Saving and Financial Planning: Some Findings from a Focus Group*, 8 FIN. COUNSELING & PLAN. EDUC. 4 (1997) (emphasizing "self-control" in saving and financial planning); Olsen & VanDerhei, *supra* note 28, at 32 (reviewing literature which suggests that employees favor defined contribution plans because they like the control and the choice to use retirement savings for other uses, if the need arises; "While

tantly, the studies also strongly suggest that people want and use investor education, which appears both to increase their saving rate and to make their investing decisions accord better with the financial principles.⁵⁹

retirement planning is important, many workers find saving for children's education, purchasing a home, and other consumption activities equally or more important.") (footnote omitted); Reno & Friedland, *supra* note 26, at 189 (citing survey results that individuals place more emphasis upon their own self-directed saving than Social Security in thinking about retirement funds and noting that "[p]erhaps individual discretion brings a sense of control, which leads to a sense of security and confidence"). The desire for individual control is reflected in the popularity of retirement or saving plans that permit an individual to have access, through loans or fund withdrawals, to retirement funds for other needs. See General Accounting Office, *401(k) Pension Plans: Loan Provisions Enhance Participation But May Affect Income Security for Some* (GAO/HEHS-98-5, Oct. 1997) (visited Sept. 15, 1998) <<http://www.gao.gov/Aindex/FY98/abstracts/he98005.html>> (on file with author) (presenting data suggesting that participation and contribution rates are higher in pension plans with loan provisions). Recent changes in IRAs seem to embrace this perspective since they expand the allowable reasons for withdrawing retirement funds without triggering a tax penalty. See Yakoboski & Pierron, *supra* note 38, at 4. From a cultural perspective, this empirical data is predictable: if people are "taught" that investing is an individual activity, they obviously will want to control it themselves.

⁵⁹ See, e.g., PATRICK J. BAYER ET AL., THE EFFECTS OF FINANCIAL EDUCATION IN THE WORKPLACE: EVIDENCE FROM A SURVEY OF EMPLOYERS 19 (National Bureau of Econ. Research Working Paper No. 5655, 1996) ("Retirement education—and frequent seminars in particular—positively affect the size of contributions to self-directed plans."); BERNHEIM, ET AL., EDUCATION AND SAVING, *supra* note 6, at 3 (presenting statistical research, based on survey, suggesting "strong indications that mandates [requiring financial education] not only increased exposure to financial education, but also systematically altered adult behavior by stimulating greater saving"); BERNHEIM & GARRETT, *supra* note 6, at 19 (using a database on household interviews, the authors find that employees rely heavily on financial education in the workplace, and that it affects financial choice); CONTE, *supra* note 39, at 23 (citing studies which show "employees regard financial education as an important and attractive benefit"); EMPLOYEE BENEFIT RESEARCH INSTITUTE, THE 1997 RETIREMENT CONFIDENCE SURVEY (RCS) SUMMARY OF FINDINGS 9 (1998) ("Worker education programs do appear to influence individual behavior. First, 45 percent of those using the educational material report that it led them to begin contributing to the plan. In addition, the RCS found that among users of educational material, 49 percent report that it led them to change the allocation of their money among the investment options offered, and 38 percent said that it led them to change the amount they contributed to the plan."); Deborah Milne et al., *Can We Save Enough to Retire? Participant Education in Defined Contribution Plans*, EMPLOYEE BENEFIT RES. INST. ISSUE BRIEF NO. 160, April 1995, at 1 (discussing positive results of investor education programs); Deborah Milne et al., *Participant Education: Actions and Outcomes*, EMPLOYEE BENEFIT RES. INST. ISSUE BRIEF NO. 169, Jan. 1996, at 22 (concluding that pension plan education produces positive saving and investing results and that investors like to be involved in investing decision-making); Paul Yakoboski & Jack VanDerhei, *Worker Investment Decisions: An Analysis of Large 401(k) Plan Data*, EMPLOYEE BENEFIT RES. INST. ISSUE BRIEF NO. 176, Aug. 1996, at 3 (noting a survey of employees in three major companies, AT&T, IBM and New York Life, shows that 46% of individuals reallocated money on the basis of educational materials explaining asset allocation and diversification); Zvi Bodie & Dwight B. Crane, *Personal Investing: Advice, Theory, and Evidence from a Survey of TIAA-CREF Participants 15* (May 28, 1997) (unpublished manuscript, on file with author) ("While TIAA-CREF participants are on average better informed and more experienced at making their own investment choices than the general population, our findings suggest that, given enough education, information, and experience, people will tend to manage their self-directed investment accounts in an appropriate manner."); see also YANKELOVICH PARTNERS INC., *supra* note 55, at 7 (reporting that surveyed investors desire more investor education from financial firms). But see CONTE, *supra* note 39, at 9 (discussing investors' confusion over educational materials).

Since American culture thus gives investor education an important and inevitable, but not an exclusive, role in saving and investing, scholars interested in financial markets, pension policy or related fields should analyze this education from various theoretical perspectives, compare current educational efforts with their theoretical conclusions, and propose improvements to the education. Legal scholars have particularly neglected this agenda as they have seldom examined investor education and, when they have, they have generally downplayed it,⁶⁰ preferring to focus their attention on paternalistic saving and investing policies that, at times, remove, or substantially restrict, individual decision-making.⁶¹ Although occasionally appearing to reveal an academic hostility to market-oriented solutions,⁶² these scholars believe—with considerable justification—that most consumers, with little time, few assets and well-documented psychological inhibitions to saving and investing optimally,⁶³ do not belong in the bewildering and often difficult investment world.⁶⁴ Yet economists

⁶⁰ Professor Hu, for example, gives equivocal support to investor education. *See* Hu, *supra* note 12, at 2372 (“The road ahead is less clear. Investor education, through modified disclosure requirements or otherwise, will help. But there are limits to the efficacy of education. A rethinking of the locus of investment decisionmaking is appropriate. Devising alternatives to the need for universal literacy and universal decisionmaking is essential.”); *id.* at 2377 (“Despite all of these limitations, I think that efforts at investor education and more comprehensible forms of mandated disclosure are worthwhile.”).

⁶¹ *See, e.g.*, LANGBEIN & WOLK, *supra* note 27, at 742 (supporting paternalism); Gordon, *supra* note 12, at 1566 (recommending that financial instruments allowing investors to capture the upside of market with some downside protection be added to investment options in pension plans); Hu, *supra* note 12, at 2378 (“regulatory steps that would have the effect of causing the less financially sophisticated to more seriously consider asset allocation funds do make sense to me.”); Weiss, *supra* note 28, at 1311-19 (recommending a number of paternalistic policies, including mandatory savings plans, that counter individuals’ abilities to hurt themselves in saving). *But see* Weiss & Sgaraglino, *supra* note 12, at 1212-13 (advocating a “mild sort of paternalism” whereby “pension funds should be permitted to allow workers to choose the level of rational risk they wish to bear.”).

⁶² *Cf.* RONEN SHAMIR, *MANAGING LEGAL UNCERTAINTY: ELITE LAWYERS IN THE NEW DEAL* 1-13 (1995) (observing that legal academics in the United States have been historically hostile to market solutions and private economic activity, including private law practice, and favorable to government solutions to social problems).

⁶³ *See supra* note 44.

⁶⁴ *See, e.g.*, Hu, *supra* note 12, at 2326 (“End runs around universal literacy and universal probabilistic decisionmaking are thus essential. Because of certain structural biases inherent to existing investment arrangements, such end-runs are especially likely to benefit those who are poorly educated and, educated or not, those who are simply unable to assume significant investment risks.”); Weiss, *supra* note 28, at 1300-11 (exploring the psychological difficulties facing investors). They may also simply express the despair of professors, who appreciate the difficulties of their subject matter and wonder how ordinary people can comprehend it. *See, e.g.*, Hu, *supra* note 12, at 2367-71 (discussing difficulties even the sophisticated investors face in understanding the complexities of finance); *see also* DAVIS, *supra* note 27, at 29 (observing that consumers’ inability to understand financial information is an economic justification for social security); KRIPKE, *supra* note 4, at 14 (discussing the SEC staff’s traditional view that the ordinary investor is incapable of making investment decisions by herself); Lawrence J. White, *Competition Versus Harmonization—An Overview of International Regulation of Financial Services*, in *INTERNATIONAL FINANCIAL MARKETS*, *supra* note 41, at 17-18 (explaining that paternalism in financial policy has traditionally been based on the belief that, even if ordinary individuals

and financial economists—that is, the actual finance and investment specialists—both hypothesize and *find* that financial education can help a typical consumer in her saving and investing decisions. By ignoring investor education, legal scholars are simply neglecting an important policy tool in the mix of possible solutions to the emerging saving and investing crisis.

Finally, the growing emphasis on investor education in America, while historically contingent, demands scholarly attention not because it is necessarily the preferred solution as a normative matter, although a normative argument could be made for it.⁶⁵ Rather, since it is a major cultural solution, investor education's neglect or absence can produce troubling, and potentially catastrophic, social consequences. If nearly all Americans have saving and investing responsibility and decision-making, particularly in defined contribution retirement plans, their well-being in retirement and even the assets that they pass on to their heirs will depend, if there is no organized investor education, upon such circumstances as an individual's inherent financial ability and/or the quality of her financial advisors. The significant wealth disparities in the United States, between those with and without such retirement plans, therefore, will be joined by further distinc-

receive information on investing, many of them either will not understand it, or can not invest well despite it).

⁶⁵ The argument would be that optimal saving and investing from an overall societal perspective will occur when, with an accompanying general social protection as a minimal Social Security program, individuals have a major role in making decisions regarding their own saving and investing behavior and are educated, as early as possible, as to the consequences of their choices, before circumstances inevitably "educate" them. This normative statement generally relies on the common sense observations that there exists a great range of individual preferences, attitudes, motivations and behavior and that any plan or policy to harness or modify them will inevitably fail. An eloquent statement of this normative position is the following:

Not only do we not possess such an all-inclusive scale of values: it would be impossible for any mind to comprehend the infinite variety of different needs of different people which compete for the available resources and to attach a definite weight to each. For our problem it is of minor importance whether the ends for which any person cares comprehend only his own individual needs, or whether they include the needs of his close or even those of his more distant fellows—that is, whether he is egoistic or altruistic in the ordinary senses of these words. The point which is so important is the basic fact that it is impossible for any man to survey more than a limited field, to be aware of the urgency of more than a limited number of needs. Whether his interests center [a]round his own physical needs, or whether he takes a warm interest in the welfare of every human being he knows, the ends about which he can be concerned will always be only an infinitesimal fraction of the needs of all men.

FRIEDRICH A. HAYEK, *THE ROAD TO SERFDOM* 58-59 (1944); *see also* Alexander, *supra* note 12, at 130 ("A sense of responsibility develops only when a person has the opportunity to act responsibly."); Michael C. Jensen & William H. Meckling, *The Nature of Man*, *J. APPLIED CORP. FIN.*, Summer 1994, at 5 ("Human beings are not only capable of learning about new opportunities, they also engage in resourceful, creative activities that expand their opportunities in various ways.").

tions between people who, for whatever reason, save and invest well in the plans and those who do not.⁶⁶ Providing an adequate investor education will help prevent this potential source of disparity of economic well-being. It is admittedly, however, only one solution and should not be used to foreclose others.⁶⁷ Whatever its justification or consequences, individual responsibility is with us, as is education. The difficult, but necessary questions are what kinds of investor education individuals need and who should deliver it to them.

III. A THEORETICAL FRAMEWORK

As a preliminary matter, investor education, like any education, means much more than supplying information to individuals.⁶⁸ Investor education suggests that individuals receive the cognitive and conceptual means to make sense of information and to guide their behavior.⁶⁹ Without this conceptual framework, they will not understand any information given as relevant to their activity, and their behavior will be incomprehensible to those who already possess the framework and operate within the activity. As they are educated regarding the activity, investors come to understand the relevance and importance of information and the motivations and behavior of those participating in it (e.g., what is important and what is not, how significant is some, as opposed to other, information, and what behavior

⁶⁶ I owe this observation to Professor Daniel Greenwood.

⁶⁷ Such other solutions include forcing investors to place a certain percentage of their retirement assets in particular kinds of investments. See ZVI BODIE & DWIGHT CRANE, *THE DESIGN AND PRODUCTION OF NEW RETIREMENT SAVINGS PRODUCTS* (Harvard Business School Working Paper 98-070, 1998) (proposing retirement investment products placing a "floor" on investment risk); Gordon, *supra* note 12, at 1566 (recommending that defined contribution plans include an equity portfolio with a collar); Weiss & Sgaraglino, *supra* note 12, at 1213 (requiring investment options in defined contribution plans to be adequately diversified). Moreover, education can hardly address disparities arising from levels of compensation, which allow some to save more than others, and from differences in employers' retirement plans. And it can not by itself address the wealth disparity between those who can and can not save. Investor education could at least give low-income individuals some basic saving and investing skills so that, when they have funds available for saving, they know what to do with them.

⁶⁸ Education is thus not captured well by the general economic concepts of "absence of information" and "information asymmetry" between a consumer and financial professional. Absence of information simply describes the situation in which an individual must make choices and decisions without complete information, while information asymmetry refers to transactions in which one contracting party has information that is not available to the other. See, e.g., White, *supra* note 64, at 16.

⁶⁹ See, e.g., STANLEY FISH, *IS THERE A TEXT IN THIS CLASS? THE AUTHORITY OF INTERPRETIVE COMMUNITIES* 365 (1980) (discussing literary interpretation and observing that when "we try to persuade others to our beliefs because if they believe what we believe, they will, as a consequence of those beliefs, see what we see; and the facts to which we point in order to support our interpretations will be as obvious to them as they are to us. Indeed, this is the whole of critical activity, an attempt on the part of one party to alter the beliefs of another so that the evidence cited by the first will be seen as evidence by the second") (emphasis in original).

follows from specific understandings).⁷⁰ For example, individuals need more than a definition to make sense of a "stock" or "bond," for they must learn why an enterprise raises funds in different ways and what risks different investments pose for them. Again, it is important to remember that, however designed, investor education must concentrate on imparting certain skills, at the expense of others, if it is to be successful (i.e., to help individuals to save and invest well in *this* society).⁷¹

It is also useful, for analytic purposes, to divide investor education into different categories based upon the goals or purposes—basically economic and financial⁷²—that the education should fulfill. A curricular order makes sense in learning since education about savings logically precedes education about investing. Finally, in considering who can best accomplish the different kinds of investor education, it is important to consider which party, whether a private firm or a government agency, has the incentives to, and can in fact, offer the education most effectively and in a cost efficient way. Any identification of appropriate parties must depend upon certain assumptions—which will be stated—about the motivations and functioning of private market actors and of government agencies.

A. *What is Investor Education?*

1. *Education About Saving*

Individuals must first learn to save, which means deferring present consumption of income or assets to meet later financial goals or, in economic parlance, adjusting consumption rationally over the life cycle so that savings and income from savings can replace income no longer available (or not available in sufficient amounts) from employment.⁷³ They must be taught to set, and see the usefulness in set-

⁷⁰ The Article does not discuss those who can not be educated (e.g., incapacitated or lacking decision-making ability). See generally Edward D. Berkowitz, *The Historical Development of Social Security in the United States*, in SOCIAL SECURITY, *supra* note 17, at 22, 29-36 (describing federal and state government safety nets, such as disability insurance, welfare, Medicaid, for persons who fall into the disabled or incapacitated category).

⁷¹ I argue elsewhere that investor education should move from its primarily financial focus to make ordinary individuals active, responsible owners of their investment property, which would encourage them to consider issues beyond their personal portfolio, such as the normative behavior of firms. See Fanto, *supra* note 51. Given, however, the crisis in saving and investing in the United States, educational efforts should first aim to improve an individual's saving and investing performance.

⁷² As I explain elsewhere, there are other goals, political or social, relating to saving and investing. See *id.* The primary goal of investor education, however, should be to improve the economic well-being of individuals, and these activities are primarily in the domain of economics and finance.

⁷³ Cf. Thaler, *supra* note 44, at 186-87 (arguing that psychological factors cause investors to fail to perform optimal life-cycle investing). This Article's references will be primarily to popular, or at least more accessible, finance and economic materials because its focus is on a

ting, such goals, which could include maintaining a certain lifestyle after retirement or having funds available for some specific future consumption (theirs or their children's).⁷⁴ Education about saving should convey the understanding that saving is an important way to achieve these goals because other sources of income may contribute less to future consumption, may not provide as large a return as invested savings or, for whatever reason, may simply disappear.⁷⁵

Education about saving thus changes one's conceptual framework and behavior regarding money and finances. To see saving as a way of achieving goals, a person must first understand her financial situation (income, expenses, assets and debts) and make a reasonable assessment of its likely future outlook. The consumer must then consider how to adjust this financial situation to meet these goals, which could require setting aside a certain amount of funds each month and/or limiting present consumption.⁷⁶ Saving as a method of attaining long-term goals should make a consumer think of herself (and family) as an economic unit, and regard each activity in financial or economic terms.⁷⁷ As a complementary way of viewing saving, each person should realize that she will have differing needs and resources at different times in the life cycle. An investor must anticipate these different needs and provide for these later life stages or "selves."⁷⁸

consumer's education. The following discussion of saving thus echoes standard advice given in numerous consumer guidebooks. See, e.g., DOL, TOP 10 WAYS TO BEAT THE CLOCK AND PREPARE FOR RETIREMENT (1997); National Association of Securities Dealers, Inc., *Investor Training, Taking Charge of Your Finances: Assessing Your Current Finances* (visited Sept. 15, 1998) <<http://www.nasd.com>>; National Institute for Consumer Education, *The Basics of Saving and Investing: A Teaching Guide*, at Unit 1 (visited Sept. 20, 1998) <<http://www.nasd.com>> [hereinafter, *Basics of Saving and Investing*] (providing a six-unit investment teaching guide); New York Stock Exchange, *You and The Investment World*, at 38-43 (visited Sept. 15, 1998) <<http://www.nyse.com/public/educate/6a/6aix.htm>> [hereinafter *You and The Investment World*] (presenting investors with advice on investment alternatives).

⁷⁴ An ambitious educational program on saving would also teach that saving benefits the entire economy (and thus individuals and their children) by making funds available to a country's firms, which improves the competitive position of these firms by increasing external resources for new projects. See BERNHEIM, THE VANISHING NEST EGG, *supra* note 6, at 39; *id.* at 40-43, 54-61 (describing the general dependency of domestic firms on domestic financing and risks associated with foreign financing, such as higher interest rates, under-investment in projects, and currency appreciation); see also White, *supra* note 64, at 32-33 (discussing how insufficient saving causes the demise of domestic industries in world markets and a general lack of confidence in a country's financial markets, resulting in unemployment).

⁷⁵ See, e.g., Gordon, *supra* note 12, at 1534-36.

⁷⁶ It would also involve planning for unexpected emergencies by means of insurance and emergency funds. See, e.g., AMERICAN COUNCIL OF LIFE INSURANCE, RETIREMENT SECURITY INFORMATION (1997) (describing various forms of insurance protection).

⁷⁷ Cf. CONTE, *supra* note 39, at 23-24 (suggesting that financial education about personal goals and budgeting enables employees to better understand business financial decisions).

⁷⁸ See POSNER, *supra* note 13, at 95 ("The concept [of multiple selves] can also be used—though here great caution is necessary—to justify, nonpaternalistically, the conferral of certain rights on the future self against the selfishness of the current self."); Sunstein, *supra* note 44, at 1184-86 (discussing the differences between one's prediction about a future event and one's actual experience of it); Richard H. Thaler & H.M. Shefrin, *An Economic Theory of Self-*

Education about saving should also include an explanation of the many psychological pressures that undermine willpower regarding saving, such as excessive focus on the present (“myopia”) and impulsiveness.⁷⁹ Appreciation of such pressures and of one’s own particular psychological profile regarding saving and future planning in general is critical since behavioral studies demonstrate that successful saving involves issues of will as much as intelligence.⁸⁰ The education should thus generate substantial self- and social knowledge, not only about the goals one sets but also regarding the consumption temptations to which a typical American consumer is subject.⁸¹ A person must also learn attitudes and behavior (even behavioral “tricks”) that help one resist such psychological pressures, such as placing funds to be saved in separate accounts, and thus removing them from the temptation of current consumption. Indeed, like other behavior enabling people to function on a day-to-day basis, successful saving involves following simplified, informal rules or “norms” that can be easily applied, are reinforced by others and become almost habitual.⁸²

More specifically, this kind of education would also convey a basic understanding about Social Security and the program’s func-

Control, in QUASI-RATIONAL ECONOMICS 77, 79 (1991) (assuming a “two-self” person; a “planner” who is concerned with the future and a “doer” who experiences the present). People must simply learn to imagine or anticipate their future views and needs.

⁷⁹ See Sunstein, *supra* note 44, at 1179-84 (describing pressures such as aversion to loss and to extremes of any kind, unrealistic optimism, overconfidence, etc.); Weiss, *supra* note 28, at 1297-1311 (describing pressures).

⁸⁰ See, e.g., EMPLOYEE BENEFIT RESEARCH INSTITUTE, 1998 RETIREMENT CONFIDENCE SURVEY, RETIREMENT PLANNING PERSONALITIES: FROM DENIERS TO PLANNERS 1-3 (1998) (categorizing kinds of personalities—deniers, strugglers, impulsives, cautious savers, planners, retiring savers, and their saving strategies); Thaler, *supra* note 44, at 187 (“Saving requires willpower, which humans (or at least men) have sometimes had trouble summoning since the time of Adam and Eve.”).

⁸¹ See BERNHEIM, THE VANISHING NEST EGG, *supra* note 6, at 66-92 (discussing how popular culture encourages present consumption).

