SEC REGULATION S-P

Summary:

SEC Regulation S-P governs the treatment of nonpublic personal information (NPI) about consumers by brokers, dealers and investment advisers. The Regulation requires firms to notify clients concerning the collection, use and sharing of client NPI. The Regulation limits the disclosure of client NPI to anyone not affiliated with the firm unless clients have been notified of the way their NPI will be shared and clients have not directed the firm to share the information. Clients are thus entitled to Opt-Out of a firm’s plan to share their NPI with others not affiliated with the firm.

There are exceptions to the requirement entitling clients to opt-out. The Regulation requires client NPI to be safeguarded and disposed of properly. This outline describes the following basic elements of the Regulation:

- Initial Privacy Notices
- Annual Privacy Notices
- Information in Privacy Notices
- Opportunity for Customers to Opt-Out
- Revised Privacy Notices
- Delivery of Privacy and Opt-out Notices
- Current Safeguard Requirements

PART I. CURRENT DISCLOSURE REQUIREMENTS

1. Initial Privacy Notices to Consumers

   a. SEC-registered brokers/dealers, investment advisers, and investment companies (“Firm”) must provide a clear and conspicuous notice that accurately reflects the Firm’s privacy policies and practices to:

      i. **Customers**, when the relationship with the customer is established. A relationship with a customer is established when the Firm and the customer enter into a continuing relationship. Examples of the commencement or a continuing relationship include:

         a. a customer effects a securities transaction through the Firm or opens a brokerage account with the Firm,

         b. opening an account with an introducing broker/dealer that clears transactions with or for its customers on a fully-disclosed basis, and

         c. entering into an advisory contract with the customer.

      ii. **Consumers**, before passing any NPI to a nonaffiliated third party. (A consumer is essentially a single transaction user of a firm’s services. If there is
no continuing relationship with a firm, the consumer does not become a customer.)

b. A Firm does **not** have to provide an initial notice if:

i. the Firm does not disclose any NPI about the consumer to nonaffiliated third parties, except under an authorized exception,

ii. the Firm does not have a customer relationship with the consumer, or

iii. the Firm does not have a customer relationship with a customer if the Firm buys a loan made to the consumer but does not have servicing rights to that loan.

c. For existing customers who purchase a new product or service from the Firm for personal, family or household use, the Firm satisfies the notice requirements if:

i. the Firm provides a revised privacy notice to the customer covering the new product or service, or

ii. the initial, revised or annual privacy notices most recently provided to the customer are accurate with respect to the new product.

d. The Firm may postpone delivery of the initial notice to the customer for a reasonable time if:

i. establishing the customer relationship is not at the customer’s choice. For example where the customer’s account is transferred to the firm by a Securities Investor Protection Corporation (“SIPC”) trustee.

ii. providing notice at the time the relationship is established would substantially delay the customer’s transaction and the customer agrees to receive the notice later. An example would be a telephone transaction between the Firm and the customer involving the prompt delivery of the financial service or product.

iii. a nonaffiliated broker/dealer establishes a customer relationship between the Firm and the customer without the Firm’s prior knowledge.

e. The initial notice to the customer must be delivered so that each customer can reasonably be expected to receive actual notice in writing or, if the customer agrees, electronically.
2. **Annual Privacy Notices**

   a. The Firm must provide a clear and conspicuous notice about its privacy policies to customers at least once every twelve consecutive months during which the relationship exists.

   b. The Firm does not need to provide annual notices to a former customer. Examples of former customers include customers who have closed their brokerage accounts, terminated their advisory contracts or the Firm is an investment company and the individual is no longer the record owner of the securities issued by the Firm.

   c. The Annual Notice to the customer must be delivered so that each customer can reasonably be expected to receive actual notice in writing or, if the customer agrees, electronically.