⁸² See Hersh M. Shefrin & Richard H. Thaler, *The Behavioral Life-Cycle Hypothesis*, in QUASI-RATIONAL ECONOMICS, *supra* note 78, at 97 (describing usefulness of “habitual rules” in enabling individuals to resist impulses, and explaining prominence of “mental accounts,” whereby individuals divide their income and assets into various accounts, some of which they consider unavailable for current consumption); Thaler & Shefrin, *supra* note 78, at 81 (observing that people often use learned “self-imposed rules of thumb” in saving because they reduce decision-making discretion). Indeed, as part of education about saving, people should be taught to establish, at least mentally, accounts for current vs. long-term expenditures. In a sense, these rules are the informal norms that guide much human behavior. See generally Assar Lindbeck, *Incentives and Social Norms in Household Behavior*, 87 AM. ECON. REV. 370, 375-76 (1997) (discussing saving and consumption norms); Richard H. McAdams, *The Origin, Development, and Regulation of Norms*, 96 MICH. L. REV. 338, 351 (1997) (defining “norms” as obligations that are not imposed by law, but can be imposed either by decentralized groups or even throughout society); Richard A. Posner, *Social Norms and the Law: An Economic Approach*, 87 AM. ECON. REV. 365, 365 (1997) (“By ‘social norm’ (‘norm’ for short) I shall mean a rule that is neither promulgated by an official source, such as a court or a legislature, nor enforced by the threat of legal sanctions, yet is regularly complied with (otherwise it wouldn’t be a rule).” (footnote omitted)).

tioning and terms of eligibility.⁸³ The education would also help a consumer achieve an elementary understanding of tax-favored retirement saving plans, such as employer pensions, IRAs and others, as well as their availability.⁸⁴ In addition, it might train a consumer about methods available from financial institutions for non-retirement saving, such as automatic paycheck deposits or debits to accounts.

2. Education About Investing

Since a major goal of investor education is to have a consumer achieve an optimal investment portfolio, the consumer must understand how to invest well. Finance theory, which studies investment strategy, should establish this basic understanding. Like any intellectual discipline, finance presupposes a familiarity with a conceptual framework and methodology, as well as with related sciences (e.g., economics, statistics and psychology).⁸⁵ As in any rigorous intellectual pursuit, moreover, its practitioners constantly re-examine and test, empirically and conceptually, its theories and results.⁸⁶ Yet a person need not understand the nuances of the scientific debates to be conversant with or, in Professor Hu's terms, "literate" as to the basic teachings of finance. Rather, the goal of education about investing is to produce consumers who are educated about the fundamentals of investment theory, and who can knowledgeably converse with finance professionals. In sum, consumers must become part of finance's "culture" by assuming its basic conceptual framework, which establishes certain goals and methods of achieving them and thus sets simple, easily applied guidelines or "norms" for appropriate investing behavior.⁸⁷

The basics of investing—in effect, the distilled wisdom of finance—are not beyond the grasp of an investor with a high school or

⁸³ This is the kind of basic information available from the Social Security Administration. See, e.g., Social Security Administration, *Understanding Social Security* (visited Sept. 15, 1998) <<http://www.ssa.gov>>.

⁸⁴ See, e.g., Pension and Welfare Benefits Administration, *What You Should Know About Your Pension Rights* (visited Sept. 20, 1998) <<http://www.2dol.gov/dol/pwba/public/pubs/youknowtoc.htm>> (describing eligibility for pensions); DOL, WOMEN AND PENSIONS: WHAT WOMEN NEED TO KNOW AND DO (1997) (educating women about rights regarding a spouse's pension). In particular, individuals need to learn of the dangers to savings of not "rolling over" withdrawals from one retirement vehicle into another. See generally William F. Bassett et al., *How Workers Use 401(k) Plans: The Participation, Contribution, and Withdrawal Decisions 21* (1998) (unpublished manuscript, on file with author) (reporting that only 28% of workers actually rollover withdrawals from retirement plans).

⁸⁵ See, e.g., RICHARD A. BREALEY & STEWART C. MYERS, *PRINCIPLES OF CORPORATE FINANCE* xxiii (5th ed. 1996) (pointing out that it is useful, in studying finance, to understand accounting, statistics and micro-economics).

⁸⁶ See, e.g., *id.* at 992-98 (identifying "10 unsolved problems in finance").

⁸⁷ See *supra* note 82.

comparable education.⁸⁸ They are found, not only in the most advanced finance treatises, but also in numerous popular books, pamphlets and electronic media presentations prepared for the average consumer.⁸⁹ A consumer should understand elementary information about available investment products, financial markets and the role of investment professionals. The consumer, for example, should comprehend the basic differences between stocks and bonds as well as the defining features of collective investing through a mutual fund (e.g., that numerous individuals pool their funds for investing in underlying securities to take advantage of economies of scale, professional money management and diversification of investments).⁹⁰ The consumer should also become familiar with the background information about these investments, which involves instruction about public securities markets, the professionals, particularly brokers, with whom investors may deal,⁹¹ and the regulation of markets and market participants.⁹²

⁸⁸ See, e.g., Langevoort, *supra* note 49, at 650 ("Economists have frequently pointed out that structuring an efficient portfolio is not all that difficult, involving primarily a buy-and-hold (i.e., inactive) strategy with investments diversified among a set of individual securities or mutual funds."); Bodie & Crane, *supra* note 59, at 4-5 (summarizing basic investing principles). But see Hu, *supra* note 12, at 2367 (suggesting that only professionals can successfully invest); Terrance Odean, *Are Investors Reluctant to Realize Their Losses*, 53 J. FIN. 1775 (1998) (discussing data indicating that investors hold losing investments too long and sell winning investments too soon); Lynn A. Stout, *Are Stock Markets Costly Casinos? Disagreement, Market Failure, and Securities Regulation*, 81 VA. L. REV. 611, 666 (1995) [hereinafter Stout, *Costly Casinos*] (suggesting that investors are irrational optimists); Lynn A. Stout, *Technology, Transactions Costs, and Investor Welfare: Is A Motley Fool Born Every Minute?*, 75 WASH. U. L.Q. 791, 812 (1997) [hereinafter *Motley Fool*] (suggesting that investors, confused about differing sources of securities information, will engage in excessive speculation); cf. Lynn A. Stout, *How Efficient Markets Undervalue Stocks: CAPM and ECMH Under Conditions of Uncertainty and Disagreement*, 19 CARDOZO L. REV. 475, 477-84 (1997) (surveying "postmodern finance" that, according to the author, calls into question much of basic finance teaching).

⁸⁹ See, e.g., BURTON G. MALKIEL, *A RANDOM WALK DOWN WALL STREET* 229 (1996); see also *Basics of Saving and Investing*, *supra* note 73. Several law books presuppose that a law professor can teach the basics of finance to law students completely unfamiliar with the subject. See, e.g., ROBERT W. HAMILTON, *MONEY MANAGEMENT FOR LAWYERS AND CLIENTS: ESSENTIAL CONCEPTS AND APPLICATIONS* xxiii (1993) ("[The book] assumes that the reader has little or no prior experience or knowledge [of finance]."); WILLIAM A. KLEIN & JOHN C. COFFEE, JR., *BUSINESS ORGANIZATION AND FINANCE: LEGAL AND ECONOMIC PRINCIPLES* iii (6th ed. 1996) ("As our audience, we have tried to keep in mind a bright young woman or man from a family of musicians, with a college major in English, now entering a law school or a graduate school of business—on the brink of discovering, with great surprise, that the study of business can be interesting and enjoyable, as well as profitable, and that it need not be intimidating.").

⁹⁰ See, e.g., *Basics of Saving and Investing*, *supra* note 73, at Units 2, 3; MALKIEL, *supra* note 89, at 441-56.

⁹¹ See, e.g., KLEIN & COFFEE, *supra* note 89, at 380-92 (discussing securities markets); *Basics of Saving and Investing*, *supra* note 73, at Unit 2; *You and the Investment World*, *supra* note 76.

⁹² See, e.g., *Basics of Saving and Investing*, *supra* note 73, at Unit 2; *You and the Investment World*, *supra* note 76.

A consumer must comprehend elementary finance to be able to think about investing from a financial perspective. An investor should understand the time value of money, investment return and risks, liquidity, and the relationship of risk to return.⁹³ Informed by this training, an investor can understand the risks inherent in different investment products and their related returns and can learn to compare investments on these bases.⁹⁴ An investor should also be introduced to some elementary investing strategies, such as portfolio diversification, which are designed to reduce or eliminate some risks.⁹⁵ This understanding would lead to an awareness of the potential value of investing in market indices, an appreciation of the difficulties faced by financial professionals in outperforming these indices, and the potential harms of excessive speculation, including the tax consequences of securities transactions.⁹⁶ Investors, moreover, should learn to identify their personal risk preferences and appropriate investment and asset-allocation strategies for themselves and, generally, for different stages of one's life cycle. Identification of risks and strategies will ensure that, when investing, consumers design and implement an optimal portfolio for their life stage and risk aversion, and overcome

⁹³ See, e.g., *Basics of Saving and Investing*, *supra* note 73, at Unit 3; National Association of Securities Dealers, Inc., *Investor Training, Taking Charge of Your Finances: An Introduction to Investing* (visited Sept. 15, 1998) <<http://www.nasd.com>>. As Burton Malkiel explains,

Risk is the chance that expected security returns will not materialize and, in particular, that the securities you hold will fall in price.

... A security whose returns are not likely to depart much, if at all, from its average (or expected) return is said to carry little or no risk. A security whose returns from year to year are likely to be quite volatile (and for which sharp losses are typical in some years) is said to be risky.

MALKIEL, *supra* note 89, at 229.

⁹⁴ See, e.g., MALKIEL, *supra* note 89, at 366-99 (discussing basic determinants of stock and bond returns); *id.* at 321 (observing that "[e]very investor must decide the trade-off he or she is willing to make between eating well and sleeping well"); *id.* at 324-25 (presenting chart of kinds of investments keyed to ability to sleep, e.g., bank accounts correspond to "semicomatose state").

⁹⁵ Compare BREALEY & MYERS, *supra* note 85, at 154 ("Diversification works because prices of different stocks do not move exactly together. Statisticians make the same point when they say that stock price changes are less than perfectly correlated."), with *Basics of Investing*, *supra* note 73, at Unit 3 ("The process of reducing risk by spreading money among various types of investments is diversification."); and with MALKIEL, *supra* note 89, at 239 ("True diversification depends on having stocks in your portfolio that are not all dependent on the same economic variables (consumer spending, business investment, housing construction, etc.).")

⁹⁶ See, e.g., BREALEY & MYERS, *supra* note 85, at 323-46 (discussing diversification through an index investment that helps an investor eliminate risk associated with individual companies and the efficient capital markets hypothesis that emphasizes how difficult it is for portfolio managers consistently to beat market indices); MALKIEL, *supra* note 89, at 422-32 (discussing advantages of index funds). See generally Stout, *Costly Casinos*, *supra* note 88, at 696-97 (discussing the dangers of excessive stock trading). But see Paul G. Mahoney, *Is There A Cure For "Excessive" Trading?*, 81 VA. L. REV. 713 (1995) (replying to Professor Stout).

unreasonable fears of risk preventing its implementation.⁹⁷ Like education about saving, education about investing must make an investor aware of major psychological factors that can adversely affect investing decision-making (e.g., excessive fear of risk or undue optimism and grandiose expectations about investment success) and of "rules of thumb" that can help one counter them (e.g., following asset-allocation strategies, ignoring daily securities movements).⁹⁸

A cultural education on finance and investing would teach a consumer to identify, and to understand the languages of, the basic documents and texts on the activity, as well as those that enable an investor to educate herself further. The investor learns where to look for information, so that she can apply, and refine, the acquired conceptual framework, and how to read the presentation conventions of this information. Investing education thus identifies the media that provide information and training about investments, such as newspapers, magazines and Web sites.⁹⁹ It also introduces one to such conventions as the presentation of price quotations in stocks, bonds or mutual funds.¹⁰⁰ As a simple example, a consumer educated about investing should be able to read knowledgeably Section C of the *Wall Street Journal* ("Money and Investing").

Education about investing should empower an individual to invest alone and also to select and use financial professionals intelligently. Financial planners, brokers, insurance agents or mutual fund managers are individuals to whom investors may delegate some or all investment responsibility. A consumer educated about investing, for example, could evaluate whether a recommended investment is suit-

⁹⁷ See *Basics of Saving and Investing*, *supra* note 73, at Unit 3; CONTE, *supra* note 39, at 25 ("Understanding the impact of pre-retirement withdrawals is key to accumulating adequate savings for retirement."); MALKIEL, *supra* note 89, at 400-21 (discussing asset-allocation strategies for different stages of the life cycle). But see Paul A. Samuelson, *The Long-Term Case for Equities, And How It Can Be Oversold*, 21 J. PORTFOLIO MGMT. 15 (1994) (questioning accepted wisdom about long-term stock investing and asset-allocation strategies).

⁹⁸ Indeed, consumers must learn not to use their new investing knowledge in such a way as to play upon their excessive fears of risk. See CONTE, *supra* note 39, at 26. Moreover, just as saving must become habitual, so also investing must involve simple "rules of thumb" that an individual can apply almost mechanically. See, e.g., National Association of Investors Corp., *NAIC's Four Easy Investment Principles* (visited Sept. 15, 1998) <<http://www.better-investing.org>> (offering simple investing principles); cf. Shefrin & Thaler, *The Behavioral Life-Cycle Hypothesis*, *supra* note 82, at 107 ("Nearly all retirement saving is done through some routinized program.").

⁹⁹ See *Basics of Saving and Investing*, *supra* note 73, at Unit 4 (listing common sources of investment information, such as *SmartMoney*, *Money* and *The Wall Street Journal*). No list of sources of such information would be complete without a reference to the World Wide Web, where there has been a literal explosion of such resources. See, e.g., *Basics of Saving and Investing*, *supra* note 73, at Appendix (listing written and on-line materials for educating investors); Robertson, *supra* note 40, at 362-74 (discussing information sources available on the Internet).

¹⁰⁰ See *Basics of Saving and Investing*, *supra* note 73, at Unit 4 (presenting worksheets on reading stock, bond, and mutual fund quotations); *You and the Investment World*, *supra* note 73, at 22-25 (explaining how to follow investment performance).

able for her personal risk preferences and whether a suggested asset-allocation strategy fits her life-cycle stage. Similarly, an investor should be taught to monitor a financial professional so as to receive the best available “deal” for a particular kind of investment.¹⁰¹ Not only must a consumer be able literally to “speak the language” of a financial professional, but also to know something about the financial industry and its incentives. Knowledge about the kinds of investment professionals and their incentive structure (e.g., full-service vs. discount brokers, fee-only vs. fee-and-commission financial planners) is critical to enable an investor to navigate profitably among them.¹⁰² Finally, an investor should learn to recognize, and to resist, the well-documented social and personal pressures that financial professionals use in recommending investments.¹⁰³

¹⁰¹ A classic example is the decision whether to invest in mutual funds that professional money managers actively manage, or those that adopt a passive investing strategy tracking a given market index. See MALKIEL, *supra* note 89, at 422-32 (describing the benefits of index strategy); *id.* at 441-46 (discussing the question of why some money managers consistently outperform market indices). *But see* JUDITH CHEVALIER & GLENN ELISON, ARE SOME MUTUAL FUND MANAGERS BETTER THAN OTHERS? CROSS-SECTIONAL PATTERNS IN BEHAVIOR AND PERFORMANCE 4 (National Bureau of Econ. Research Working Paper No. 5852, 1996) (“The existence of funds that are expected to beat the market provides a potential justification for the effort which many consumers expend in choosing between funds rather than simply investing in indexes.”). Because of their increased investing responsibility, consumers are likely to look with more frequency to financial advisors, particularly as the value of their investment portfolios grows. See Marilyn Harris, *Time to Hunt for an Investment Pro?*, BUS. WK., May 11, 1998, at 106E2 (advice on finding a financial advisor); *Money Managers: Take My Advice*, ECONOMIST, Jan. 31, 1998, at 78 (describing the growth in investment advisory business as employees accumulate high value portfolios). Such reliance does not eliminate the need for investing education since, as in dealing with any professional, consumers are likely to receive the best service if they have enough training to monitor the advisor’s performance.

¹⁰² See, e.g., American Ass’n of Retired Persons, *Investors Age 50+ Know Little About Investment Charges, New AARP Survey Shows* (visited Sept. 15, 1998) <<http://www.aarp.org/press/1998/042398.html>> (describing survey results evidencing that a majority of the older population does not understand broker commissions); *Basics of Investing, supra* note 76, at Unit 4 (describing kinds of professionals and their incentive structure); National Association of Securities Dealers, Inc., *Investor Training, Taking Charge of Your Finances: How to Select a Broker* (visited Sept. 15, 1998) <<http://www.nasd.com>>. A consumer must understand that a broker may make an inappropriate investment recommendation because the broker personally benefits more by this recommendation or because the broker is negligent. *Cf.* COX, *supra* note 8, at 1102-10 (explaining legal rules addressing competence of financial professionals and their fiduciary obligation to ensure that recommended investments are suitable to clients); NORMAN S. POSER, *BROKER-DEALER LAW AND REGULATION 2-1 to 2-112* (2d ed. 1998) (discussing fiduciary obligations of brokers). A broker may also steer a customer towards appropriate investments that give the broker a slightly higher commission, or a proprietary mutual fund company will push its funds over those of its rivals.

¹⁰³ See generally Langevoort, *supra* note 49, at 634-69 (discussing such psychological pressures as a broker’s pressuring an investor into feeling she will lose social standing by not making a particular investment and generating a trust that causes a client to accept any investment recommendation to please the broker).

3. Education About Financial Fraud

Education about financial professionals leads to another kind of investor education that teaches individuals to avoid becoming victims of financial fraud and abuse. This kind of fraud, which has a long pedigree,¹⁰⁴ arises from dealings between those who have assimilated the investment culture and those who have not,¹⁰⁵ the ease with which financial transactions occur, the readily disposable nature of the assets at issue (e.g., cash) and the unfortunate credulity and greed of many victims.¹⁰⁶ Court cases involving financial professionals, such as unscrupulous brokers and investment advisers, provide countless examples of this kind of fraud, or even of outright theft.¹⁰⁷ Since investments can be complex and financial criminals are profit-oriented, investment fraud and abuse will continue to take new forms.

Anti-fraud education simply teaches a consumer how to recognize and avoid common forms of financial fraud and abuse.¹⁰⁸ Here, even more than in the two preceding kinds of investor education, it is important to provide individuals with simple rules or norms, similar in nature to those given to neophytes in any human activity, that they can apply without much thought. Children are warned not to talk to strangers; similarly, consumers are instructed to "hang up" the telephone whenever they hear certain selling pitches.¹⁰⁹ As further education, consumers should learn the basic features and rationale of

¹⁰⁴ See, e.g., CHARLES P. KINDLEBERGER, *MANIAS, PANICS AND CRASHES: A HISTORY OF FINANCIAL CRISES* 66-82 (3d ed. 1996) (discussing the effect of changes in the market on occurrences of financial fraud).

¹⁰⁵ Even persons sophisticated in investing fall prey to some fairly simple investment fraud. See, e.g., Steve Stecklow, *New Era's Bennett Gets 12-Year Sentence*, WALL ST. J., Sept. 23, 1997, at B15 (discussing New Era "Ponzi scheme" whereby rich individuals and institutions made contributions to a Pennsylvania organization that promised them that "wealthy benefactors" would match their funds and forward the total amount to the donors' favorite charities; needless to say, the matching benefactors did not exist).

¹⁰⁶ This is the only explanation of the startling phenomenon of people actually sending their account information to Nigerians who promise, by letter, free cash in return for use of one's bank account. See Central Bank of Nigeria, *Press Statement on Advance Fee Fraud Scam*, ECONOMIST, Sept. 13, 1997, at 25.

¹⁰⁷ See, e.g., *Thompson v. Smith Barney, Harris Upham & Co.*, 709 F.2d 1413, 1416 (11th Cir. 1983) (discussing "churning": "Churning occurs when a securities broker buys and sells securities for a customer's account, without regard to the customer's investment interests, for the purpose of generating commissions."). See generally POSER, *supra* note 102, at 3-1 to 3-126 (describing broker fraud).

¹⁰⁸ This Article does not suggest that education alone can deal with financial fraud or that it should be used to lessen the scope of the duties of financial professionals toward consumers. See generally COX, *supra* note 8, at 1082-1135 (general survey of broker regulation); POSER, *supra* note 102, at 4-1 to 4-22 (describing traditional compensatory damages available to consumers as damages against broker-dealers).

¹⁰⁹ See, e.g., *Basics of Saving and Investing*, *supra* note 73, at Unit 5 (listing abusive sales techniques and recommending consumer action—generally that consumers hang up). Indeed, hanging up the telephone is the only sensible response to many broker calls. See, e.g., Deborah Lohse, *Tricks of the Trade: 'Buffett is Buying This' and Other Sayings of the Cold-Call Crew*, WALL ST. J., June 1, 1998, at A1 (describing abusive broker sales behavior).

the kinds of investment fraud that they are most likely to encounter.¹¹⁰ They should also be taught how to prevent the kinds of fraud that unscrupulous financial professionals in reputable firms practice. Once again, instruction on the psychological pressures used by financial salespeople is important in improving one's resistance to financial fraud or abuse. Further, continuing education on saving and investing, coupled with anti-fraud training, should enable a consumer to predict the possibilities of fraud in new financial products.

B. Who Should Educate?

1. Families

Since saving is now a critical survival skill and since learning its cognitive and behavioral aspects requires constant reinforcement, the best educator is the family, however defined or constituted. That is, if the goal of all three forms of investor education is to teach easily applied habits, norms or behavioral "rules of thumb," it makes sense to look to the family, which can inculcate them in a durable way.¹¹¹ From an early age, a child can be introduced to the culture of deferred consumption through the teaching and example of other family members, and even through compelled saving behavior.¹¹² The same can be said for investing. Families can teach over the years, by example and through discussion adjusted for a young person's developing abilities, the basics of investing, investment options and materials on investing. Education against financial fraud could also be part of the young person's socialization, no different from other protective guidance given to children.

Although the above discussion may seem merely amusing to the reader, the role of the family in each kind of investor education should not be overlooked, or limited to inculcating basic saving behavior. The available empirical evidence suggests that family training produces educated investors in every sense of the term.¹¹³ While

¹¹⁰ See *Basics of Saving and Investing*, *supra* note 73, at Unit 5 (describing basic fraudulent schemes).

¹¹¹ See Thaler & Shefrin, *supra* note 78, at 85 ("The best predictors of which individuals will fall into which groups [of savers] are probably related to family background, since the family is the most likely place for the individual to learn (or not learn) the rules and norms necessary to overcome the self-control problems.") (footnote omitted); cf. Eric A. Posner, *The Regulation of Groups: The Influence of Legal and Nonlegal Sanctions on Collective Action*, 63 U. CHI. L. REV. 133, 149-50 (1996) (discussing the results on ethnic groups of the different kinds of rules used by the state to modify behavior).

¹¹² As an amusing example, one thinks of the family saving lesson remembered by Woody Allen's character in *ANNIE HALL* (United Artists 1977): "Never buy retail."

¹¹³ Some of this evidence is anecdotal. Cf. Howard Gleckman, *Generation \$ Is More Like It*, BUS. WK., Nov. 3, 1997, at 44 (discussing the increased saving rate among young adults).

giving the family an important role in investor education was questionable when few American households included investors, it is less so today when more Americans *do* and *must* invest. Moreover, because ordinary individuals have increasing access to financial information and educational materials,¹¹⁴ the family has sufficient tools to act as the primary financial educator of children.¹¹⁵ Accordingly, any governmental policy initiatives must include as a goal strengthening the family as educator of investing and provider of saving and investing norms.¹¹⁶

At present, however, it is not reasonable to rely completely upon families to provide all the kinds of investor education. Although more people save and invest than in the past, significant numbers of Americans do not, and can not, engage in this activity.¹¹⁷ Some children will not have the opportunity to receive this family education, just as they lack other family educational advantages. Also one can not be sure whether in consumption-oriented American society, even financially sophisticated parents will take the time to educate their children on saving and investing. The best-trained Wall Street professional may have no time to provide education (or may decide that it would be better simply to make more money so that her children do not ever have to worry about saving and investing). In addition, although families can educate children about common kinds of financial fraud, their informal, shared knowledge will not adequately address its more innovative forms.

2. Schools

Because families can not in all cases provide investor education to children, schools should supplement what education families can furnish. Schools are major participants in the "acculturation" process and can thus bring students into the saving and investing culture. As in other forms of education involving critical skills for social survival,

Yet other evidence is more systematic. See BERNHEIM ET AL., EDUCATION AND SAVING, *supra* note 6, at 24 (finding that exposure to school financial education does not increase saving in students when they had frugal parents and observing, "[i]t also raises the following intriguing possibility: if the children of frugal parents save more because they learn the basic elements of household saving at home, then the impact of high school financial education may vary significantly and systematically across the population"); Thaler, *supra* note 44, at 187 (noting that individuals learn about retirement plans through role models); cf. CHUBB & MOE, *supra* note 19, at 101 ("The strongest and most consistent finding in research on student achievement is that family background is a major influence, perhaps even a decisive one.") (footnote omitted).

¹¹⁴ See *infra* Part III(B)(3).

¹¹⁵ Financial firms are now providing educational aids to families. See, e.g., MERRILL LYNCH, THE FURTHER ADVENTURES OF SAVIN' DAVE AND THE COMPOUNDERS (1997) (comic book with a saving and investing message, and promoting Merrill Lynch's National Saving Month); STEIN ROE, YOUNG INVESTOR FUND: THE EDUCATIONAL INVESTMENT (1998) (brochure describing equity fund designed for child investors).

¹¹⁶ See *supra* Part III(B)(1).

¹¹⁷ See generally Gordon, *supra* note 12, at 1534-38 (discussing data).

the knowledge to be imparted by investor education is too important to be left to families, for society has an obvious interest in training individuals to provide for themselves throughout their lives.¹¹⁸ The requirement of universal schooling ensures that investor education will reach all students so long as it is part of a school curriculum. Like other subjects, the kinds of investor education can be taught in stages and adjusted for student abilities, as well as repeated and tested to reinforce learning. Since American schooling is subject to centralized government control at the state level,¹¹⁹ the state educational bureaucracy should adopt a standardized investor education model for use in local schools, particularly high schools, and periodically update it to reflect developments in law, finance and the financial markets.

In fact, basic investor education has entered the high school (and, in some cases, the elementary and middle school¹²⁰) curriculum in many states since the mid-1970s. As of 1997, thirty-seven states have some policy on high school consumer education, which generally includes training in consumer decision-making, economics, personal finance and consumer rights. Of these thirty-seven states, twenty-nine mandate, in some fashion, that high school students receive consumer education (with fourteen of the twenty-nine specifically requiring instruction in personal finance).¹²¹ Educators have also developed standardized materials for this investor education curriculum. The best example of this standardization is from the National Institute for Consumer Education, under whose auspices educators, consumer advocates, financial industry representatives and regulators have produced course materials designed to help educate students about basics of saving, investing and avoidance of financial fraud.¹²²

¹¹⁸ See, e.g., AMY GUTMANN, *DEMOCRATIC EDUCATION* 28-33 (1987) (discussing the dangers of placing all educational authority with parents).

¹¹⁹ See generally CHUBB & MOE, *supra* note 19, at 4-5 (discussing the structure of control in local schools). This Article does not address the rich literature on whether schools should be subject to centralized government control or open to market competition. See generally Hakim, *supra* note 19, at 1-15 (highlighting the benefits to be obtained from implementing a competition-based educational system).

¹²⁰ See generally Constance L. Hays, *First Lessons in the Power of Money*, N.Y. TIMES, Apr. 12, 1998, § 3, at 1 (describing, among other things, basic economic and finance courses in primary schools).

¹²¹ See BERNHEIM ET AL., *EDUCATION AND SAVING*, *supra* note 6, at 5-8, Table 1 (noting that educational requirements vary in states, even for those mandating investor education; for example, a state may require that consumer education be integrated into an existing course, that it be developed as a separate course, or simply that consumer education materials be distributed to students).

¹²² See *Basics of Saving and Investing*, *supra* note 73 (describing activity of the National Institute for Consumer Education ("NICE"), its development of investor education materials with the help of the National Association of Securities Dealers and the members of its advisory committee, who include education specialists and financial industry representatives). Funding for development of these educational materials came from private and public sources. This Institute also acts as a clearinghouse for the numerous supplementary materials for this curriculum. See *id.* at *Appendix* (listing free and inexpensive sources of investor education, including

The available empirical evidence about the effects of this formal investor education, while limited, is positive.¹²³ The evidence suggests that the school consumer education has increased Americans' exposure to investor education¹²⁴ and, more importantly, has actually improved saving and investing behavior by those who have taken the school finance courses.¹²⁵ It is also not unreasonable to conclude that the education has had other positive effects that are difficult to measure, such as decreasing students' susceptibility to fraudulent investing schemes and improving their personal budgeting.

Given the social importance of investor education and the preliminary success of school training, the question arises whether the federal government should do more to compel the states to provide, or to expand, investor education in schools. Since the federal government administers Social Security and other welfare programs, oversees the pension system and is well-positioned to have a global perspective on national saving and investing behavior and its relation to the national economy it should be concerned about investor education.¹²⁶ At the same time, it has little direct control over the national education curriculum, and it is unlikely that investor education alone would motivate Congress to face the constitutional questions that would arise from an aggressive federal government move into this area.¹²⁷ Since, moreover, the number of states mandating some form

those available on-line); *see also* JumpStart Coalition for Personal Financial Literacy, *Education Materials* (visited Sept. 15, 1998) <<http://www.jumpstartcoalition.org/search1.html>> (offering "personal finance education materials for use in Kindergarten through 12th grade classrooms").

¹²³ Some anecdotal evidence is negative, however. *See, e.g.*, Scott Bernard Nelson, *High-School Seniors Get An F in Money Management*, Kiplinger Online, News of the Day, May 22, 1997 <www.kiplinger.com/dailynews/dn052297.html> (reporting on the lack of financial literacy in high school seniors).

¹²⁴ *See* BERNHEIM ET AL., EDUCATION AND SAVINGS, *supra* note 6, at 11-17 (discussing the findings of a study that examined the impact of curriculum requirements on financial education).

¹²⁵ *See* BERNHEIM ET AL., EDUCATION AND SAVINGS, *supra* note 6, at 22-23 (describing results suggesting an increase in the saving rate as a function of exposure to financial education); *id.* at 27-28 (describing higher net worth of individuals exposed to the education). The first generation of students subject to this education are those in "Generation X," and these individuals are reported to be high savers and financially savvy. *See, e.g.*, Tripp Baltz, *Generation X-ers Favor Self-Investing Social Security Payments, Speaker Says*, BNA PENSIONS & BENEFITS DAILY, Dec. 8, 1997, available in LEXIS, pension library (describing saving preferences of younger workers); Gleckman, *supra* note 113, at 44 (reporting an increased saving by the younger generation).

¹²⁶ Indeed, the federal government is mandated by law to develop initiatives on investor education, although these initiatives are not specifically aimed at schools. *See infra* Part III(B)(4)(a).

¹²⁷ The provision of, and questions concerning, education have traditionally been left to the states. A constitutional question relating to education, for example, would be whether education, or a minimum level of education, is a fundamental right, entitling individuals to protection under the Equal Protection Clause of the Fourteenth Amendment. *See, e.g.*, *San Antonio Independent School District v. Rodriguez*, 411 U.S. 1, 18 (1973) (holding that the strict scrutiny test should not be used to examine the Texas school financing system because education is not a fundamental right under the Constitution). *See generally* Susan H. Bitensky, *Theoretical Foun-*

of investor education has increased, states may eventually have uniform investor education requirements and a curriculum.¹²⁸

Yet the federal government could strongly reinforce a role in investor education schooling that it has already employed and for which it is well-suited—that of facilitator and promoter of local educational efforts. Federal financial market regulators should encourage financial market participants to continue to work with educators to develop educational materials and to offer their services in schools,¹²⁹ and the regulators could supply curriculum guidance in their particular areas of expertise. The Department of Education could also support investor education in elementary, middle and secondary schools by its available means (e.g., grants for teaching, sponsorship of conferences and research in this area) without upsetting any state/federal balance. This activity would signal the federal government's recognition of the importance of this education and encourage the states to develop further investor education requirements and curricula.¹³⁰

3. *The Market*

Since families and schools do not yet uniformly educate their children about saving and investing, another education provider is needed. "Continuing" investor education would also provide consumers with an opportunity to "refresh," update and improve their financial knowledge. This kind of education is crucially important. Although saving and investing have become critical activities, the necessary level of investor education has not yet been attained, and therefore many individuals reach adulthood having received no investor education or educational opportunities, which constitutes a social failure that needs to be addressed. The questions, of course, are who should provide this education and how? More specifically, should it be left to private educational providers or should the government ensure its provision?

Before considering the appropriate government role in investor education outside the schools, it is important to review briefly

dations for a Right to Education Under the U.S. Constitution: A Beginning to the End of the National Education Crisis, 86 NW. U. L. REV. 550, 563-73 (1992) (surveying U.S. Supreme Court cases in this area).

¹²⁸ See BERNHEIM ET AL., EDUCATION AND SAVING, *supra* note 6, at 6 (describing gradual adoption of the investor education laws).

¹²⁹ For example, the New York Stock Exchange sponsors extensive educational programs that attract students and teachers. See Claudia H. Deutsch, *Goldman, Sachs Invests Time in City Schools*, N.Y. TIMES, Oct. 14, 1997, at B8 (describing volunteer work of investment bank's partners and employees in New York City schools); New York Stock Exchange, *Invest in Yourself: A Message to Educators* (visited Sept. 20, 1998) <<http://www.nyse.com/public/educate/6e/63ix.htm>> (describing "Invest in Yourself" program to help educate middle and high school students about investing).

¹³⁰ See *infra* Part IV(A) (describing national saving and investing campaign coordinated by state and local financial regulators).

whether, from a theoretical perspective, private actors have incentives to provide investor education, and what they are, in fact, doing. Investor education appears to be the kind of service or product that private parties in a market should supply. Since the basics of saving and investing are straightforward, standardized and thus easy to reproduce and package, they are a commodity. Economic theory suggests that, under most circumstances, the market will produce and provide commodities to consumers at favorable prices (e.g., not significantly above marginal cost).¹³¹ It is, of course, necessary to keep in mind potential circumstances that could undermine this "free market" result. Since investor education is a commodity, private actors may not supply it in adequate quantities for, or in forms easily accessible to, consumers, for they could not capture all the profits of their efforts (i.e., other companies could copy the information or the format).¹³² A few firms might dominate consumer financial services and, if this market had high entry barriers, they could ignore investor education altogether or charge anti-competitive prices for it.¹³³

No market problems in American consumer financial services currently hinder the market's provision of investor education to consumers at a low cost. Financial services are highly competitive because low start-up costs allow a relative ease of entry for new participants.¹³⁴ Advances in communications technology enable new entrants to have access to information about markets, investment products and investors, formerly the main competitive advantage of established firms.¹³⁵ A financial firm or group of financial firms simply can not dominate the retail or consumer investing industry so as to be

¹³¹ See generally OLIVER E. WILLIAMSON, *THE MECHANISMS OF GOVERNANCE* 61-63, 98-100 (1996) (demonstrating how different safeguards in the market produce low prices); Alan Schwartz & Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630, 643-47 (1979) (explaining that, in a market producing commodities for consumers, optimal pricing will occur as long as the market is competitive, because market participants can not distinguish between, and discriminate in pricing as to, informed and uninformed consumers).

¹³² See, e.g., White, *supra* note 64, at 15 (noting the external effect on the market when one company adopts a new development idea of another).

¹³³ See, e.g., *id.* at 12 (discussing the development of market power and its effects on quantity of a product in the market).

¹³⁴ See generally SMITH & WALTER, *supra* note 40, at 14-15 (noting the increase in financial businesses and the effects of competition in the financial market). Entering the financial services industry does involve considerable costs, many of them regulatory in nature, as well as a significant human capital cost. These human costs, as well as those arising from firms' efforts to provide globally all financial services to their customers, have led to industry consolidation. See *Global Investment Banks: Fools' Gold*, *ECONOMIST*, Dec. 13, 1997, at 61 (discussing the benefits and problems associated with the merger of two large Swiss banks).

¹³⁵ See FRANKLIN R. EDWARDS, *THE NEW FINANCE: REGULATION AND FINANCIAL STABILITY* 8 (1996) ("The ability to retrieve, store, process, manipulate, and transmit large masses of data at low cost made it easier for financial institutions to offer new products and enter new markets to compete for customers."); SMITH & WALTER, *supra* note 40, at 394 (noting that consumer financial services involve the provision of interchangeable products and services).

able to impose restrictions on, or to hinder, the provision of investor education.¹³⁶

Indeed, financial firms vigorously compete specifically in consumer "asset management" because ordinary people increasingly invest through the industry, particularly in defined contribution plans and IRAs.¹³⁷ This competition ensures that the firms supply consumers with investor education products and services at low cost and in user-friendly formats and also constantly improve them. Asset management firms need to distinguish themselves from their competitors for consumers. While the most attractive characteristic is superior investment advice, strategy and returns, long-term investment performance on an expense-adjusted basis is difficult to achieve.¹³⁸ Financial firms must attract and maintain consumers as customers through other means, primarily by providing ancillary investing services.¹³⁹

Investor education is one such service. Since it is standardized and communications technology has lowered its cost of reproduction, firms can supply it to consumers at little or no charge. Although a firm cannot generate significant profits directly from a standard educational product or from any innovations to it (which competitors easily and immediately imitate), the firm will supply the education and continue its innovations because the service generates customer goodwill and encourages consumers to invest through the firm. The more consumers know about saving and investing, the more likely they are to save and to invest through financial firms, and specifically through one particular firm (as opposed to leaving their savings in bank deposits or outside the financial services industry).¹⁴⁰ In addition, investor education enables consumers to understand the range of investment products a firm has to offer, and encourages them to use these products in their portfolio. The education may also lead consumers to realize the potential benefits that they can receive from brokers or other financial professionals employed by the firm. In

¹³⁶ This situation could, of course, change. Numerous large consolidations and mergers between banks and other financial institutions have recently occurred (e.g., Citibank/Travelers), and these transactions could have an adverse effect on the provision of services, like investor education, to consumers.

¹³⁷ See, e.g., EDWARDS, *supra* note 135, at 73 (discussing investment growth in mutual fund shares as opposed to bank deposits); SMITH & WALTER, *supra* note 40, at 381-82 (noting changes in investment business created by competition); see also *Investors, Unite*, ECONOMIST, (Supp.) Oct. 25, 1997, at 3, 3-5 (discussing competition in asset management).

¹³⁸ Cf. *supra* note 101.

¹³⁹ See EDWARDS, *supra* note 135, at 16 (describing how investment banks came to offer customers check-writing and payment services formerly provided only by commercial banks).

¹⁴⁰ See, e.g., BERNHEIM & GARRETT, *supra* note 6, at 19 (noting that educated individuals rely on financial professionals for information and advice, rather than their employers).

sum, education is a form of financial firm product advertisement, but, as in most advertising, it benefits both firms and consumers.¹⁴¹

There has been, in fact, a remarkable increase in the number of investor education products and services offered by financial firms to consumers at minimal or no cost.¹⁴² Mutual fund companies,¹⁴³ investment banks and brokerage houses,¹⁴⁴ financial industry trade groups,¹⁴⁵ and self-regulatory organizations¹⁴⁶ supply retail investors with tools and services enabling them to have a basic education in saving and investing. These tools also help investors understand general finance, risks, asset-allocation strategies, finance professionals and the language of investing—in short, a useful introduction to, or further familiarity with, the culture of saving and investing. Further, consumers can also apply the educational tools to their own personal circumstances in financial planning. If an investor requires additional advice, some companies even offer personalized financial planning

¹⁴¹ See, e.g., Kevin J. Delaney, *Mutual Funds Use a New Spin To Sell Wares*, WALL ST. J., Aug. 27, 1997, at C1 (“Mutual-fund companies have begun to sell their wares the way consumer-goods companies market cereal and laundry detergent.”). Not everyone is pleased with the consumer characterization of investing. See, e.g., Don Phillips, *Owner or Consumer? Open Letter to the SEC* (last modified May 2, 1997) <<http://www.morningstar.net/cgi-bin/Getnews.exe?newsstory=ms/OpEd/letterToSEC1/Lettertosec4.html>> (president of rating organization of mutual funds argues against regulatory actions accepting the view of ordinary investors as consumers).

¹⁴² The following references cannot pretend to be exhaustive, but are only representative, since new firm educational products and services appear on a daily basis, particularly on the Internet.

¹⁴³ See, e.g., Fidelity Investments, *Know What You Own and Know Why You Own It* (visited Sept. 15, 1998) <<http://www.fidelity.com>> (educating consumers about the importance of saving, particularly for retirement needs, elementary finance, kinds of investments, tax-reducing retirement options, kinds of mutual funds, investment basics and asset-allocation strategies); see also T. ROWE PRICE, T. ROWE PRICE RETIREMENT PLANNING ANALYZER (1997) (CD-ROM retirement planner).

¹⁴⁴ See, e.g., *CharlesSchwab* (visited Sept. 15, 1998) <www.schwab.com> (providing, in the “Planning” section, materials of discount broker Charles Schwab on the basics of saving and investing as well as retirement planning, with information about life-cycle investing); Merrill Lynch, *Investor Learning Center* (visited Sept. 15, 1998) <www.plan.ml.com/investor> (providing information and interactive forms to design investment goals and portfolios).

¹⁴⁵ See Investment Company Institute, *Mutual Fund Connection* (visited Sept. 15, 1998) <www.ici.org> (offering, at the Web site of the Investment Company Institute (“ICI”), general educational materials explaining the nature of a mutual fund, its risks and benefits (chiefly diversification), the kinds of mutual funds, the typical fees, expenses and services of a fund, and the pricing and redemption of mutual fund shares).

¹⁴⁶ See FACT BOOK, *supra* note 53, at 57 (explaining that, since individual investors still generate much of the direct investing in securities, the New York Stock Exchange offers investor education on its Web site); *You and the Investment World*, *supra* note 73 (education on personal and macroeconomic reasons for investing, the functioning of stock exchanges, the language of the financial press, kinds of investments and their risks and basic advice on asset-allocation strategies and ways of investing); see also *Investor Training*, *supra* note 73 (educating investors as to reasons for investing, investment options, and providing guidance on assessing one’s personal financial situation and setting financial goals); NASDAQ, *Investment Tips* (visited Sept. 15, 1998) <www.nasdaq.com/services/services.stm> (providing links to the NASD’s educational materials, including those of NICE, as well as sophisticated tools to track the value of a portfolio).

services and seminars.¹⁴⁷ The firms and organizations deliver this education in traditional ways (e.g., through written materials),¹⁴⁸ but developments in information technology, particularly CD-ROMs and the World Wide Web, have greatly enhanced its provision, sophistication and, significantly, its use by consumers.¹⁴⁹

The commodity nature of investor education, the sophistication of financial products and industry competition all ensure that the educational products and services of financial firms are more than “window dressing” to attract consumer funds.¹⁵⁰ Indeed, the education would not be successful unless it offered consumers some understanding about a firm’s investment products and strategies. Competition in financial services forces firms to do more than conduct a superficial teaching in order to explain the superiority of their products and services. Although there are superior educational products, it generally does not matter what educational product a consumer uses, since the products have become “standardized” through competition.¹⁵¹

¹⁴⁷ See James S. Hirsch, *Fidelity, CBS Are Considering Finance Show*, WALL ST. J., Sept. 17, 1997, at B1 (discussing Fidelity’s proposed (but later abandoned) television show on personal finance); Robert McGough, *No-Load Fund Investors Still Buying Advice*, WALL ST. J., Sept. 11, 1997, at C1 (discussing advisory services provided by mutual funds); *Money Managers: Take My Advice*, *supra* note 101, at 78-79 (noting that increased advisory services are packaged as investor education in financial firms).