3. **Information Included in Privacy Notices**

   A Firm must include the following information in its privacy notices

   a. categories of NPI collected. *Example:* information on the customer’s transactions with the Firm or its affiliates.

   b. categories of NPI disclosed. The Firm should provide examples to illustrate the types of categories of information to be disclosed.

   c. types of affiliated and nonaffiliated third parties with whom the NPI will be shared. The Firm should provide examples of affiliates and nonaffiliated third parties that are financial services providers, non-financial companies and others.

   d. categories of NPI about former customers and the categories of affiliated and nonaffiliated third party to whom the disclosures are made, except as allowed by the rule.

   e. for disclosures made to nonaffiliated third parties who are service providers or joint marketers, a statement describing the categories of information disclosed and the categories of third parties involved. The Firm should state whether (1) the service provider performs marketing services on the Firm’s behalf (and another financial institution, if applicable), or (2) the third party is a financial institution with which the Firm has a joint marketing agreement.

   f. an explanation of the consumer’s right to opt-out, including how the customer may exercise that right.

   g. disclosures about the consumer’s ability to opt-out of disclosures of information among affiliates.
h. the Firm’s policies and practices with respect to protecting the confidentiality and security of NPI. The Firm should describe in general terms who has access to the information and whether it has security practices in place to ensure the confidentiality of the information.

i. any disclosures made with regard to nonaffiliated third parties subject to exception to this rule.

4. Form of Opt-out Notice to Consumers and Opt-out Methods

a. If the Firm wishes to disclose NPI about its consumer, it must provide a clear and conspicuous notice to the consumer that accurately explains the consumer’s right to opt out of the information sharing.

b. The opt-out notice must also include:

   i. a statement that the Firm will disclose or reserves the right to disclose NPI,

   ii. a statement about the consumer’s right to opt-out,

   iii. a reasonable means to opt-out,

   iv. identify the categories of information to be disclosed and the categories of entities the information will be shared with, and

   v. the financial services or products subject to the consumer’s opt-out direction.

c. Reasonable opt-out methods include:

   i. designating checkboxes in a prominent place on forms with the opt-out notice,

   ii. including a reply form with the opt-out notice,

   iii. providing an electronic means to opt-out,

   iv. providing a toll-free number.

d. Unreasonable opt-out methods include:

   i. the customer having to write a letter to exercise opt-out.

   ii. the only means to opt out as described in a subsequent notice to the initial notice is to use a checkbox supplied in the initial notice.

e. The Firm may require a specific means for opting –out.
f. The opt-out notice may be included in the same form as the initial notice.

g. Where the opt-out notice is provided after the initial notice, a copy of the initial notice must accompany the opt-out notice.

h. Where two or more consumers jointly obtain one product, the Firm may provide one opt-out notice. However, individual opt-out notices may be required if the Firm allows each individual to opt-out.

5. Revised Privacy Notices

A revised privacy notice meeting the requirements of the initial notice must be issued when the Firm wishes to:

a. disclose a new category of NPI to an unaffiliated third party,

b. disclose NPI to a new category of unaffiliated third party, or

c. disclose NPI about a former customer to a nonaffiliated third party if that former customer did not have the opportunity to opt-out.

6. Delivery of Privacy and Opt-out Notices

a. The Firm must provide any privacy and opt-out notices so that each consumer can reasonably be expected to receive actual notice in writing or if they agree, electronically.

b. Examples of reasonable means of delivering the privacy and opt-out notices include:

   i. hand delivery of printed notice to the consumer,

   ii. mail delivery of a printed notice to the consumer’s last known address, and

   iii. where the transaction is electronic, post the notice on the site and require the consumer to acknowledge the notice before completing the transaction.

c. Examples of unreasonable means of delivery include:

   i. posting a sign in the branch office or publishing general advertisements of the privacy policy, and

   ii. sending the notice via e-mail when the consumer does not obtain the financial product or service from the Firm electronically.

d. Delivery of annual notices is sufficient where:
i. the customer uses the Firm’s website to access financial products and services, agrees to receive notices through the website, and the notice is posted in a conspicuous place on the website, or

ii. the customer has asked the Firm not to send any information regarding the customer relationship and the current privacy notice remains available to the customer upon request.

e. Oral delivery of the notice by itself is never sufficient to meet the requirements of this rule.

f. For customers only, the Firm must provide required notices in manner so that the customer can retain them, obtain them later in writing or if the customer agrees, electronically.

g. Joint notices (with other financial institutions) may be used, provided the notice is accurate with respect to the Firm and the other financial institutions.