¹⁴⁸ See, e.g., CHARLES SCHWAB, *THE ESSENTIAL INVESTOR* (1997) (informational pamphlet on long-term investing); FIDELITY INVESTMENTS, *MANAGING RISK IN YOUR PORTFOLIO: A FIDELITY GUIDE FOR EXPERIENCED INVESTORS* (1995) (describing risk, risk management and asset allocation); Investment Company Institute, *A Guide to Mutual Funds* (visited Sept. 20, 1998) <<http://www.ici.org/pdf/guide2mutualfunds.pdf>>; MERRILL LYNCH, *YOU AND YOUR MONEY: A FINANCIAL HANDBOOK FOR WOMEN INVESTORS* (1997) (informing women investors about everything from kinds of credit to stock options); The Vanguard Group, *Plain Talk: The Vanguard Investment Planner* (visited Sept. 20, 1998) <<http://vanguard.com/educ/lib/plain/investplan.html>>.

¹⁴⁹ See *supra* text accompanying notes 142-47 (providing examples of use of technology in educational materials); see also YANKELOVICH PARTNERS, INC., *supra* note 55, at 12 (referring to growing numbers of investors who use personal computers to obtain investment information). But see ARTHUR B. KENNICKELL & MYRON L. KWAST, *WHO USES ELECTRONIC BANKING? RESULTS FROM THE 1995 SURVEY OF CONSUMER FINANCES 18* (Federal Reserve Board Finance and Economics Discussion Series No. 1997-35, 1997) (demonstrating that consumer use of electronic means to make saving and investing decisions is very limited).

¹⁵⁰ See Schwartz & Wilde, *supra* note 131, at 638 (observing that competition in the educational services market protects consumers who do not regularly research market products).

¹⁵¹ Indeed, there might well be a cause for suspicion about firm-provided investor education, for instance, if consumers heard only about the benefits of actively managed mutual funds and nothing about indexed investing. As it is, the Vanguard Group, one of the largest mutual fund companies, provides investors with training about indexing in its voluminous educational materials. See The Vanguard Group, *Learning Center* (visited Sept. 15, 1998) <<http://www.vanguard.com/educ/inveduc.html>> (offering consumers a “University” with a course on “The Fundamentals of Mutual Funds”); see also The Vanguard Group, *Literature Library* (visited Sept. 15, 1998) <<http://www.vanguard.com/educ/lib/litlib.html>> (offering viewpoints of Vanguard’s legendary founder, John Bogle, the champion of index investing, such as “Bogle on Indexing” and “The Riddle of Performance Attribution”); The Vanguard Group, *Plain Talk: The Vanguard Investment Planner* (visited Sept. 15, 1998) <<http://www.vanguard.com/educ/>

Competition in educational services from firms and organizations other than financial firms, whether nonprofit¹⁵² or for-profit, also compels financial firms to create "quality" educational products. Almost countless members of the financial press,¹⁵³ rating organizations,¹⁵⁴ investor groups¹⁵⁵ and others¹⁵⁶ provide at little or no cost to consumers investor educational materials and tools.¹⁵⁷ Moreover,

lib/plain/investplan.html>. Similarly, a consumer can read about the advantages of discount brokerage (e.g., through Charles Schwab) and of full-service brokers (e.g., through Merrill Lynch). Competition among financial firms even results in financial firms discussing competing investing strategies, products, and financial services. See, e.g., The Vanguard Group, *Plain Talk About Index Investing* (visited Sept. 15, 1998) <<http://www.vanguard.com/educ.lib/plain/index.html>>, at 5 (explaining that "[a] suitable compromise [between indexing and an actively managed strategy] may be to build equity and bond portfolios (or even combine them through a balanced approach) with a "core" holding in an appropriate index fund. Around that core investment, an investor may select specific actively managed funds that appear likely, in the investor's judgment, to add incremental investment performance over the long run.").

An obvious consumer problem, is the bewildering number of educational products, which is exacerbated by computer technology. See Stout, *Motley Fool*, *supra* note 88, at 812 ("Investors' opinions will become increasingly fragmented as different individuals come to rely on an ever-increasing number of different and disagreeing sources."); cf. John C. Coffee, Jr., *Brave New World?: The Impact(s) of the Internet on Modern Securities Regulation*, 52 BUS. LAW. 1195, 1200-01 (Aug. 1997) (arguing that financial professionals will still need to act as "gatekeepers" for investors (i.e., insure that reputable companies offer securities), despite the access of more information to consumers). My point is simply that most of these products provide the necessary education. Consumers just need to be educated to use one product out of the many available.

¹⁵² See, e.g., American Association of Retired Persons, *Getting Answers: Information and Research* (visited Sept. 15, 1998) <<http://www.aarp.org/answers.html>> (providing links to investment tips and other economic security programs); American Association of Retired Persons, *Smart Investing* (visited Sept. 15, 1998) <<http://www.aarp/getans/smartinvest.html>> (presenting basic finance and investment advice, including tips on dealing with a broker and evaluating risk).

¹⁵³ See, e.g., *How To Retire Successfully*, BUS. WK., July 21, 1997, at 59-92 (special report to help consumers invest).

¹⁵⁴ See, e.g., Morningstar, Inc., *Morningstar.Net* (visited Sept. 15, 1998) <<http://www.morningstar.net>> (providing a rating service of mutual funds).

¹⁵⁵ See, e.g., American Association of Individual Investors, *AII.com* (visited Sept. 15, 1998) <<http://www.aaii.com>> (providing numerous educational materials, services and seminars for consumers).

¹⁵⁶ See *Money Managers: Take My Advice*, *supra* note 147, at 79 (reporting that Nobel prize-winning economist William Sharpe is starting an Internet service to correct mistakes in most financial advisory software).

¹⁵⁷ As anyone knows who has "surfing the Net" or browsed through an investor section of a large bookstore or software company, it may well be impossible to list all the investor education tools and services. See, e.g., Edward C. Baig, *For Investors of All Stripes, A Cornucopia on the Net*, BUS. WK., Dec. 22, 1997, at 104 (detailing consumer informational and educational resources on the World Wide Web); Amy Dunkin, *The Web User's Guide to Screening Stocks*, BUS. WK., Sept. 22, 1997, at 114-16 (describing Internet stock analysis tools); Daisy Maxey, *S&P to Introduce Customized On-Line Investment Advisory Service Today*, WALL ST. J., Jan. 12, 1998, at B12B (describing new "Personal Wealth" venture of Standard & Poor's to offer consumers on-line financial advice at <<http://www.personalwealth.com>>); Michael R. Sesit, *Internet Site Offers Help to Investors*, WALL ST. J., July 23, 1997, at C1 (describing Web site, <<http://www.riskview.com>>, that permits individual investors at no cost to calculate the risk of their portfolios); Stout, *Motley Fool*, *supra* note 88, at 807 (describing "Motley Fool" on-line investment advisory service); Gary Weiss, *Web of Hype and Glory*, BUS. WK., June 16, 1997, at 108 (discussing web sites that offer investor education and information); see also *supra* note

since new technology permits consumers to bypass financial services firms¹⁵⁸ if they are helped by these independent educational services, financial firms need to justify their value. The provision of superior education is one possible justification.

Consumer financial services firms, as well as the financial marketplace in general, provide worthwhile investor education to consumers at little cost and in accessible formats. Consumers can thus easily continue whatever investor education they received at home or in school, or if they never received such education, can acquire the educational tools and services to begin their acculturation into the saving and investing world. In light of all this private educational activity, what investor education efforts, in addition to facilitating familial development of saving and investing norms and encouraging formal education in the schools, can the government usefully undertake?

4. *The Government*

a. Education About Saving and Investing

State or federal financial regulators should not see as *their* main tasks the establishment of a basic investor education curriculum and the teaching of consumers. Not only do they not have the resources to conduct this education, but there is no general need for their involvement, on account of the activity of the market (broadly defined to include nonprofit organizations). Active intervention by regulators to set minimum standards of investor education (a “quality assurance” role often undertaken by the government in other kinds of education¹⁵⁹) is also unnecessary since the standardization of the product and the competitiveness of the financial services industry ensure this quality. The regulators should, however, ensure that these standards are being regularly applied. Because financial firms have strong, profit-oriented incentives, which financial regulators lack, to make their educational products and services as innovative and “user-

122; *InvestorGuide* (visited Sept. 15, 1998) <<http://www.investorguide.com>> (advertising *InvestorGuide* as “the leading guide to investing on the web”); *The Syndicate* (visited Sept. 15, 1998) <<http://www.moneypages.com>> (investor service focusing on mutual funds).

¹⁵⁸ See, e.g., Peter Galuszka, *Guess Who’s Courting the Beardstown Ladies?*, BUS. WK., Sept. 22, 1997, at 90 (discussing direct investing movement and National Association of Investor Corporation that encourages this movement and educates investors); Barbara Hetzer, *Direct Stock Buying: A Load of New No-Loads*, BUS. WK., June 16, 1997, at 152 (describing the increasing opportunities of small investors to buy stock directly from companies and thus to bypass brokers). Financial firms are also feeling pressure from on-line brokerage and trading. See Deborah Lohse, *Wit Capital Will Launch On-Line Site*, WALL ST. J., Sept. 15, 1997, at B12 (describing an on-line service proposing to bring initial public offerings directly to individuals without financial firm involvement).

¹⁵⁹ See HART ET AL., *supra* note 5, at 2-7 (discussing quality concerns as a justification for government control of education).

friendly" as possible, any models or standards that government officials would devise would likely add little to the "standard" product, would quickly become outdated, and would retard industry experimentation.¹⁶⁰ State or federal financial educators should simply encourage the continued market development of consumer educational materials, which they could also review for minimum educational qualification and for the prevention of investor fraud or abuse.

Although the exact contours of the role are not always easy to define, the government has an important role in the delivery of investor education. Rather than being the chief conductor of saving and investing education, the government should act as a "cheerleader" for these activities and should promote and facilitate consumer use of the educational services of for-profit and nonprofit providers. Federal and state agencies could use their resources to conduct an active and continuous publicity campaign to encourage consumer saving and investing. Although incidental to the campaign's promotional purpose, some elementary investor education should be part of this campaign so as to reinforce basic saving and investing "norms," as well as to reach members of the population overlooked by private education providers. The federal executive branch should orchestrate a national campaign, and each government agency or Congressional committee should participate in areas within its jurisdiction and competency.

Private financial services firms also have incentives to support a national saving and investing campaign since the industry can only benefit from increased consumer saving and investing. Certainly the industry's existing educational efforts have a hortatory or promotional side,¹⁶¹ but industry participants alone are unlikely to be the most effective campaigners. The government is an excellent "bully pulpit" with many effective instruments of persuasion at its disposal. Since citizens expect pronouncements on issues of general concern from the government, financial firm publicity will produce better results if supplemented with active government involvement in promoting saving and investing. In fact, behavioral and economic research suggests that the government's promotional efforts have a significant positive effect upon saving and investing behavior.¹⁶² Indeed, the literature suggests that the government occupies a critical position in creating and changing the kind of "rule of thumb" norms so important

¹⁶⁰ The investor educational materials of government agencies are generally inferior to those offered by private market parties. See *infra* Part IV(A).

¹⁶¹ See, e.g., Merrill Lynch, *Time to Save* (visited Sept. 15, 1998) <<http://www.plan.ml.com/personal/saving>> (highlighting Merrill Lynch's sponsorship of a National Saving Month campaign to encourage saving among students).

¹⁶² See BERNHEIM, THE VANISHING NEST EGG, *supra* note 6, at 121 (explaining the importance of a national government campaign for consumer saving).

for saving and investing because it can publicize their importance and help generate a "norm community" of savers and investors.¹⁶³

A good example of a federal agency's performance of the "cheerleading" and market facilitator roles is the recent activity of the Department of Labor's Pension and Welfare Benefits Administration ("PWBA"), which helps administer private pension plans subject to ERISA.¹⁶⁴ Because of the low rate of consumer saving and the impending retirement of the "Baby Boomers," the PWBA began a Retirement Savings Education Campaign in 1995 to educate Americans about the importance of saving, investing and using pension plans.¹⁶⁵ Its extensively publicized campaign materials convey this promotional message, provide some basic guidelines on saving and investing and refer consumers to financial and nonprofit firms for full education.¹⁶⁶ The PWBA also enlisted financial firms in its campaign through the nonprofit American Savings Education Council ("ASEC"),¹⁶⁷ which conducts research on saving, co-sponsors public

¹⁶³ See generally McAdams, *supra* note 82, at 362-64 (discussing the importance of publicity in establishing a norm consensus); *id.* at 400-07 (discussing how the law can be used to signal, and thus to establish, a consensus around certain norms); Posner, *supra* note 111, at 149-50, 187 (describing how the government can strengthen pre-existing norms and encourage generalized norm creation); Cass R. Sunstein, *Social Norms and Social Roles*, 96 COLUM. L. REV. 903, 929-30 (1996) (discussing the government's ability to create and reinforce social norms). See, e.g., David Charny, *Illusions of a Spontaneous Order: 'Norms' in Contractual Relationships*, 144 U. PA. L. REV. 1841, 1847-48 (1996) (suggesting that norm creation across large populations needs centralized state intervention); cf. Lawrence Lessig, *The Regulation of Social Meaning*, 62 U. CHI. L. REV. 943, 972-86 (1995) (discussing, among other things, the role of government in the generation of social meaning).

¹⁶⁴ The PWBA administers Title I of ERISA, which regulates reporting, disclosure and fiduciary matters pertaining to plans. The Internal Revenue Service administers Title II, which deals with eligibility of pension plans, vesting requirements and funding. The Pension Benefit Guaranty Corporation manages an insurance program covering employees in the event of plan termination. See generally FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS, *supra* note 23, at 35-36.

¹⁶⁵ See DOL, *Retirement Savings Education Campaign* (last modified May 1998) <<http://www.dol.gov/dol/pwba/public/pubs/introprg.htm>>.

¹⁶⁶ See *id.*, at 1-4 (listing PWBA's educational activities and publications available to investors); see also DOL, *Pension and Welfare Benefits Administration, Protect Your Pension: A Quick Reference Guide* (visited Sept. 15, 1998) <<http://www.dol.gov/pwba/public/pubs/protect/guieoc.htm>> (presenting general facts about pensions); DOL, *supra* note 76 (explaining the importance of inquiring about an employer's pension plans, using an IRA and recommending that consumers set retirement goals, learn basic investment principles and ask questions of financial advisors). The PWBA also provides references (or, on its Web site, hypertext links) to providers of investor education, such as ICI and AARP. See *supra* note 165 (where links are listed).

¹⁶⁷ Founded in 1995 as part of the Employee Benefit Research Institute and funded by the financial services industry, ASEC has "charter partners" or sponsors that include financial companies like American Express, Bankers Trust, Fidelity, the Variable Annuity Life Insurance Company and Prudential Investments, as well as trade groups of financial firms, such as the American Council of Life Insurance and ICI. See *Sponsors: American Savings Education Council* (visited Sept. 20, 1998) <<http://www.asec.org/sponshh.htm>>; see also ASEC, *Strategic Plan: Building Public Awareness and Understanding of Saving and Retirement Planning* (visited Sept. 15, 1998) <<http://www.asec.org/straplan.htm>> (explaining that ASEC's mission is "to

educational events about its importance with government officials and develops tools for saving education that have a consciousness-raising and general educational purpose.¹⁶⁸ Moreover, in a recent interpretive bulletin on participant investment education, the PWBA specifically facilitated private market educational efforts by adopting a regulation that encouraged more employers to have financial firms provide investor education to employees participating in defined contribution plans.¹⁶⁹

Indeed, the PWBA's educational activities, coupled with a bipartisan national concern about adequate retirement saving and in-

undertake and encourage initiatives aimed at raising public awareness about what is needed to successfully ensure long-term financial security in retirement.”)

¹⁶⁸ See DOL, *supra* note 73 (listing sources of information on saving, investing and selecting a financial professional); ASEC, *Ballpark Estimate, Definitions of Saving and Retirement Terms* (visited Sept. 15, 1998) <<http://www.asec.org/ballpark.htm>> (providing a worksheet so that an individual can get a rough idea of how much he or she will need at retirement and a glossary of saving and retirement terms); ASEC, *What is ASEC?* (visited Sept. 15, 1998) <<http://www.asec.org/pamphlet.htm>>; ASEC, *The Power to Choose* (visited Sept. 15, 1998) <<http://www.asec.org/asecpwr1.htm>> (explaining retirement needs, the limitations of Social Security and tax-favorable savings plans, particularly those provided by employers); ASEC, *How Do I Get There From Here?* (visited Sept. 15, 1998) <<http://www.asec.org/there2.htm>> (listing sources of information on saving and investing and also giving advice on selecting a financial professional). See generally CONTE, *supra* note 39, at 28 (describing ASEC's recent activities).

¹⁶⁹ See Participant Investment Education, Interpretive Bulletin 96-1, 29 C.F.R. § 2510.3-21(c) (1997). The PWBA and employers were concerned that employees participating in defined contribution plans did not understand enough about investing. Many employers, however, declined to conduct, or to have financial firms conduct, programs to help employees because they feared that they would increase their fiduciary liability—an avoidance of which is one reason for establishing a defined contribution plan. Under ERISA, employers as plan sponsors have fiduciary obligations to plan beneficiaries, which include an obligation to account for plan losses due to a breach of fiduciary duties. See 29 U.S.C. §§ 1103, 1104, 1109 (1996). Pursuant to Section 404(c) of ERISA and to the applicable regulations, an employer can limit, but not eliminate, such fiduciary liability by establishing individual participant accounts and allowing participants to exercise control over them. See 29 U.S.C. § 1109(c) (1996). This limitation requires that a participant have sufficient information on investment alternatives under the plan to make an informed investment decision, but not that employers provide employees with general investing advice or education. See 29 C.F.R. § 2550.404c-1(c) (1998). The Interpretive Bulletin established a “safe harbor” for four kinds of information and education that employers, and particularly financial firms operating the plans for them, can supply without triggering a fiduciary obligation (i.e., without being deemed to be giving investment advice): (i) a description of the plan and its operation, the benefits of plan participation, the disadvantages in withdrawing funds prior to retirement and basic information about alternatives under the plan, (ii) general information on financial concepts, different rates of return on investments, inflation, future retirement income needs, investment time horizons and risk tolerance assessment, (iii) the presentation of asset-allocation models keyed to individuals with different time horizons and risks (i.e., life-cycle investing), which essentially helps an employee grasp the general finance information through specific examples and (iv) interactive materials and worksheets that allow an employee to compare his or her own circumstances to the asset-allocation models. See Interpretive Bulletin 96-1, *supra*. The PWBA also took the “market friendly” position of suggesting that other kinds of educational information and services that these firms may develop would likely fall within the safe harbor. Cf. Lynn Asinof, *Click & Shift: Workers Control Their Benefits On-Line*, WALL ST. J., Nov. 21, 1997, at C1 (observing that workers increasingly control their benefits on-line).

vesting, resulted in the recent enactment of the SAVER Act, which has an explicit educational focus.¹⁷⁰ This Act specifically mandates that the Department of Labor ("DOL") convey to the public information about retirement saving and plans, particularly by means of a permanent Internet site.¹⁷¹ The Act's definition of such information is essentially that provided by basic saving and investing education.¹⁷² The Act seems to envision that the site will focus on a description of retirement plans and will provide references to other Internet sites that provide the education.¹⁷³ Even more importantly, it requires the President to convene three educational summits to bring government officials and private parties (both for-profit and nonprofit firms) together, to "facilitate the development of a broad-based, public education program to encourage and enhance individual commitment to a personal retirement savings strategy"¹⁷⁴

¹⁷⁰ See Savings Are Vital to Everyone's Retirement Act of 1997, 29 U.S.C. §§ 1146-47 (Supp. 1997). The legislative history enumerates the following purposes of the Act:

- (1) to advance the public's knowledge and understanding of retirement savings and its critical importance to the future well-being of American workers and their families;
- (2) to provide for a periodic, bipartisan national retirement savings summit in conjunction with the White House to elevate the issue of savings to national prominence; and
- (3) to initiate the development of a broad-based, public education program to encourage and enhance individual commitment to a personal retirement savings strategy.

Id. § 1146 (Historical & Statutory Notes) (citing Savings Retirement Act of 1977, Pub. L. No. 105-92, § 2, 111 Stat. 2139 (1997)).

¹⁷¹ See 29 U.S.C. § 1146(d) (1997).

¹⁷² See 29 U.S.C. § 1146(e)(2) (requiring that the Secretary of Labor convey such information as "(A) the forms of retirement income savings; (B) the concept of compound interest; (C) the importance of commencing savings early in life; (D) savings principles; (E) the importance of prudence and diversification in investing; (F) the importance of the timing of investments; and (G) the impact on retirement savings of life's uncertainties, such as living beyond one's life expectancy.").

¹⁷³ See 29 U.S.C. §§ 1146(c)(1), (d)(1)-(5) (specifying in (d)(5) that the DOL Web site provide "links to other sites maintained on the Internet by governmental agencies and nonprofit organizations that provide additional detail on retirement income savings arrangements and related topics on savings or investing").

¹⁷⁴ 29 U.S.C. § 1147(a)(2). The first of these summits was held on June 4-5, 1998 in Washington. See The National Summit on Retirement Savings, *Summit Agenda* (visited Sept. 15, 1998) <<http://www.saversummit.org/agenda.htm>> (providing agenda for the summit); Employee Benefit Research Institute, *Current State—Savings and Education Today* (visited Sept. 15, 1998) <<http://www.ebri.org/rcs/dallas>> (providing material for presentation by EBRI president Dallas Salisbury at the summit); see also CONTE, *supra* note 39 (providing the agenda briefing book for the summit). Indeed, since the SAVER Act provides that the summits should involve the participation of public and private parties and be privately and publicly funded, the summits give a good example of government encouraging private market educators. See 29 U.S.C. § 1147(b),(e),(j); see also Alliance for Investor Education, *Alliance Mission and Members* (visited Sept. 15, 1998) <<http://www.investoreducation.org/mismembers.htm>> (Web site of Alliance for Investor Education, a nonprofit organization sponsored by trade groups and assisted by governmental agencies, that "is dedicated to facilitating greater understanding of investing, investments and the financial markets among current and prospective investors of all ages").

A difficult issue regarding the government's role in investor education is how, and how much, government agencies, as part of a national saving and investing campaign, should conduct some substantive education on important issues to which financial firms or nonprofit organizations might not give adequate attention. For example, should the government discourage consumers from excessive stock speculation and risk-taking in investing and advocate a strategy of portfolio diversification adjusted to an individual's life cycle and risk preferences as an optimal investing strategy for most Americans?¹⁷⁵ Similarly, if brokers and other financial professionals are understood to exert excessive influence upon individual investors, should an agency warn consumers to be on their guard about this influence when seeking advice from professionals?¹⁷⁶

A government agency, such as the Social Security Administration, the PWBA, the DOL, and federal bank regulators,¹⁷⁷ is certainly

Additionally, the Secretary of Labor must prepare a report on the summit. *See* 29 U.S.C. § 1147(g). For the report on the first summit, see DOL, FINAL REPORT ON THE NATIONAL SUMMIT ON RETIREMENT SAVINGS (Sept. 3, 1992).

¹⁷⁵ *See* Stout, *Costly Casinos*, *supra* note 88, at 696-97 (arguing that special quasi-educational effort is required to discourage investors from engaging in excessive stock trading).

¹⁷⁶ *Cf.* Langevoort, *supra* note 49, at 693-94 (arguing, in effect, that financial professionals should have a duty to bring negative information about their recommendations to customers' attention, a duty that would disrupt the psychological power of brokers in the sales process).

¹⁷⁷ Federal banking regulators, for example, want consumers to understand that federal government deposit insurance protects only bank deposits, not other investments made through a bank or a bank affiliate. Federal deposit insurance provides up to \$100,000 of insurance protection for a deposit account or accounts of an individual in any insured depository institution. The Federal Deposit Insurance Corporation, which administers the insurance coverage program, provides insurance to a bank if the bank complies with FDIC regulations and if it pays a premium that is adjusted for the "riskiness" of the bank. *See* JONATHAN R. MACEY & GEOFFREY P. MILLER, *BANKING LAW AND REGULATION* 279-300 (2d ed. 1997); EDWARDS, *supra* note 135, at 152-55. Since the story of legal restrictions on bank sales of nondeposit investment products and of the transformation of banking is complex, it suffices here to say that, in the last two decades, as investment banks and mutual fund companies began to attract consumer funds by offering both payment system products, such as interest-bearing checking services, and numerous investment products that offered possibilities of greater return (and risk) than savings deposits, consumers moved their funds from banks. *See generally id.* at 13-34 (observing that banks' asset bases shrank as borrowers turned to sources (e.g., capital markets) other than commercial loans); ROBERT E. LITAN, *THE REVOLUTION IN U.S. FINANCE* 1-35 (1991). Bank regulators, with the acquiescence of the courts, thus interpreted banking law more expansively to allow banks and bank affiliates to provide customers the products and services offered by their financial services competitors. *See generally* MACEY & MILLER, *supra*, at 495-554. Congress has yet to pass the necessary legislation repealing the legal separation between banking and investment banking.

Bank regulators worry that consumer misunderstandings about insurance coverage could undermine the soundness of the banking, payment and overall financial system in a stock market downturn, with potentially disastrous consequences for the economy. If, for example, bank customers purchase non-deposit investment products under the mistaken belief that the products are insured for declines in market value, a significant market downturn might produce a panic among customers as they learn of their mistake. The rush to withdraw funds from investments could reinforce the downturn and lead to a massive crisis of confidence in the financial system, i.e., a systemic failure. *See* EDWARDS, *supra* note 135, at 123 (defining a systematic crisis as "a disturbance that severely impairs the working of the financial system and, at the extreme, causes

justified in educating and, in some cases, is required to educate consumers about its programs and about its regulatory authority. Further, this activity could also include some kinds of basic saving and investing advice to consumers. Indeed, as part of the saving and investing campaign, government agencies *should* use their power to go beyond specific messages related to their regulatory authority, and to drive home certain key points about saving and investing, other than that a consumer should save, invest and use available educational materials. Their messages will lend weight to the educational activities of for-profit and nonprofit firms by reinforcing the basic saving and investing rules of thumb, and they can target lower income Americans often ignored by such firms.¹⁷⁸ The line between acceptable and unacceptable messages of government advocacy is not entirely clear, however, which means that any agency must approach this “education reinforcement” activity with care. An agency can beneficially echo saving guidelines and generally accepted financial principles. However, the agency must be careful about lending its support to any particular investing strategy that is not universally accepted in the financial community as being superior to any other. Even if an agency feels that, on the whole, one strategy (e.g., index-

a complete breakdown in it. Systemic risks are those risks that have the potential to cause such a crisis”). Banking regulators, like all financial regulators, live in fear of financial “meltdowns” for which blame can be laid partly or wholly at their door. Cf. Donald C. Langevoort, *The SEC as a Bureaucracy: Public Choice, Institutional Rhetoric, and the Process of Policy Formulation*, 47 WASH. & LEE L. REV. 527, 530 (1990) (arguing that SEC regulators are irrationally risk averse for purposes of self-preservation). And they realize that, locked into combat with other financial intermediaries, banks might do little to dispel customer impressions (which would be a competitive advantage) that bank non-deposit investment products are “safer” than those of bank competitors. The regulators thus emphasize education about deposit insurance as more consumers purchase non-traditional investment products from banks. See, e.g., Federal Deposit Insurance Corporation, Interagency Statement on Retail Sales of Nondeposit Investment Products, 1994 FDIC Interp. Letter LEXIS 16 (Feb. 17, 1994) (requiring, in a joint statement, issued by the Board of Governors of the Federal Reserve System, the FDIC, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision, on bank sales of non-deposit investments, banks to adopt procedures (e.g., written disclosures and warnings, separate names for investment products, separate location in bank and separate employees for sales of these products) designed to ensure that retail customers understand that these investments are not FDIC-insured, are not obligations of the bank and are subject to investment risk, including loss of principal); Federal Deposit Insurance Corporation, *Insured Or Not Insured—That is The Question* (visited Sept. 15, 1998) <<http://www.fdic.gov/consumer/ins-not.html>> (pamphlet emphasizing the non-deposit product/deposit distinction); Office of the Comptroller of the Currency, *Deposits and Investments: There's a Critical Difference* (visited Sept. 15, 1998) <<http://www.occ.treas.gov/ftp/depvsinv.txt>> (same). If banks continue their affiliation with other financial firms specializing in consumer-oriented investment products, bank regulators may have to consider whether they should undertake other kinds of investor education. See, e.g., Videotape: *It's Your Money* (Federal Reserve Board (video seminar on saving and investing by members of the Federal Reserve Board); Charles Gasparino, *Do Fund Mergers Hurt Small Investors?*, WALL ST. J., July 8, 1997, at C1 (discussing links between banks and fund companies).

¹⁷⁸ Admittedly, some of the best educational materials come from financial firms that are targeting people with significant disposable income. Yet it is critical that education also reach those who can save only small amounts. See CONTE, *supra* note 39, at 16-17.

ing) is better for consumers, it should not publicly favor it, provided consumers can receive adequate education about the strategy from a forceful private advocate.

As a pragmatic matter, a government agency, such as the SEC, cannot warn consumers generally to be on their guard against brokers and financial professionals. This warning would not only alienate powerful constituencies, but it would also undermine the welfare of the many consumers who benefit from these professionals.¹⁷⁹ The best way to ensure that consumers resist any psychological selling pressures used by financial professionals is to have consumers educated in the basics of saving and investing, which includes the appropriate psychological education.

b. The Government as Anti-Fraud Educator

Consumers also need first-time and continuing education about financial abuse and fraud from a provider other than families and schools. The financial services industry, broadly defined to include trade associations and participating nonprofit groups, could conduct this kind of investor education. Since its members are already involved in general saving and investing education, they could add this task to their educational efforts. Given their position, financial firms could identify and understand new permutations of abusive or fraudulent behavior. They also have incentives to police their industry. Legitimate firms want consumers to distinguish them from fraudulent organizations, and their provision of education to counter abusive practices provides a sign of legitimacy. Firms may educate consumers about fraud typical of financial professionals, since this misbehavior undermines customer confidence in financial services that is so critical to the industry's well-being.¹⁸⁰ In addition, consumer organizations that supply education naturally want to protect their members from abuse and fraud by educating them to be aware of their forms.

Yet even the most reputable financial firms do little to educate consumers about abusive or fraudulent financial practices. Rather, the only detailed private education on this subject comes from the quasi-governmental self-regulatory organizations, such as the National Association of Securities Dealers ("NASD")¹⁸¹ and the New

¹⁷⁹ See YANKELOVICH PARTNERS, INC., *supra* note 55, at 6 (noting that the majority of investors surveyed are pleased with their brokers).

¹⁸⁰ See, e.g., Langevoort, *supra* note 49, at 630 n.6 ("There is no doubt that the securities industry has a strong economic incentive to promote the impression that manipulative sales practices are limited to a small subset of brokers, for their entire business is built on customer trust.")

¹⁸¹ See, e.g., *Basics of Saving and Investing*, *supra* note 73, at Units 5, 6; NASD, *Investor Training, Taking Charge of Your Finances: How to Select a Broker, Investor Protection* (visited Sept. 15, 1998) <<http://www.nasd.com>>.

York Stock Exchange ("NYSE"),¹⁸² and from nonprofit consumer organizations.¹⁸³ This is not surprising given that conflicting interests make even legitimate financial professionals unsuitable to undertake investor education about consumer abuse or fraud. Despite concerns about legal sanctions and adverse publicity that will affect their market position, firms may be tempted by profit to engage, directly or indirectly, in clearly prohibited practices.¹⁸⁴ The line between illegitimate and legitimate financial practices, moreover, is also not always easy to draw, particularly regarding innovations in financial products, and practices can move from the legitimate to illegitimate category over time.¹⁸⁵ If certain practices or products are profitable and if their legality is uncertain (or not even questionable), it is not reasonable to expect that financial professionals will educate the public about ways of avoiding them, thus reducing their own profit. While competition in financial services helps ensure that financial firms will offer adequate saving and investing education to consumers, the same competition makes it unlikely that these firms will be at the forefront of educating consumers about innovative, potentially fraudulent financial practices, or simply about legitimate, but potentially abusive, sales tactics.¹⁸⁶ Furthermore, although consumer financial organizations can (and do) educate consumers about abuse and fraud, they do not have all of the expertise or resources necessary wholly to take on this educational burden.

The government in one or more forms, through agencies and self-regulatory organizations, as well as in partnership with consumer groups, should therefore be the primary educator about financial abuse and fraud, including fraud and deception in firm investor education materials. Unlike financial firms, it suffers no disabling conflict-of-interest in warning consumers against new fraud or abusive practices, although it may initially lack the knowledge and expertise to identify them.¹⁸⁷ Its educational efforts, moreover, follow from its enforcement of the laws and other regulatory responsibilities. A gov-

¹⁸² See *You and the Investment World*, *supra* note 73, at 33-37.

¹⁸³ See, e.g., AARP, *At Your Fingertips* (visited Sept. 15, 1998) <<http://www.aarp.org/program/finance>> (discussing telemarketing fraud).

¹⁸⁴ See Langevoort, *supra* note 49, at 647-48 (describing the tendency of supervisors in financial firms to focus on the "bottom line" in an effort to be able to deflect legal and moral responsibility for prohibited behavior by their employees); see also *Is This Marriage a Mistake?*, *ECONOMIST*, Jan. 31, 1998, at 75-77 (describing the lack of supervision in a Swiss bank that led to enormous losses).

¹⁸⁵ See, e.g., SELIGMAN, *supra* note 55, at 397-416 (describing the abolition of fixed commission rates at the NYSE).

¹⁸⁶ See, e.g., In the Matter of NationsSecurities and Nationsbank, N.A., Securities Act 1998 SEC LEXIS 833 (May 4, 1998) (settling charges against these financial institutions alleged to have engaged in fraudulent sales practices to consumers that blurred the distinction between insured bank deposits and non-government insured securities).

¹⁸⁷ Part of this education will thus be to inform consumers how to contact the government to bring new abusive or fraudulent schemes to the relevant agency's attention.

ernment agency identifies prohibited behavior regarding saving and investing and counteracts it by prosecuting offenders for violations of their fiduciary or other duties,¹⁸⁸ and by licensing and supervising investment professionals.¹⁸⁹ Publicizing these activities both deters future violators and educates investors about existing fraudulent or abusive schemes.¹⁹⁰ As new schemes appear, whether versions of old ones or genuinely innovative fraud, the government addresses them and, through the media publicity of its action and court decisions, further alerts investors.¹⁹¹ An explanatory list, or summary of past successful prosecutions regarding abuses of investors, would resemble the kind of list of common crimes affecting children that police officers distribute in schools.¹⁹² The cost of this education, moreover, is relatively small since communication technology makes it increasingly easier and cheaper for the government to communicate this information.

Americans also *expect* the government to perform this educational task, which state and federal financial regulators have traditionally fulfilled.¹⁹³ Consumers respect financial market authorities who have a reputation for integrity in policing financial fraud and abusive practices.¹⁹⁴ They look to government agencies for protection from,

¹⁸⁸ See, e.g., Roberta S. Karmel, *Is the Shingle Theory Dead?*, 52 WASH. & LEE L. REV. 1271, 1273 (1995) (discussing broker's implied representation of fair dealing or "shingle theory"); Langevoort, *supra* note 49, at 669, 675-76, 680-81, 691 (discussing duties imposed on brokers).

¹⁸⁹ See H.R. REP. NO. 104-864, at 39-40 (1996); S. REP. NO. 96-293, at 2-5 (1996) (explaining how the National Securities Markets Improvement Act of 1996 addressed the problem of lack of regulatory supervision of many investment advisors by dividing supervisory responsibility over advisors between the SEC and state authorities). The government can also "publicize" its enforcement through regulatory responses to questionable behavior. See, e.g., Langevoort, *supra* note 49, at 686-88 (discussing special regulatory response to "penny stock" fraud—requiring enhanced disclosure in sales of these stocks).

¹⁹⁰ See Langevoort, *supra* note 49, at 658 n.97 (referring to SEC and NASD efforts to publicize broker disciplinary information); cf. V.S. Khanna, *Corporate Criminal Liability: What Purpose Does It Serve?*, 109 HARV. L. REV. 1477, 1492, 1531 (1996) (discussing the powerful message-sending role of corporate law).

¹⁹¹ See, e.g., NASAA (visited Sept. 15, 1998) <<http://www.nasaa.org>> (Web site of the North American Securities Administrators Association, Inc. ("NASAA") warning about recent rise in "ethnic affinity fraud" (financial fraud targeted to particular ethnic groups by members of same group) and providing a list of recent fraudulent schemes, including "Cyberspace Fraud and the Small Investor").

¹⁹² State or federal government financial regulators or members of self-regulatory organizations could also discuss with students the dangers of financial fraud. See *infra* Part IV(A).

¹⁹³ See generally STEPHANIE W. KANWIT, 2 FEDERAL TRADE COMMISSION 22-1 to 22-59 (1995) (describing Federal Trade Commission regulation of false and deceptive advertising). The available government materials against securities fraud are voluminous. See, e.g., NASAA, *supra* note 191; *Basics of Saving and Investing*, *supra* note 73, at *Appendix* (listing numerous governmental agencies, together with their materials and Web sites).

¹⁹⁴ See KRIPKE, *supra* note 4, at 8. But see ROBERTA S. KARMEL, REGULATION BY PROSECUTION: THE SECURITIES AND EXCHANGE COMMISSION VS. CORPORATE AMERICA 187-92 (1982) (discussing problems of SEC overreaching in law enforcement).

and guidance about, such practices and are likely to cooperate with these agencies in helping to identify perpetrators of fraudulent schemes. Just as the government has a critical role in reinforcing optimal saving and investing norms, it plays a significant part in maintaining the bounds of acceptable and prohibited investing behavior. Social expectations thus reinforce the conclusion that the government, generally through financial regulators, should conduct continuing investor education designed to protect ordinary people against abuse and fraud in saving and investing.

IV. AN EVALUATION OF SEC INVESTOR EDUCATIONAL INITIATIVES

This Part of the Article evaluates the SEC's investor educational initiatives from the above theoretical framework. It focuses on the SEC because the Commission has been the most active federal agency in this area. Most of these initiatives significantly extend the SEC's traditional mission, which is, simply put, disclosure related to securities transactions.¹⁹⁵ It is one thing for the SEC to ensure that companies offering and selling securities, or engaged in transactions affecting their securities, disclose, among other things, information about their business, management, the features of the securities and any major transactions. It is quite another thing for the SEC to train consumers how to save and to invest, which involves their intelligent use of the disclosed information. Any SEC education about fraud or abusive practices, however, is less of a regulatory stretch, since it is ancillary to the SEC's law enforcement role.

The current SEC chairman (1993 to present), Arthur Levitt, has been the catalyst for the SEC's educational initiatives. In 1993 he established an Office of Investor Education and Assistance and has himself reached out to ordinary investors through town meetings (a format popular with the man who appointed him, President Clinton).¹⁹⁶ Under his direction, the Office prepares educational pamphlets for consumers, makes them available on its Web site, has recently been engaged in a national (and even international) investor education campaign and has itself greatly increased the contact between the SEC and ordinary consumers, through electronic and other means.¹⁹⁷ It has also been involved in an important initiative to simplify the language of all disclosure documents filed with the SEC, by

¹⁹⁵ See generally ANNE M. KHADEMIAN, *THE SEC AND CAPITAL MARKET REGULATION: THE POLITICS OF EXPERTISE* 83-87 (1992) (discussing the enforcement of SEC disclosure regulations).

¹⁹⁶ See *Permanent Subcomm. on Investigations of the Senate Comm. on Government Affairs*, 105th Cong. 18 (1997) (statement of Arthur Levitt, Chairman, SEC) (describing town meetings as "typically well-attended (often over 1,000 investors attended each meeting) and feature a series of seminars for investors on a wide variety of topics").

¹⁹⁷ See *infra* Part IV(A).

transforming them into "plain English."¹⁹⁸ In addition, the SEC's Division of Investment Management, which oversees the mutual fund industry, has recently sought to make mutual fund disclosure more instructive for consumers by focusing on important fund issues and facilitating the comparison of funds.¹⁹⁹ The SEC staff has even suggested that, given the subject's importance, Congress pass legislation on investor education.²⁰⁰

These SEC educational efforts may be little more than a passing political trend²⁰¹ and, from a "public choice" perspective, an example of an often-used strategy of regulatory agencies justifying their existence by dramatizing an issue that demands their regulatory intervention.²⁰² Yet the SEC, as the primary government agency regulating the securities markets, *should* be involved in investor education and should expand its disclosure mission to include education. The pressures leading to the importance of investor education—the problems with Social Security, the growth of defined contribution plans, and the decline of saving in the United States, amid changing demographics²⁰³—are not of the SEC's making. The focus on disclosure was appropriate when few Americans were investors and they mainly relied upon full-service brokers; it is inadequate when investing has become an everyday, yet important, activity for over half of the American population, many of whom invest without a financial professional. The SEC would also incur considerable political risk if its lack of attention to education contributed to a market disaster (e.g., small investors left financial markets in a panic in a market downturn or out of concern of market fraud, partly because of their educational deficiencies).²⁰⁴

¹⁹⁸ See *infra* Part IV(B).

¹⁹⁹ See *infra* Part IV(C).

²⁰⁰ See Christine Williamson, *ICI Talks Up Education, Expectations, PENSIONS & INVESTMENTS*, June 9, 1997, at 35 ("Barry P. Barbash, director of the Division of Investment Management . . . warned if the industry does not itself regulate its educational efforts and provide more disclosure, and regulators are unable to persuade vendors to provide more information, Congress will be forced to deal with investor education, particularly as it relates to retirement planning.").

²⁰¹ Democratic administrations often exhibit classic American populism in government, which translates into renewed SEC regulatory attention to the small investor. See, e.g., SELIGMAN, *supra* note 55, at 548-50 (discussing initiatives after the election of Jimmy Carter). Since, under present political conditions with a Republican-controlled Congress, the Democratic administration is wary of proposing significant market regulatory initiatives, investor education is a politically acceptable program; it emphasizes aid to small investors pleasing to Democratic populists and the self-help orientation acceptable to free-market Republicans.

²⁰² See, e.g., Jonathan R. Macey, *Administrative Agency Obsolescence and Interest Group Formation: A Case Study of the SEC at Sixty*, 15 CARDOZO L. REV. 909, 914 (1994). This "crisis" presentation does at times characterize the SEC's "plain English" initiative. See *infra* Part IV(B).

²⁰³ See *supra* Part II(A).

²⁰⁴ See Langevoort, *supra* note 177, at 530 (discussing risk aversion by regulators).

The SEC likely now has the regulatory authority to be involved in investor education, although its staff's references to the possible need for legislation may reflect their acknowledgment that the pertinent statutes do not clearly address this issue. This authority is arguably incidental, and even unnecessary, to the SEC's statutory mission in various securities acts to ensure adequate disclosure in the public interest.²⁰⁵ If many ordinary investors can not even understand how disclosed information relates to investing, disclosure cannot achieve its communicative purpose.²⁰⁶ Moreover, if the central purpose of the Securities Exchange Act of 1934 is to create "fair and honest [securities] markets,"²⁰⁷ this purpose cannot be achieved without investors being educated not only about fraud, but also about the functioning of these markets, the securities traded on them, the role of the markets in personal investing and wealth creation—in short, about all of the knowledge that investor education should impart.