PART II. CURRENT SAFEGUARDING REQUIREMENTS

1. Procedures for Safeguarding Customer Records

   a. Every Firm must adopt written policies and procedures that address the administrative, technical, and physical safeguards for the protection of customer records and information. The objectives of the policies and procedures must:

      i. insure security and confidentiality of customer records and information,

      ii. protect against any anticipated threats or hazards to the security or integrity of customer records and information, and

      iii. protect against unauthorized access to or use of customer records and information that could result in substantial harm or inconvenience to the customer.

2. Disposal of Consumer Report Information and Records

   a. Every Firm that maintains or possesses “Consumer Report Information” purpose must properly dispose of the information by taking reasonable steps to protect against unauthorized access or use of the information in connection with its disposal.

   b. Consumer Report Information means any record of about an individual in whatever form that is a consumer report, including a compilation of such records. It does not include information that does not identify an individual e.g., aggregate information or blind data.
ADDitional Materials

Financial Services Institute: Summary of Independent Dealer-Broker Policies

The Financial Services Institute (FSI) conducted a survey of the privacy disclosure policies of its members. FSI provides examples from the results of the survey\(^1\). and is located at the following website:

The survey lists examples of independent dealer-broker privacy policies under the following headings:

A. Privacy Policy Disclosure of Information Sharing with Affiliated Entities.

B. Privacy Policy Disclosures of Information Sharing Exceptions.

C. Privacy Policy Disclosures of Information Sharing with Non-Affiliated Persons.

D. Privacy Policy Disclosures Related to State Law.

A. Privacy Policy Disclosure of Information Sharing with Affiliated Entities

The survey lists three types of privacy policies:

i. Firms (the majority of those surveyed) that specifically list in their policy affiliated companies with whom they share information.

ii. Firms (a minority of those surveyed) that use general descriptions of the affiliated entities with which they may share information.

iii. Firms (few) that combine the two approaches above.

B. Privacy Policy Disclosures of Information Sharing Exceptions

The survey includes disclosures which vary in detail. The significant variance found in the level of detail concerning disclosures to non-affiliates corresponds to the degree to which the firm outsources business functions.

C. Privacy Policy Disclosures of Information Sharing with Non-Affiliated Persons

\(^{1}\) See:

This section addresses how firms inform clients of the opt-in or opt-out. The examples provided are from firms that do not permit the disclosure of non-public client information unless it falls within one of the Reg. S-P exceptions. There are several advantages of having a restrictive policy. These advantages include:

i. avoiding the administrative burden and cost of tracking client opt-ins or opt-outs,

ii. avoiding the administrative burden and cost of tracking compliance with laws of states that require an opt-in,

iii. helps in dealing with the departure of a financial adviser who takes client information with them, and

iv. helps in dealing with squaring the terms of the firm’s policy with both client and investment adviser expectations when the adviser joins another firm.

Some firms rather than provide an opt-out disclosure, notify their clients of their intent to share the information with a non-affiliated entity and give the clients 30 days to opt-out. If no response has been received from the client in 30 days, the firm shares the information.

i. Advantages: Flexibility in choosing when to share the information

ii. Disadvantages: Greatly multiplies the administrative task of tracking client consents.

Most of the firms surveyed describe sharing of information with a departing adviser and his/her new firm. However, the information shared is typically limited. Firms with a liberal privacy policy (i.e., sharing information with the departing representative and the new firm) have the following advantages:

i. avoids the cost and potential liability of trying to enforce a restrictive policy when a financial adviser leaves the firm,

ii. offers a recruiting advantage over firms with more restrictive policies,

iii. helps deal with the challenge of tracking clients who opt-out of sharing their NPI, and

iv. helps with the challenge of tracking compliance with laws of states that require clients to opt-in to the sharing of their information.

Most of these firms allow opt-out through an 800 number.

D. Privacy Policy Disclosures Related to State Law

A number of states require customers to opt-in to the sharing of personal information. Firms with liberal privacy policies must track customers who have opted-in. Neither Reg. S-P nor state law require reference to specific state law requirements. Most of the firms that participated do
not refer to the requirements. The article provides examples of firms that mention state requirements.

The article also has a couple of examples of companies that use the disclosures to inform a client that they can change their mind about opting-in or opting-out.