While the SEC's educational efforts have been useful, it could greatly improve them if it redirected its activities, in accordance with the Article's guidance, to concentrate on anti-fraud education and to do more to promote and facilitate the educational services of financial and nonprofit firms.²⁰⁸ In the general educational materials and activities of the Office of Investor Education and Assistance, the SEC appropriately educates consumers about illegal and abusive practices in financial services and markets, and usefully provides means for consumers to contact it about these practices. Yet its saving and investing education does not measure up to the educational activities of private firms. Therefore, this education should be redesigned to be part of a federal government campaign to encourage saving and investing, and to publicize and facilitate access to private educational resources and services while still itself providing investors with basic

²⁰⁵ See, e.g., 15 U.S.C. § 77g (1994) (empowering the SEC to determine what information is needed in registration statements as being "necessary or appropriate in the public interest or for the protection of investors"); 15 U.S.C. § 78m (empowering the SEC to require the filing of information "as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security"); 15 U.S.C. § 80a-1(b)(1) (justifying regulation of mutual funds because investors purchase their securities "without adequate, accurate, and explicit information, fairly presented").

²⁰⁶ That many ordinary investors do not read disclosed information and instead rely on market price and recommendations of financial professionals would not change the analysis, for the securities acts do not authorize the SEC to assume that only professionals participate in securities markets and that all ordinary investors hand their portfolios over to professionals—a situation that, in any case, bears no connection to reality.

²⁰⁷ See 15 U.S.C. § 78b; see also COX, *supra* note 8, at 653-55.

²⁰⁸ A general problem with the SEC's educational efforts is that, unlike market participants, the SEC does not fully feel cost pressures, although Congress reviews its budget and it is required both to review its regulations from a cost/benefit perspective and to consider the burdens they imposes upon businesses. See, e.g., Small Business Regulation Fairness Act of 1996, Pub. L. No. 104-121, 110 Stat. 857 (1996) (encouraging the effective participation of small businesses in the federal regulatory process). *But see* KRIPKE, *supra* note 4, at 59 (contending that the SEC's cost/benefit analysis is often perfunctory).

saving and investing norms. The SEC's "plain English" initiative and mutual fund disclosure simplification and presentation exhibit a valuable partnership with the financial services industry, which will allow consumers to understand basic information about investing in a format to which they can easily apply the investor education provided by others. The SEC, however, should explicitly recognize the necessary relationship between the consumer-oriented disclosure and the firms' educational services and make the firms link their disclosure documents to these services. Finally, the SEC should begin a sustained reflection on its role in investor education and heighten awareness of education's importance by issuing a "concept release" on investor education, and inviting comment from all those involved and interested in the subject.²⁰⁹

A. <www.sec.gov/invkhome>

The "Investor Assistance & Complaints" section of the SEC's Web site,²¹⁰ the "virtual home" of the Office of Investor Education and Assistance, exemplifies both the usefulness of the SEC's investor education efforts and its need for redirection. The introduction by the Office's Director suggests its educational ambitions: "We provide a variety of services to address the problems and questions you may face as an investor. We cannot tell you what investments to make, but we can tell you how to invest wisely and protect your hard earned investment dollars from securities fraud or abuse."²¹¹ In much of its material, the Office appropriately provides education about fraud and questionable financial practices, particularly by finance professionals, and facilitates communication from consumers to the SEC. The Office, for example, urges investors to contact the SEC if they have "suffered wrongdoing at the hands of a bad broker or investment ad-

²⁰⁹ In a companion piece, I argue that, once it has refocused its saving and investing educational activities, the SEC should do more to teach people about governance and corporate morality. See Fanto, *supra* note 51.

²¹⁰ See *Investor Assistance & Complaints* (last modified August 21, 1998) <<http://www.sec.gov/invkhome.htm>> [hereinafter *Investor Assistance & Complaints*]. The SEC also provides the information on its Web site in written materials that it distributes.

²¹¹ Nancy M Smith, *The SEC's Office of Investor Education and Assistance* (last modified August 7, 1997) <<http://www.sec.gov/consumer/abotoiea.htm>> [hereinafter *SEC's Office of Investor Education and Assistance*] (the section's hypertext links lead to other documents whose titles suggest the SEC's educational ambitions: *About the Office of Investor Education and Assistance*, *Ask Questions*, *Invest Wisely: Advice From Your Securities Industry Regulators*, *Invest Wisely: An Introduction to Mutual Funds*, *How to Use the Edgar Database of Corporate Information*, *SEC Division of Enforcement Complaint Center*); see also *Investor Assistance & Complaints*, *supra* note 210. The SEC also provides hypertext links to other government, SRO and nonprofit Web sites of interest. See, e.g., *Other Sites of Interest* (last modified June 18, 1998) <<http://www.sec.gov/others.htm>> [hereinafter *Other Sites*] (listing other U.S. government, market regulator, self-regulatory organization, educational institution and professional organization Web sites).

viser”²¹² The section also provides links to the SEC’s Division of Enforcement complaint hotline and to Division notices that alert investors about recent questionable financial practices or investments targeted at consumers.²¹³

The SEC does not limit its educational efforts, however, to fraud prevention but also offers general saving and investing education; one of the purposes of the Office is, after all, to tell people “how to invest wisely.”²¹⁴ It is unquestionably difficult for the agency to conduct anti-fraud education without saying something about investing, investments and securities markets. Yet the SEC’s saving and investing education is uneven when compared to the educational materials of financial and nonprofit firms, because the SEC has not always identified what kind of investor it is addressing (i.e., sophisticated vs. unsophisticated). Furthermore, the SEC sometimes mixes elementary points about investing with issues demanding some sophistication.

The SEC’s most basic educational brochure, *What Every Investor Should Know*, has a clear, useful discussion of securities markets, basic financial instruments, investment companies and instructions about opening brokerage accounts and stock trading.²¹⁵ Yet in the

²¹² SEC’s Office of Investor Education and Assistance, *supra* note 211. The Web site also observes that investor complaints may lead to investigations and expose such obvious fraudulent practices as “a bad broker, an illegal boiler-room operation, a ponzi scheme or an insider trading ring.” *Id.* This quotation exhibits an occasional problem in the SEC’s educational materials: the SEC fails to explain what it is talking about. Do all investors, for instance, understand what a “ponzi scheme” is?

²¹³ See *Investor Assistance & Complaints*, *supra* note 210. To target specifically “cold calling,” for example, the SEC recently prepared a pamphlet (on-line and in written form) that explains to investors cold calling and the kinds of firms from which it is practiced, alerts them to cold-calling tactics and advises them of their rights and organizations to contact for help. See *Cold Calling* (last modified June 16, 1998) <www.sec.gov/enforce/alerts/coldcall.htm>.

²¹⁴ SEC, *Ask Questions* (last modified June 16, 1998) <<http://www.sec.gov/consumer/askqinv.htm>> [hereinafter *Ask Questions*]. Even these materials include education on fraud prevention. For example, the brochure entitled *Ask Questions* gives consumers a list of questions to ask brokers or financial professionals, some of which are designed to head off abusive practices and prepare the investor for the psychological pressure exerted by brokers. See *id.* The advice is sometimes comically paternalistic. See *id.* (“Taking notes [in response to answers to questions] also sends a signal to your broker: I’m a smart and serious investor who wants to know more about the risks and rewards of investing.”). It also strains credulity that a dishonest broker would answer some of the SEC’s suggested questions truthfully (e.g., “Is this purchase really in my best interest, or are you trying to win a prize?”). See *id.* The brochure *Invest Wisely: Advice From Your Securities Industry Regulators* similarly gives the kind of basic information about detecting fraud that one would expect from a securities market “cop”: “NEVER send money to purchase an investment based simply on a telephone sales pitch . . . NEVER make a check out to a sales representative . . . BE ALERT FOR: Representations of spectacular profit, such as, [y]our money will double in six months . . . Remember, if it sounds too good to be true, it probably is!” *Invest Wisely: Advice From Your Securities Industry Regulators* (last modified December 12, 1997) <<http://www.sec.gov/consumer/inws.htm>> [hereinafter *Advice from Your Securities Industry Regulators*] (emphasis in original).

²¹⁵ See *What Every Investor Should Know: A Handbook from the U.S. Securities and Exchange Commission* (last modified October 21, 1996) <<http://www.sec.gov/consumer/weisktc.htm>> [hereinafter *What Every Investor Should Know*]. This brochure also discusses

Ask Questions brochure, a consumer is given a list of useful questions to ask about financial products, the progress of investments and problems with brokers, but many of them make little sense unless the investor is already familiar with basic finance concepts, such as asset allocation, diversification and risk, that are absent from the brochure (and are not found on the SEC's Web site).²¹⁶ Moreover, in its *Invest Wisely* brochure on brokers, after disclaiming that it will provide any general investor education,²¹⁷ the SEC offers consumers its own investing advice ranging from simple anti-fraud remarks²¹⁸ to statements requiring some finance knowledge²¹⁹

Despite their problems, these SEC saving and investing educational efforts involve only the limited activity of organizing and maintaining a Web site and printing documents, which also supply useful anti-fraud education. An obvious answer to the above criticisms is that the SEC spend *more* time, effort and money on saving and investing education, particularly on finance and investing strategies.²²⁰ Although Chairman Levitt has admirably tried to make the SEC more responsive to the needs of consumers, the SEC can not produce educational products and services superior to those supplied by private firms in a highly competitive environment. The SEC staff

SEC supervision of brokers and other financial professionals, which brings it within the SEC's anti-fraud ambit. *See id.*

²¹⁶ *See Ask Questions, supra* note 214 ("Does this investment match my investment goals? . . . Why is this investment suitable for me? . . . What are the specific risks associated with this investment? . . . What is the maximum I could lose?") Similarly, while the brochure *What Every Investor Should Know* provides useful descriptions of basic financial instruments, as well as a glossary of investment terms, it, too, offers little finance explanation. *See e.g., What Every Investor Should Know: Section 4. How to Choose an Investment* (last modified October 22, 1996) <<http://www.sec.gov/consumer/weisk/weisk4.htm>> [hereinafter *How to Choose an Investment*] ("One of the more basic relationships in investing is that between risk and reward. Very often, investments that offer potentially high returns are accompanied by relatively higher risk factors. It is up to you to decide how much risk you can assume.")

²¹⁷ *See Advice from Your Securities Industry Regulators, supra* note 214 (encouraging readers to get "[i]nformation regarding the fundamentals of investing and basic financial terminology . . . at your local library."); *see also How to Choose an Investment, supra* note 216 (referring investors to other sources for information about securities, while downplaying the obvious sources, such as financial services firms).

²¹⁸ *See Advice from Your Securities Industry Regulators, supra* note 214 ("Investments in securities issued by a company with little or no operating history or published information may involve greater risk.")

²¹⁹ *See Advice from Your Securities Industry Regulators, supra* note 214 ("The higher the expected rate of return, the greater the risk . . . In some cases, such as partial or two-tier tender offers, failure to act can have detrimental effects on your investment."); *see also Invest Wisely: An Introduction to Mutual Funds* (last modified Oct. 21, 1996) <<http://www.sec.gov/consumer/inwsmf.htm>> [hereinafter *An Introduction to Mutual Funds*] (warning that "[a]lthough past performance is not a reliable indicator of future performance, volatility of past returns is a good indicator of a fund's future volatility," while also stating in a simple maxim, "[a] mutual fund is a company that brings together money from many people and invests it in stocks, bonds, or other securities").

²²⁰ *See Investor Assistance & Complaints, supra* note 210 (promising more information, which could include more general education: "More To Come! Watch this space for future developments!").

simply lacks the continuous contact with consumers, the strong profit motive and/or the need to justify its existence that would enable it to design and tailor general educational efforts to consumers' needs.²²¹

More importantly, extensive education efforts, as well as any substantial increase in these efforts, distract the SEC from the tasks for which it is better suited. The SEC should continue to focus the investor assistance section of its Web site and general investor publications on alerting investors about new and regularly occurring kinds of securities fraud and abuse, as it has successfully done. It should also perform the significant "cheerleading" function of encouraging consumers to save and invest, a function that (as the PWBA has demonstrated) is appropriate for government agencies, but that, until recently, the SEC has all but ignored in its educational materials.²²² The SEC has several brochures describing itself and its regulatory authority that could contribute to this educational function.²²³ For example, in outlining its authority over new securities issuances and securities trading, the SEC could also describe the importance of private securities markets and personal investing for the economy and the well-being of citizens. The SEC should not underestimate the effect that publicizing its regulatory authority will have on encouraging saving and investing, for evidence suggests that consumers are encouraged to invest if they realize that securities markets are subject to laws and that an active agency is enforcing them.²²⁴

The SEC should therefore conduct saving and investing education as ancillary to its fraud prevention education and to its "cheerleading" activities so as to drive home to investors saving and investing norms.²²⁵ Rather than attempting to design the optimal educational product, the SEC would do better to consult with the financial industry on its members' educational products, encourage continued product and services development and review educational materials

²²¹ Even nonprofit organizations, like AAIL, owe their very existence to satisfying the needs of individual investors and thus have a strong motive to design services attractive to them.

²²² In his town meetings, however, Chairman Levitt has always admirably performed this "promotional" educational task.

²²³ See, e.g., *The U. S. Securities and Exchange Commission: What It Is, What It Does* (last modified November 18, 1996) <<http://www.sec.gov/asec/asecart.htm>>; *The Work of the SEC* (last modified August 5, 1997) <<http://www.sec.gov/asec/wot.htm>>.

²²⁴ See RAFAEL LA PORTA ET AL., LAW AND FINANCE 40-42 (National Bureau of Econ. Research Working Paper No. 5661, 1996) (describing importance of law in permitting capital markets to function); Rafael La Porta et al., *Legal Determinants of External Finance*, 52 J. FIN. 1131, 1149-50 (1997) (same).

²²⁵ For example, in summarizing its oversight over mutual funds and investment advisors, the SEC could briefly discuss the nature of a mutual fund, the kinds of funds, and their basic features and advantages. The SEC could also combine some of its current brochures into an "investor's handbook" that explained the SEC's regulation of different investment products and markets and provided an elementary description of them.

for any abuses.²²⁶ In addition, it should limit itself to echoing several basic, but important, saving and investing rules.²²⁷ Indeed, the SEC exemplified the correct balance between promoting saving and investing and conducting basic investor education in its sponsorship of a week-long "Facts on Saving and Investing Campaign" from March 29 to April 4, 1998, with the participation of other government agencies, state securities regulators, consumer organizations and financial industry trade groups.²²⁸ Not only did the SEC and the other participants focus on simple saving and investing norms through high visibility events,²²⁹ but it also produced educational materials designed to convey and reinforce these norms.²³⁰

Most importantly, the SEC should inform consumers that financial and nonprofit firms are supplying investor education, and repeatedly encourage them to use these educational materials and services. As a regulator, the SEC may not think it appropriate to publicly high-

²²⁶ In fact, the SEC should undertake a general review of educational materials produced by consumer financial services firms for abuses or irregularities in them. Cf. Ellen E. Schultz, *Employees Looking for Advice on 401(k)s Often Face Obstacles*, WALL ST. J., Feb. 6, 1998, at C1 (discussing potential abuses in investor education relating to mutual fund expenses and fees).

²²⁷ See, e.g., Securities Industry Association, *Understanding Market Risks: What Every Investor Should Know*, at 1 (visited Sept. 15, 1998) <http://www.sia.com/investor_information/html/publications.html> (referring to consultations with the SEC's Office of Investor Education and Assistance in preparing the brochure). While there is no great need for the SEC to recommend to consumers a particular investment strategy, in its general educational messages the SEC could give warnings to the effect that, despite the many different investing strategies, it is difficult for any one person (including a professional) consistently to beat the market and that diversification should characterize most investors' portfolios. See Stout, *Costly Casinos*, *supra* note 88, at 692 n.271 ("The government might, however, require all stocks to carry the following label: 'WARNING: Self-Selection Ensures that You Probably Are Not Going To Be as Talented at Trading as You Think You Might Be.'"); Robert B. Thompson, *Securities Regulation in an Electronic Age: The Impact of Cognitive Psychology*, 75 WASH. U. L.Q. 779, 782 (1997) (discussing possible investor warnings to address cognitive weaknesses and pressures resulting from the use of framing in securities regulations). In fact, the SEC occasionally makes such statements in its materials. See, e.g., *How to Choose an Investment*, *supra* note 216 ("Don't speculate. Speculation can be a useful investment tool for those who can understand and manage the risks involved and those who can afford to lose money. For the average investor, more conservative investment strategies are generally appropriate."); *An Introduction to Mutual Funds*, *supra* note 219 (suggesting that higher expense funds are not necessarily more profitable, which is an indirect reference to the benefits available from no-load, index funds).

²²⁸ See *Overview: Get the Facts. It's Your Money. It's Your Future* (last modified Feb. 24, 1998) <<http://www.sec.gov/consumer/cosra/about/facts.htm>> (describing campaign, campaign partners, events in nearly twenty states). The campaign, in fact, involved activities in twenty-one countries in the Western Hemisphere, which highlights the growing importance of investor education in other countries as market capitalism increases worldwide.

²²⁹ See, e.g., *id.* (describing SEC-hosted National Roundtable on Saving and Investing on Mar. 30, 1998).

²³⁰ See, e.g., SEC, *Get the Facts on Saving and Investing: A Roadmap to Start You on a Journey to Financial Security Through Saving and Investing* (visited Sept. 15, 1998) <<http://www.sec.gov/consumer/cosra/brochure.htm>> (providing some basic guidelines on saving and investing, such as a financial plan, the benefits of saving, elementary concepts of investing, fundamentals about mutual funds and brokers and ways to avoid fraud and abuse). Moreover, the SEC's campaign Web site provides a hyperlink to the site for the Alliance for Investor Education.

light the educational efforts of a particular firm.²³¹ Yet it now refers investors, by hypertext links on its Web site, to other Web sites that might be of interest to them. Some of these “quasi-public” sites, like those of the NYSE and the NASD, have good educational materials.²³² The SEC could take the additional step of openly referring investors, with appropriate disclaimers, to these sites and to others, such as those of trade groups.²³³ It should then encourage the SROs and trade groups to point consumers to excellent sites of their member firms, which would give an additional spur to the already existing firm competition to provide consumer educational services.²³⁴

B. Plain English

The “plain English” movement began in law over a decade ago.²³⁵ Its appearance in securities regulation is again due to the particular interest of Chairman Levitt and to the fact that, since investing is now a consumer area, adequate communication to ordinary investors is critical, just as it was earlier in leases, loans and insurance contracts. The more specific reason for the SEC’s attention to “plain English” came from the results of a report of a task force of private and government lawyers studying simplification of securities disclosure.²³⁶ Recognizing that much disclosure language was opaque, the

²³¹ As noted below, in its “plain English” initiative, the SEC does publicly praise private firms that have produced plain English disclosure documents. Since many educational materials now exist, the SEC may fear slighting one or more firms by omitting mention of their educational materials if it lists those of other firms.

²³² The SEC also has a hyperlink with the ASEC. See *Other Sites*, *supra* note 211.

²³³ The SEC’s “Facts on Saving and Investing Campaign” clearly involved the highlighting for consumers of the availability of private investor educational resources, if only because of the involvement therein of many financial industry trade groups and consumer organizations specializing in advising consumers on saving and investing. Moreover, Chairman Levitt has recently publicly praised the educational activities of private firms. See *Remarks by Arthur Levitt, U.S. Securities and Exchange Commission* (May 15, 1998) (visited Sept. 15, 1998) <<http://www.sec.gov/news/speeches/spch212.txt>> [hereinafter *Levitt Remarks*]. Is it too much to suggest that he may have taken some inspiration for this recent focus from a reading of an earlier draft of this Article? See Letter from Arthur Levitt, Chairman, SEC, to James A. Fanto, author (Mar. 24, 1998) (thanking author for article).

²³⁴ SROs or trade groups, like the ICI or the Securities Industry Association, could periodically highlight and praise the educational materials of one or more firms or firms’ educational innovations.

²³⁵ See Plain English Disclosure, Securities Act Release No. 7380, 62 Fed. Reg. 3152, 3154 (Jan. 21, 1997) [hereinafter *Proposing Release*] (to be codified at 17 C.F.R. pt. 228, 229, 230 and 239). For a general discussion of the legal “plain language” movement, see LAWRENCE M. SOLAN, *THE LANGUAGE OF JUDGES* 118-38 (1993).

²³⁶ See SEC, *REPORT OF THE TASK FORCE ON DISCLOSURE SIMPLIFICATION* (1996) [hereinafter *DISCLOSURE SIMPLIFICATION*]. Appointed by Chairman Levitt, the task force was chaired by a private lawyer, Philip Howard, a named partner in Howard, Darby & Levin and author of the book, *DEATH OF COMMON SENSE*, and included staff members from different SEC divisions.

task force recommended that the SEC “enhance [the] readability [of disclosure documents] by individual investors.”²³⁷

It is difficult *not* to regard the SEC’s “plain English” initiative with some cynicism. The “crisis” of opaque disclosure will lead to more work (and continued employment) for the securities bar and SEC staff—that is, for those who are in large part responsible for the obfuscatory legalese in disclosure documents in the first place.²³⁸ The initiative also confirms the late Professor Kripke’s observation that, since lawyers, rather than economists and finance professionals, are most influential in the SEC staff, the agency invariably emphasizes the importance of law and rhetoric, rather than economics and finance, in its regulations.²³⁹ Even if the SEC staff and securities lawyers should shoulder much of the blame for a securities disclosure that generates opaque documents, they are at least trying to remedy the problem.²⁴⁰

The SEC’s “plain English” initiative not only helps simplify disclosure, but also highlights the importance of, and contributes to, in-

²³⁷ *Id.* at 17 (“Develop a ‘plain English’ introduction to the prospectus to enhance its readability by individual investors, by eliminating boilerplate ‘legalese’ and requiring a summary of key information.”) (emphasis in original); *see also* Proposing Release, *supra* note 239, at 3152 n.17.

²³⁸ For example, Howard, Darby & Levin is primarily a securities firm, and the SEC acknowledges the help of securities lawyers in its “plain English” initiative. *See, e.g.*, SEC, *A Plain English Handbook: How to Create Clear SEC Disclosure Documents* (visited Sept. 15, 1998) <<http://www.sec.gov>> [hereinafter *Plain English Handbook*] (listing securities lawyers who aided the SEC’s efforts). The SEC downplays that the state of disclosure documents owes much to the bar’s compliance with SEC regulations and the staff’s guidance. *See, e.g.*, Proposing Release, *supra* note 235, at 3153-54 (“Recognizing that many of our rules have contributed to the legalistic language and tone of these documents . . .”, but describing at length its numerous attempts through the years to require companies to simplify disclosure). The securities bar, however, has not been uniform in its support of the initiative. *See, e.g.*, *Letter of Committee on Securities Regulation of the Business Law Section of the New York State Bar Association to the Securities and Exchange Commission* (Mar. 21, 1997) (visited Sept. 15, 1998) <<http://www.sec.gov/rules/proposed/s7397/gutmall.htm>> (offering qualified support for the initiative); *Letter of Committee on Federal Regulation of Securities, Section of Business Law of the American Bar Association to the Securities and Exchange Commission* (Mar. 31, 1997) (visited Sept. 15, 1998) <<http://www.sec.gov/rules/proposed/s7397/liftin1.htm>> (questioning aspects of initiative).

²³⁹ *See* KRIPKE, *supra* note 4, at 18. “Plain English” is, in fact, a way for rhetorically-trained lawyers to reassert their usefulness and expertise in an investment world dominated by mathematicians and economists. The SEC’s writing and organizing recommendations at times appear to come from high school English teachers who are not particularly conversant with, and somewhat fearful of, the latest computer technology. *See Plain English Handbook, supra* note 238, at 55 (recommending that a writer take sections of a disclosure document and “tape or tack to the wall the pages” as an aid in considering the best order of presentation). The drafters seem to be unaware of word processing programs that allow multiple configurations of documents.

²⁴⁰ In the past, the SEC has urged practitioners to write simpler disclosure documents. *See, e.g.*, Clarification of Prospectuses, Securities Act Release No. 4844, 31 Fed. Reg. 10,667, 10,668 (Aug. 11, 1966) (“The chief goal of registration is disclosure for the benefit of investors and that involves, among other things, the use of language that can be understood readily by the persons to whom it is addressed. Failure to use language that is clear and understandable by the investor may operate to defeat the purpose of the prospectus.”) (footnote omitted).

vesting education.²⁴¹ Simplifying information to promote effective communication in securities disclosure inevitably raises questions as to whether consumers have the necessary background or "culture" to understand even this information.²⁴² Yet the SEC does not always squarely face, nor clearly think through, the connections between the initiative and investor education. Thus, the initiative's educational implications appear haphazardly, with the result that educational tasks are inappropriately placed upon parties, such as individual companies, when others, such as financial services firms, are already performing them. Unless it is integrated into a well-conceived SEC educational initiative, "plain English" will simply be "window dressing," bringing few ordinary people into the investment world.

In the "plain English" releases,²⁴³ the SEC appears not to realize fully the educational implications of its initiative, and thus offers confusing signals to companies preparing disclosure documents. It states that "plain English" and disclosure simplification involve clarifying language and improving presentation. Since a disclosure document addresses investors with different levels of financial sophistication,²⁴⁴ the SEC requires that a company generally adopt language understandable to the least sophisticated among them and presentation techniques that satisfy both sophisticated and unsophisticated investors. Under the final rule, a company must use "plain English" writing principles in initial parts of prospectus, where a company often summarizes important information, and ensure that the language and presentation of the rest of the document are "clear, concise, and understandable."²⁴⁵ There is no question that the SEC's "plain English"

²⁴¹ Others have discussed the advantages and disadvantages of "plain English." See, e.g., SOLAN, *supra* note 235, at 129-38 (discussing misguided effort to simplify necessary legal complexities).

²⁴² The Task Force on Disclosure Simplification made this connection. See DISCLOSURE SIMPLIFICATION, *supra* note 236, at 17 (observing that in prospectuses "[t]rivial points sometimes receive as much attention as material information, and in the end may bury points significant to an investment decision" and recommending better writing and presentation to remedy the problem; but also making the general educational recommendation, i.e., "the use of a 'plain English' glossary to explain technical terms used in the document."). See, e.g., Isaac C. Hunt, Jr., *Plain English—Changing the Corporate Culture*, 51 U. MIAMI L. REV. 713, 714 (1997) (quoting a Commission member observing that disclosure does not achieve its purpose if it fails to communicate with the investor).

²⁴³ See Plain English Disclosure, Securities Act Release No. 7497, 63 Fed. Reg. 6370 (Feb. 6, 1998) [hereinafter Final Release] (to be codified at 17 C.F.R. 228, 229, 230, 239 and 274); Proposing Release, *supra* note 235.

²⁴⁴ See Proposing Release, *supra* note 235, at 3155 ("The educational background and financial sophistication of your current or prospective investors should dictate the language you use."). The Final Release omits discussion of kinds of readers, but implies that the new disclosure will reach a wider audience, i.e., consumers. See Final Release, *supra* note 243, at 6370 ("Prospectuses will be simpler, clearer, more useful, and we hope, more widely read.").

²⁴⁵ Final Release, *supra* note 243, at 6384. Under the adopted "plain English" rule, a company must use "plain English principles in the organization, language, and design of the front and back cover pages, the summary, and the risk factors section" of a prospectus. *Id.* These principles are six: "(i) Short sentences; (ii) Definite, concrete, everyday words; (iii) Ac-

writing principles and clarification standards, which are the foundations of good writing, will lead to, and have produced clearer, more understandable disclosure.²⁴⁶ Yet the examples of the "plain English" or clarifying redrafting of poor prospectus disclosure, although much better written,²⁴⁷ do not always help an ordinary investor who is unfamiliar with many financial, accounting and business terms in the prospectus or with investing in general.²⁴⁸

The SEC suggests the educational implications of its initiative when, like the Disclosure Task Force, it recommends the inclusion of glossaries in prospectuses for "[t]erms that are not clear from the context [and to] facilitate understanding of the disclosure."²⁴⁹ But its support for these tools is qualified because it fears that reliance on glossaries and the necessary cross-references will interrupt the flow of writing and discourage ordinary investors from reading the documents (since it takes time and effort to move back and forth through them), although these are the very people that a glossary is designed to help. Rather, the SEC recommends that documents provide, at appropriate places, a "concise explanation" of complex provisions or terms.²⁵⁰ Yet the SEC's examples of explanations would not effect complete communication to the financially uneducated. It is not always clear where any particular explanation would stop and this recommendation does not entirely avoid the problem of cross-references. The SEC offers yet another standard, which states that a company

tive voice; (iv) Tabular presentation or bullet lists for complex material, whenever possible; (v) No legal jargon or highly technical business terms; and (vi) No multiple negatives." *See id.* at 6384. The rule encourages the use of pictures and charts to make this part of the document accessible to ordinary investors. As for the rest of the prospectus, the rule demands that a company present the information in a prospectus "in a clear, concise and understandable manner," following four standards: (1) "Present . . . clear, concise sections, paragraphs, and sentences . . . [with the use of] . . . short, explanatory sentences and bullet lists; (2) Use descriptive headings and subheadings; (3) Avoid frequent reliance on glossaries or defined terms as the primary means of explaining information in the prospectus. . . ; (4) Avoid legal and highly technical business terminology." *See id.*

²⁴⁶ *See* DIVISION OF CORPORATION FINANCE ET AL., BEFORE & AFTER EXAMPLES FROM THE PLAIN ENGLISH PILOT PROGRAM AND A *PLAIN ENGLISH HANDBOOK* (1998) [hereinafter BEFORE & AFTER EXAMPLES] (contrasting disclosure before and after it was rewritten with "plain English" writing principles); *see also* Proposing Release, *supra* note 235, at 3156-58 (giving similar examples). Numerous companies participated in a "pilot program" to use "plain English" in their disclosure documents. *See* Final Release, *supra* note 243, at 6370.

²⁴⁷ *See, e.g.,* Proposing Release, *supra* note 235, at 3156-58.

²⁴⁸ For example, the rewritten sentence "[o]ur losses were caused, in part, by the annual write-off of a portion of the goodwill resulting from the ten acquisitions we made during this period" does not communicate much to an investor who has no knowledge of accounting. *See* Proposing Release, *supra* 235, at 3157, 3159 (declining to discuss how to improve disclosure of financial ratios, which clearly raises the question of explanations to unsophisticated investors).

²⁴⁹ *See* Proposing Release, *supra* note 235, at 3159.

²⁵⁰ *See id.; see also* Final Release, *supra* note 243, at 6384 ("[A]void frequent reliance on glossaries or defined terms as the primary means of explaining information in the prospectus. Define terms in a glossary or other section of the document only if the meaning is unclear from the context. Use a glossary only if it facilitates understanding of the disclosure . . .").

should “[a]void legal and highly technical business terminology.”²⁵¹ The elimination, rather than the explanation, of complex information does not enhance effective communication. And the SEC affirms that “plain English does not mean ‘dumbing down’ complex information.”²⁵²

In its *Plain English Handbook: How to Create Clear SEC Disclosure Documents*,²⁵³ the SEC acknowledges the connection between disclosure simplification and investor education, without giving much guidance on how far the education should extend.²⁵⁴ The Handbook states that a “plain English” document must satisfy the needs of the audience²⁵⁵ and thus recommends that a company identify its investors and ask such questions as “How familiar are they [i.e., typical investors] with investments and financial terminology? [and] What investment concepts can you safely assume they understand?”²⁵⁶ Recognizing that unsophisticated investors are ubiquitous in the public securities market, the Handbook assumes that disclosure *must* target *and* educate them. A company can do this, while still addressing sophisticated investors, by making “basic, *educational* information visually distinctive from the rest of the text”²⁵⁷ The Handbook also recommends that a company take an explicitly educational approach in the organization of its disclosure documents.²⁵⁸ The Handbook does not merely recommend eliminating “jargon and legalese,” but observes that, when there is “no plain English alternative” for a word or term, the company should provide a meaningful explanation of it.²⁵⁹ Yet the Handbook does not indicate how much background information a company must provide for financially unsophisticated

²⁵¹ Final Release, *supra* note 243, at 6384.

²⁵² Proposing Release, *supra* note 235, at 3155; *see also* Final Release, *supra* note 248, at 6374 (“Using plain English does not mean omitting important information. These rules only require you to disclose information in words investors can understand and in a format that invites them to read the document.”).

²⁵³ *Plain English Handbook*, *supra* note 238.

²⁵⁴ Warren Buffett, who wrote the Handbook’s preface, underscores its educational purpose in his explanation that, when writing Berkshire Hathaway’s annual report, he imagines that he is addressing his sisters who, “[t]hrough highly intelligent . . . are not experts in accounting or finance.” *Id.* at 2.

²⁵⁵ *See id.* at 5 (“Plain English means analyzing and deciding what information investors need to make informed decisions, before words, sentences, or paragraphs are considered. A plain English document uses words economically and at a level the audience can understand.”).

²⁵⁶ *Id.* at 9. It even tells companies to ask: “What are [investors’] demographics—age, income, level of education, and job experience?” *Id.*

²⁵⁷ *Id.* at 10 (emphasis added). The SEC observes that some companies know, through their investor relations department, the exact demographics of their investors. *See id.* at 9. Few public companies, however, are likely to have only *financially* sophisticated investors as capital providers.

²⁵⁸ *See id.* at 16 (“[Y]our audience’s degree of investment expertise will also affect how you organize the document. If you are writing for financially unsophisticated investors, your document’s overall organization may take an *educational* approach. You may need to explain industry terms or concepts where they first appear.”) (emphasis added).

²⁵⁹ *Id.* at 30.

investors or how many different kinds of investors it must target in its disclosure.

The SEC's "plain English" initiative thus potentially places vague educational requirements on all companies selling securities that do not have the justification traditionally offered for mandatory disclosure. Even more importantly, these requirements do not take account of the market reality that financial firms and others are already providing educational services and products. Mandatory disclosure has always provoked considerable debate and disagreement,²⁶⁰ but scholars and practitioners have generally agreed that it makes sense when it requires companies to provide easily verifiable and comparable information for the sophisticated analysts (and plaintiffs lawyers) who typically read prospectuses.²⁶¹ Requiring companies to assess the characteristics of diverse investors and conduct financial education for them cannot rely upon this justification.²⁶² No doubt, some companies will provide education to attract investors, with or without legal requirements.²⁶³ But others may decide that any educational efforts for consumers are not worth the costs, because they find enough capital from educated investors (including the financial intermediaries through which many ordinary people invest). Companies registering or listing their securities on an exchange may also justifiably ask why they are being compelled to provide investor education in disclosure documents, when financial and nonprofit firms are already supplying this educational service.

Yet the "plain English" initiative usefully directs companies to clarify language and organization throughout disclosure documents,

²⁶⁰ Compare Joel Seligman, *The Historical Need for a Mandatory Corporate Disclosure System*, 9 J. CORP. L. 1, 52-53 (1983) (arguing that compulsory disclosure encourages saving and benefits investors by reducing security price variance), with Edmund W. Kitch, *The Theory and Practice of Securities Disclosure*, 61 BROOK. L. REV. 763, 770-73 (1995) (arguing that competitive pressure and penalties for inaccurate disclosure reduce the amount of information produced under mandatory disclosure law).

²⁶¹ See, e.g., Frank H. Easterbrook & Daniel R. Fischel, *Mandatory Disclosure and the Protection of Investors*, 70 VA. L. REV. 669, 679, 685, 689-90 (1984) (discussing theoretical and actual benefits of mandatory disclosure). The courts have also so read disclosure requirements. See, e.g., *Wielgos v. Commonwealth Edison Co.*, 892 F.2d 509 (7th Cir. 1989). But see *MacMahan & Co. v. Warehouse Entertainment, Inc.*, 900 F.2d 576, 579 (2d Cir. 1990), *cert. denied*, 501 U.S. 1249 (1991) (holding that "the disclosure required by the securities laws is measured not by literal truth, but by the ability of the material to accurately inform rather than mislead prospective buyers") (citation omitted).

²⁶² Companies are likely to pass along the costs of the new disclosure to all investors, particularly to the investment professionals and financially sophisticated, who would be forced to subsidize this consumer educational effort. Additionally, because investment companies act as intermediaries for many investors, consumers may actually end up paying much of the costs of a "plain English" disclosure that they do not in fact use, but that is supposed to benefit them. In addition, every regulation can affect the competitive ability of firms. That is, if "plain English" imposes net costs on American firms and others raising funds publicly in the capital markets of the United States, it could harm these firms and markets.

²⁶³ See Galuszka, *supra* note 158, at 90 (discussing firms that encourage direct consumer investing in their stock).

and essentially requires them to create a valuable, simplified consumer-oriented part of a prospectus.²⁶⁴ Despite their mutual fund investments, consumers are investing directly in companies and are likely to increase this activity as technology facilitates this type of investment.²⁶⁵ They do not read lengthy disclosure documents, no matter how plainly written, and it makes no sense to encourage them to do so. Yet they benefit from an understandable summary of key company and securities information, and the development of a prospectus outline/summary designed for consumers is a valuable contribution of the initiative. In essence, the SEC requires a company to provide consumers with the equivalent of a “profile” disclosure document.²⁶⁶

The simplified consumer format, however, is only the first step, and the educational issue remains. The SEC should have used the “plain English” initiative to make consumers realize that they need to consult the investor education tools and services provided by financial service firms, so as to understand any particular investment in a broader financial context. In effect, this connection can now occur since many consumers invest through brokers, fund companies or other on-line services that offer educational materials and financial advice. The SEC should revise its “plain English” format to make consumers aware of the importance and availability of investor education. It could require that, in the consumer-oriented prospectus sections, companies provide consumers with some elementary warnings about the generic risks of the particular kind of investment and then encourage them to educate themselves about the potential place of this investment in their portfolio.²⁶⁷ A “plain English” prospectus would then have to point—or, in electronic prospectuses, provide a direct hypertext link—to specific educational providers, such as the

²⁶⁴ The creation of a simplified consumer section of a disclosure document is a central thrust of the initiative because plain English writing principles apply only to the cover pages, summary and risk factors sections of the prospectus, which introduce, and summarize the material in the entire document. See Final Release, *supra* note 243, at 6370; Proposing Release, *supra* note 235, at 3160-63.

²⁶⁵ See Lohse *supra* note 158, at B12; *AAIL.com*, *supra* note 155 (providing numerous services for consumers).

²⁶⁶ See *infra* Part IV(C); see also Final Release, *supra* note 248, at 6374 (requiring that an investment company apply plain English principles to its profile). In fact, the SEC should have gone farther in designing a consumer prospectus section by requiring companies to provide a summary section and a discussion of an investment’s risk factors; under the new rule, it must draft these sections using “plain English” principles only if it decides to supply them in a disclosure document. See *id.* at 6373 (“We decided against this [requirement of a summary] because a summary may not be helpful in all prospectuses.”). In practice, however, most companies do provide prospectus summaries.

²⁶⁷ In effect, the SEC requires such risk discussion when a company provides a risk disclosure summary. See Final Release, *supra* note 243, at 6373 (“You should place any risk factor in context so investors can understand the specific risk as it applies to your company and its operations.”). While the SEC discourages a discussion of risk in purely generic terms, such a general discussion could be useful to consumers.

self-regulatory organization where the company lists its securities, and to the SEC for referrals to other providers and for anti-fraud educational materials.²⁶⁸ While this mandatory connection would not resolve all uncertainties about "plain English" disclosure, it should at least make clear to companies that their primary obligation is to provide a straightforward consumer prospectus summary, and to consumers that they need investor education to invest safely and wisely.

C. Investment Company Disclosure Formats

Because of the popularity of mutual funds, and their use in retirement plans, consumers need to receive education about them so that they understand the advantages of mutual fund investing and the benefits of particular kinds of funds and fund investment strategies. Investments by Americans in mutual funds have grown exponentially, both in retirement and non-retirement accounts.²⁶⁹ This growth is not surprising, because mutual funds provide consumers with the professional money management and investment options that were previously available only to the wealthy. More importantly, by their nature, mutual funds raise basic finance issues critical to wealth enhancement (e.g., diversification, specialized investing, strategies ranging from passive indexing to active management and changing asset allocation over life cycles) that consumers need to understand.

Two recent and significant SEC changes to investment company disclosure²⁷⁰ implicate investor education because they are designed

²⁶⁸ For example, a prospectus summary dealing with stock might contain the following warning:

This investment makes you an owner of a "share" of the company's assets and subjects you to risks particular to the company, as discussed below, and to stock investing in general. You should decide whether the investment is suitable to your personal circumstances and fits with your other investments. For help in making this decision, you should consult investor educational materials and your financial advisor, if you have one.

To obtain information on investor education and education providers, please contact [specify the NYSE, the NASDAQ, or any other exchange where the company's securities are listed]. The Securities and Exchange Commission will also direct you to educational services, as well as help you protect yourself against investment fraud and abuse (please call [telephone number] or go to its web site, www.sec.gov).

²⁶⁹ See 1998 *Mutual Fund Fact Book*, *supra* note 41, at 1 (describing increase in total assets in mutual funds from \$1.07 trillion in 1990 to \$4.5 trillion in 1997); *id.* at 16 (noting that the number of mutual funds has more than doubled since 1990). Approximately 16% of the \$7.9 trillion of total retirement assets are invested in mutual funds. See *id.* at 44.

²⁷⁰ See Registration Form Used by Open-End Management Investment Companies, Securities Act Release No. 7398, 62 Fed. Reg. 10,898 (Mar. 10, 1997) [hereinafter Registration Proposal]; Registration Form Used by Open-End Management Investment Companies, Securities Act Release No. 7512, 63 Fed. Reg. 13,916 (Mar. 23, 1998) [hereinafter Final Registration Release]; New Disclosure Option for Open-End Management Investment Companies, Securities

to make the disclosure more useful and understandable to consumers, specifically by enabling them to grasp the basic features of a fund and by enhancing their ability to compare it to similar funds.²⁷¹ That is, by focusing consumers' attention on certain fund features and their comparability, the revised disclosure helps them understand that they can not view any investment in isolation, but must view it in comparison to similar investment products and as part of an optimal portfolio. The amended disclosure format thus has mutual funds provide consumers with some knowledge that comes from investing education—a general understanding about kinds of investments, advantages of combining of investments and the need for their portfolios to change over time and circumstances. At the very least, it requires the funds to put information into a format to which consumers could easily apply the education about saving and investing that the funds already provide. In a third proposed change to investment company names,²⁷² the SEC justifiably targets an anti-fraud educational issue: preventing an investment company from misleading consumers by its use of an inappropriate name.

The two amendments resulting in the new disclosure format originate from a valuable cooperation between mutual fund companies and the SEC.²⁷³ In designing the new fund disclosure format, the SEC staff took the advice of firms in an area where they are likely to offer the best solutions, since fund companies communicate daily with, and have an interest in satisfying, consumers. As in the "plain

Act Release No. 7513, 63 Fed. Reg. 13,968 (Mar. 23, 1998) [hereinafter Final Profile Release]; see also Proposed New Disclosure Option for Open-End Management Investment Companies, Securities Act Release No. 7399, 62 Fed. Reg. 10,943 (Mar. 10, 1997) [hereinafter Profile Proposal].

²⁷¹ See Final Registration Release, *supra* note 270, at 13,917 (observing that the two major disclosure initiatives are "intended to: improve fund disclosure by requiring prospectuses to focus on information central to investment decisions; provide new disclosure options for investors; and enhance the comparability of information about funds."); Final Proposal Release, *supra* note 270, at 13,969-70 (requiring "[s]tandardized [f]und [s]ummaries . . . [i]mproved [r]isk [d]isclosure . . . [g]raphic [d]isclosure of [v]ariability of [r]eturns . . ." and other fund information in plain English).

²⁷² Investment Company Names, Investment Company Act, Release No. 22,530, 62 Fed. Reg. 10,955 (Mar. 10, 1997) [hereinafter Names Proposal]. The SEC has not yet released a final rule on this proposal.

²⁷³ The SEC has tried to standardize and simplify mutual fund disclosure because it recognizes that fund investments are mainly designed for consumers. See, e.g., Investment Company Act Release No. 13,436, 48 Fed. Reg. 37,928 (Aug. 22, 1983) (adopting a two-tier disclosure format for mutual fund registration with a prospectus and a "Statement of Additional Information"); Investment Company Act Release No. 16,244, 53 Fed. Reg. 3, 192 (Feb. 4, 1988) (adopting uniform fee table in funds); Investment Company Act Release No. 16,245, 53 Fed. Reg. 3,868 (Feb. 10, 1988) (adopting a uniform formula for calculating fund performance); Investment Company Act Release No. 19,382, 58 Fed. Reg. 19,050 (Apr. 12, 1993) (adopting a uniform presentation of management's discussion of fund performance); Investment Company Act Release No. 21,216, 60 Fed. Reg. 38,454 (July 26, 1995) (proposing amendments to simplify money market fund disclosure). See generally Registration Proposal, *supra* note 275, at 10,899-901 (discussing these developments).

English” initiative, however, the SEC’s amendments would have been more valuable if it recognized the relation of the disclosure format to fund educational products and services. The SEC should improve its initiatives by taking the next logical steps of requiring fund companies to link the new disclosure format to their—and SEC anti-fraud—educational materials, and of alerting consumers about the existence and importance of these materials.²⁷⁴

The Registration Final Release, developed from industry experimentation with different disclosure formats,²⁷⁵ requires a fund to provide investors with a standardized, simplified summary of a fund.²⁷⁶ The educational implications of the format are significant since, under the Release, funds would provide information in a way that facilitates a consumer’s use of investor education. A fund prospectus would summarize the fund’s basic investment objectives and the general strategies of its fund advisor for achieving them (e.g., that the equity fund has adopted a “growth” approach and that it achieves this objective through purchases of securities of companies with specific characteristics).²⁷⁷ The risk disclosure requires a fund to identify in general terms the risks to which it is subject because of its portfolio, objectives and strategies.²⁷⁸ The disclosure thus encourages a

²⁷⁴ One problem with the new disclosure format is that, like much of investor education, it encourages investors to concentrate only on their portfolios and to ignore “larger” social issues relating to company activity. See Fanto, *supra* note 51. Again, it is appropriate that the SEC focus first on ensuring that investors understand the connection between an investment in a particular fund and their overall portfolios before it encourages them to consider such issues.

²⁷⁵ See Registration Proposal, *supra* note 270, at 10,899 n.16, 10,909 n.101 (discussing experimental approaches and pilot plans); see also Letter from Paul Schott Stevens, Senior Vice President, General Counsel, Investment Company Institute to Jonathan G. Katz, Secretary, Securities and Exchange Commission (June 9, 1997) <http://www.ici.org/nla_comment.html> (commenting on Registration Proposal).

²⁷⁶ The SEC relates the proposal to its “plain English” initiative because the SEC observes that mutual fund prospectuses have grown too complex and legalistic and fund shareholders do not find them useful in making investment decisions. See Registration Proposal, *supra* note 270, at 10,899 n.6; Final Registration Release, *supra* note 270, at 13,918.

²⁷⁷ See Registration Proposal, *supra* note 270, at 10,910 (“The information might describe, for example, whether an equity fund emphasizes value or growth, or blends the two approaches, or whether the fund invests in stocks based on a ‘top-down’ analysis of economic trends or a ‘bottom-up’ analysis that focuses on the financial condition and competitiveness of individual companies.”) (footnote omitted); *id.* at 10,902 (requiring a fund to disclose whether it intends to concentrate on particular kinds of securities and/or on an industry or group of industries); *id.* at 10,910 (discussing requirement that a fund disclose whether it expects to have a yearly turnover rate equal to or greater than 100% and the tax consequences of this turnover for investors); see also Final Registration Release, *supra* note 270, at 13,920 (discussing generally how investors will be able to determine the strategy of a fund).

²⁷⁸ See Registration Proposal, *supra* note 270, at 10,903; Final Registration Release, *supra* note 270, at 13,919-20. This risk presentation arose out of the SEC’s consideration of responses to an earlier concept release in which it asked the fund industry for its views on what is the appropriate disclosure of risk. See Investment Company Act Release No. 20,974, 60 Fed. Reg. 17,172 (Apr. 4, 1995) (requesting views and comments); see also *supra* note 270, at 10,900 (discussing response to this release). The SEC does not propose any quantitative risk disclosure, such as standard deviation, beta and duration, which could help investors numerically evaluate and compare fund risk. See Registration Proposal, *supra* note 270, at 10,911 &

consumer to think about the relationship between risk and return in a fund. Indeed, a fund may, but is not required to, identify the kind of investor for which it is suitable, depending upon an investor's risk tolerance and preferences.²⁷⁹ Such disclosure makes sense in the asset-allocation and life cycle decision-making that is a fundamental part of knowledgeable investment decisions.²⁸⁰ A requirement that a fund also provide a bar chart of risk/return information comparing the fund's returns over the last ten years to those of an appropriate market index,²⁸¹ pushes consumers to compare a fund's performance to that of other funds, particularly to a market index. This comparison in effect leads consumers to consider whether a particular actively managed fund does better than a passive indexing investing strategy.²⁸²

The SEC's related Final Profile Release particularly underscores the educational implications of the revised fund disclosure format, as well as the format's origin in market experimentation. The Release permits a fund to provide investors with a short, readable profile of a fund that facilitates comparison of funds, allows them to judge the fund's appropriateness for their investing strategy,²⁸³ and on the basis of which they can make an investment decision.²⁸⁴ The purpose of the profile is clearly to help the ordinary consumer who invests in funds for retirement and other savings, who "face[s] an increasingly diffi-

n.136 (explaining that the fund industry's response to its concept release on risk disclosure showed that firms disagree about appropriate quantitative risk measurement standards and about the ability of consumers to understand and to use effectively quantitative risk measurement, but allowing continued industry experimentation with risk disclosure).

²⁷⁹ See Final Registration Release, *supra* note 270, at 13,921. The original proposal required that the disclosure form include an identification of an appropriate investor for a fund. See Registration Proposal, *supra* note 270, at 10,903. In response to opposition by commentators who thought that the requirement would conflict with suitability rules imposed on brokers and investment professionals (i.e., that brokers determine whether an investment is suitable for a client), the SEC made such identification optional in the new registration form.

²⁸⁰ See Registration Proposal, *supra* note 270, at 10,903 (requiring a fund to identify risks peculiar to it, the most prominent being that funds offered by banks are not FDIC-insured); Final Registration Release, *supra* note 270, at 13,921-22 (same).

²⁸¹ See Final Registration Release, *supra* note 270, at 13,922-24.

²⁸² The bar chart comparison would not include returns adjusted for sales loads, but only a general warning that, if the loads were included, the funds' returns would be lowered. See Final Registration Release, *supra* note 270, at 13,923 n.62, 13,924-25 (requiring a table of sales loads and expenses associated with the fund that would allow fund shareholders to compute easily the differences between sales fees and fund expenses). There is an increasing SEC concern with fund fees and disclosure regarding them, and it is likely that the SEC may revisit the subject of fee disclosure. See *Levitt Remarks*, *supra* note 233.

²⁸³ See Profile Proposal, *supra* note 270, at 10,945 ("Requiring profiles to present information in a standardized format should help investors identify key information about a fund and make comparisons among different funds."); Final Profile Release, *supra* note 270, at 13,968 (adopting proposed rule).

²⁸⁴ The profile would alert investors that they could obtain from the company a full prospectus (which, in any event, would be sent to them upon confirmation of purchase). See Final Profile Release, *supra* note 270, at 13,969; see also Profile Proposal, *supra* note 270, at 10,944 ("The profile would allow investors to choose the amount and format of information they want before making an investment decision.").

cult task in choosing among different fund investments,"²⁸⁵ and who has limited financial sophistication. Since many of these investors cannot understand the lengthy, financially and legally complex fund prospectuses,²⁸⁶ they increasingly look to simple comparisons, evaluations and ratings of funds offered by market services,²⁸⁷ or to the more accessible materials supplementary to a prospectus, such as sales literature and advertisements, supplied by fund companies.²⁸⁸ Under SEC and ICI supervision, fund companies conducted an experiment with fund profiles and found them to be popular with consumers, which led to the proposal and final rule.²⁸⁹

The format and manner of distribution of the profile complements any consumer investor education. A fund can provide in the profile only nine items of information in a set order,²⁹⁰ with the first four items covering fund goals, strategies, risks and fees. The profile would thus have the same basic educational purposes of simplified disclosure, fund comparability, portfolio suitability and "ease of fit" with education about investing that characterize the Registration Final Release.²⁹¹ To enhance access to profiles, a fund company could distribute them to consumers widely through various media, including through mass mailing, newspapers and electronic delivery.²⁹² In fact, the SEC recognizes the suitability of the profile to the growing Inter-

²⁸⁵ Final Profile Release, *supra* note 270, at 13,968 ("In the Commission's view, the growth of the fund industry and the diversity of fund investors warrant a new approach to fund disclosure that will offer more choices in the format and amount of information available about fund investments.") (footnote omitted).

²⁸⁶ Cf. Robert Barker, *Just How Juicy Is That IPO?*, BUS. WK., Oct. 6, 1997, at 168, 168-69 (giving investors "tips" about skipping through lengthy prospectuses).

²⁸⁷ See *Morningstar.Net*, *supra* note 154 (referring to Morningstar's fund service).

²⁸⁸ See, e.g. Clifford E. Kirsch et al., *Mutual Fund and Variable Insurance Products Performance Advertising*, 50 BUS. LAW. 925, 933-35, 952-59 (1995) (summarizing the law, regulation and problems with simplified fund prospectuses and fund advertising); Paul S. Stevens & Craig S. Tyle, *Mutual Funds, Investment Advisers, and the National Securities Markets Improvement Act*, 52 BUS. LAW. 419, 425-27, 459-60, 468 (1997) (discussing development of simplified fund disclosure and advertising).

²⁸⁹ See Profile Proposal, *supra* note 270, at 10,944 (describing history of experimentation with profiles by large fund companies). See generally INVESTMENT COMPANY INSTITUTE, THE PROFILE PROSPECTUS: AN ASSESSMENT BY MUTUAL FUND SHAREHOLDERS (1996) (presenting to the SEC results of consumer attitudes regarding fund profiles).

²⁹⁰ See Final Profile Release, *supra* note 270, at 13,972. In the rule proposal, the SEC suggested that a fund present the items in a simplified, popular question-and-answer format. See Profile Proposal, *supra* note 270, at 10,945. To allow for industry experimentation in the profile, the SEC omitted this requirement from the Final Release. See Final Profile Release, *supra* note 270, at 13,972. The "plain English" principles would still apply to the profile. See *id.* at 13,969-70, 13,972.

²⁹¹ See Final Profile Release, *supra* note 270, at 13,975-76 (declining to require a fund to identify the "ideal" investor in it (although recommending that a fund make such an identification)). The other items would provide information on the fund's investment advisor and portfolio manager, purchase and sale of fund shares (two items), fund distributions and their taxation, and fund services—all items that the industry has found to be important to consumers. See *id.* at 13,978-79, 13,986.

²⁹² See Final Profile Release, *supra* note 270, at 13,981 n.115.

net use by fund companies and fund customers, since a company could electronically provide a profile and a hypertext link to the full prospectus and other fund information.²⁹³

While the Names Proposal, which requires that a fund invest at least 80% of its assets in a specific kind or kinds of securities if its name suggests a fund focus on them,²⁹⁴ provides an example of the SEC's traditional mission of ensuring accurate disclosure, it also has an anti-fraud educational purpose related to the SEC's role in protecting and educating consumers against illegal and/or abusive practices of financial professionals. The SEC explains that consumers increasingly use mutual funds to meet their retirement and other investment needs, and base their fund investments, as is proper, on asset-allocation theory—a primary component of investing education.²⁹⁵ Furthermore, in making asset-allocation decisions, they use well-defined kinds of funds, such as stock, bond and money market funds to meet their target portfolio composition. Yet, in the SEC's view, investors rely too much on fund names in arriving at these decisions.²⁹⁶ If a mutual fund implies through its name that it specializes in particular investments, but does not in fact do so, it undermines the

²⁹³ See *id.* at 13,981 n.120. On electronic delivery of disclosure documents, see generally HOWARD M. FRIEDMAN, *SECURITIES REGULATION IN CYBERSPACE* 2-1 to 3-40 (1997). Fund companies could also tailor profiles used in retirement plans to the plans' needs and participants' investment limitations. See Final Profile Release, *supra* note 270, at 13,981-82. A controversial issue in the profile project was the potential liability of a fund and fund distribution participants because of the potential use of the profile to sell fund shares. See *id.* at 13,970-72. Given my focus on the educational import of the profile, I do not examine this issue.

²⁹⁴ See Names Proposal, *supra* note 272, at 10,956. The SEC promulgated this rule proposal pursuant to the National Securities Markets Improvement Act of 1996, which amended Section 35(d) of the Investment Company Act to empower the SEC to address potentially misleading company names by its rule-making authority. See Pub. L. No. 104-290, § 208, 110 Stat. 3416, 3432 (1996). Section 35(d) now provides as follows:

(d) Deceptive or Misleading Names. It shall be unlawful for any registered investment company to adopt as a part of the name or title of such company, or of any securities of which it is the issuer, any word or words that the Commission finds are materially deceptive or misleading. The Commission is authorized, by rule, regulation, or order, to define such names or titles as are materially deceptive or misleading.

Prior to this amendment, the SEC prohibited, by order, names of specific investment companies pursuant to its power under a prior version of Section 34(d) to bar materially deceptive or misleading names. See 15 U.S.C. § 80a-34(d) (1988). The SEC's proposed new Rule 35d-1 requires a "floor" investment amount for fund companies advertising themselves as specializing in certain kinds of securities (e.g., stock, bond, Treasury, government, tax-exempt) or securities of issuers in a particular industry (e.g., utilities) or countries or geographic regions. See Names Proposal, *supra* note 272, at 10,957-58. The SEC proposes that the rule not apply to funds for which it has already provided guidance about appropriate portfolio composition, such as index, balanced, and small capitalization. It would also exempt bond funds from the rule since it is studying the proper characterization of these funds, a subject related to quantitative risk disclosure. See *id.* at 10,959-60.

²⁹⁵ See Names Proposal, *supra* note 272, at 10,956-957.

²⁹⁶ See *id.* at 10,956.

beneficial effects of consumers' asset allocation and thus of investor education generally. The SEC hopes consumers avoid this deception by reading disclosure documents (as simplified by the Registration and Profile Proposals, as well as by the "plain English" initiative), but it feels that consumers' excessive reliance on fund names justifies its addressing the problem through substantive regulation.²⁹⁷

As in the "plain English" initiative, the SEC should improve the new fund disclosure format by explicitly linking it to investor education provided by financial and nonprofit firms. Although the new format invites a consumer to apply a basic education about investing to the disclosed information, a fund company does not provide that education in a profile. Even the Names Proposal presumes that an investor understands the basic differences between a stock and bond fund. The SEC should thus take the additional regulatory step of requiring a mutual fund to tie the revised fund disclosure to investor education materials supplied by the fund—or by some other financial intermediary—as well as to SEC anti-fraud education and its references to education providers.²⁹⁸ In fact, linkage between information and education should occur throughout a profile: when, for example, a fund discusses its risks and identifies the appropriate kind of investor for the fund, it should point the investor specifically to educational materials on risk, asset allocation and life-cycle investing.²⁹⁹ While the SEC must work out the details of the linkage,³⁰⁰ additional mutual fund disclosure reform could thus be another significant opportunity for the SEC to recognize publicly the developments in investor edu-

²⁹⁷ This Proposal may implicitly conflict with the SEC's two fund disclosure format amendments. It is one thing to simplify and shorten disclosure to facilitate consumer reading; it is quite another thing to justify substantive regulation because of an assumption that, since investors read *only a few words* (i.e., the names of funds), the SEC must ensure the accuracy of these words. One could argue, in the SEC's favor, that investors may read a profile, or a prospectus, but still place too great reliance on a name because they justifiably regard it as an important sign that "trumps" sections of the prospectus contradicting it.

²⁹⁸ See *supra* note 268 (presenting possible prospectus language). A significant difference between company and fund disclosure is that many, but not all, fund companies, unlike non-financial companies, provide educational services and materials to which they could easily link a profile or prospectus. If, like a non-financial company, a fund company does not provide such services, it could link its disclosure documents to the services of the ICI or of the brokerage firms through which the fund is sold (as well as to the SEC Web site, where further educational references are available).

²⁹⁹ In its disclosure simplification, whether in company or fund prospectuses, the SEC worries about confusing a consumer by providing cross-references, etc. Yet the electronic delivery of disclosure documents and educational materials, with the availability of hypertext links, ensures that the use of glossaries and cross-references does not impede reading and comprehension, since a reader can easily access them.

³⁰⁰ For example, the SEC would have to address any concerns of fund companies that they would increase their liability if they provided links to their educational materials. See, e.g., 15 U.S.C. § 77e (1994) (prospectus liability under the Securities Act of 1933); cf. 15 U.S.C. § 77b(a)(10)(b) (exempting supplementary sales literature from the prospectus definition); 17 C.F.R. § 230.135a (1997) (restricting advertising for mutual funds).

cation by financial firms and nonprofit organizations and to encourage consumers to use these educational services.

D. A Concept Release on Investor Education

In light of the SEC's educational and education-related efforts, it may well be time for the SEC to issue a concept release on investor education. The SEC typically circulates a concept release as a result of a significant development in the securities markets and explains therein its regulatory response, or offers potential responses, to the development and asks interested persons for their views on appropriate SEC action.³⁰¹ A release thus serves two important functions: (1) It focuses SEC attention on the development, and its regulatory authority to address it, and (2) it stimulates reflection by all kinds of parties—financial firms, their lawyers, economists, legal scholars, consumer groups and private investors. With the information gathered from the concept release, the SEC can intelligently decide whether to undertake further regulatory initiatives to address the market development.

The SEC now needs to adopt a formal position on investor educational developments in the securities markets (or at least to discuss them in detail), and to take a critical look at its own valuable, but not entirely coordinated, educational activities. If the SEC engages in this public reflection, it should recognize the value of the educational efforts of financial and nonprofit firms, and redirect its own activities in cooperation with them to provide consumers with the best opportunity to receive saving, investing and anti-fraud education. A release will also lead firms, consumer organizations and other regulators to bring to the SEC's attention additional educational materials, services and research on investor education, as well as possibilities of joint, or separate, government and market educational activity. The concept release will also require the SEC to justify its statutory authority in this field, and thus highlight any need for additional legislation. Finally and most importantly, the release would greatly contribute to the ongoing national campaign to encourage saving and investing, and to make consumers understand the importance of investor education for their financial future.³⁰²

³⁰¹ See, e.g., Investment Company Act Release No. 20,974, *supra* note 278.

³⁰² The release would thus fit well within the national campaign and activities generated by the SAVER Act and by the SEC's own "Facts on Saving and Investing Campaign."

V. CONCLUSION

Numerous pressures and events have made it important that ordinary Americans save more and invest their savings well. The major government safety net, the Social Security program, can not entirely fund the income needs of the elderly, and the aging of the "Baby Boom" generation seriously threatens the solvency of the program. For a number of reasons, companies are increasingly likely to offer their employees retirement plans where, at best, they and the employees contribute funds to retirement accounts, and where employees themselves have the responsibility to direct the investment of the funds. An individual's financial well-being in retirement thus depends much upon her own saving and investing decision-making. In an age where government programs are generally not expanding, individual Americans also need to save and invest outside retirement programs for other goals, such as their children's education and their own aging parents' welfare.

A growth in investment opportunities, which allows ordinary investors to meet their saving and investing goals, has accompanied these pressures for enhanced investment performance. No longer is investing restricted to the wealthy, who alone can benefit from professional money management. Rather, funds offer consumers an extraordinary choice of investment options and professional management, whether inside or outside retirement plans. Technology facilitates an investor's access to these collective vehicles and the services they provide, as well as to direct investing in companies. Yet the range of investment choices and financial services poses a problem for consumers, who must navigate among a bewildering number of selections, now that saving and investing have become everyday, but necessary, activities.

Investor education should assist consumers in meeting their new saving and investing responsibilities. As a cultural matter, this education is an inevitable part of the solution to the financial problems facing ordinary Americans, and to the growing wealth disparity between Americans, which the new responsibility of ordinary people for investment decision-making may exacerbate, although it is neither the *only* solution, nor the one most likely to help the many lower-income individuals without any real means of savings. The Article thus begins the necessary work of identifying the kinds of investor education and the appropriate party or parties to conduct them. Indeed, since the importance of investor education can only increase, as consumer mutual fund and direct investing grows inside and outside retirement plans and perhaps even within Social Security itself, and as saving

and investing become even more a part of everyday life, additional reflection on this subject is needed, particularly on the proper allocation of educational responsibilities between the government and private parties. It is best that this reflection not occur in a haphazard fashion or as a result of a crisis, such as a major stock market correction, but, if at all possible, through a careful observation, analysis and evaluation of market experimentation and government efforts.³⁰³

³⁰³ Securities markets worldwide have recently become more volatile. This market development makes reflection on investor education even more critical because, if investors are not "trained" to understand such volatility, they can panic with potentially adverse consequences to the markets.