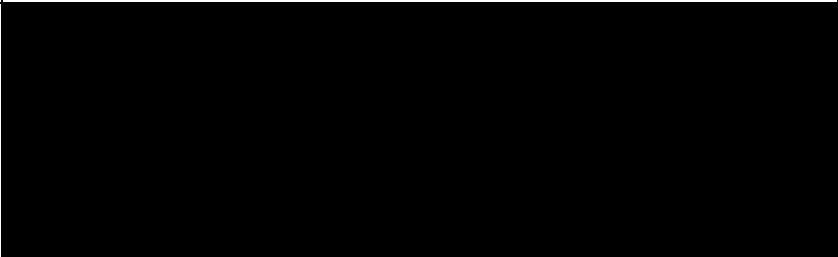


# THE COMMITTEE FOR THE FIDUCIARY STANDARD

## Analysis of Senator Tim Johnson’s Proposed Study of Broker and Adviser Obligations The Committee for the Fiduciary Standard . February 2010

*Note: Text in the left-hand side of the following table has been copied from Senator Johnson’s proposed draft amendment to the Senate’s draft financial reform bill.*

<p>Purpose: To provide for a study by the Securities and Exchange Commission to determine appropriate obligations of brokers, dealers, investment advisers, and their associated persons relating to the provision of personalized investment advice about securities to retail customers,...</p>	<p>SEC Chairman Mary L. Schapiro testified to the Financial Crisis Inquiry Commission on January 14 regarding a fiduciary duty for advisors: “When investors receive similar services from similar financial service providers, it is critical that the service providers be subject to a uniform fiduciary standard of conduct that is at least as strong as exists under the Investment Advisers Act [of 1940], and equivalent regulatory requirements, regardless of the label attached to the service providers.”</p> <p>A new study is not necessary. These questions were addressed in a 2008 study performed for the SEC by the Rand Institute for Civil Justice, “Investor Perspectives on Investment Advisers and Broker-Dealers.”</p> <p><a href="http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf">http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf</a></p>
<p>Purpose: ... to provide for a report by the Commission to Congress in 18 months, and to require a rulemaking by the Commission to address regulatory gaps and overlap in regulation identified by the study in the protection of retail customers.</p>	<p>Having considered these issues for many years, SEC staff is familiar with them. The issue is NOT a lack of information but rather that the SEC is restricted by the current statutory structure and language from addressing all of the known regulatory gaps and overlap through rulemaking. Passage of a bill authorizing SEC rulemaking would resolve this issue. To the extent the SEC can address gaps, it is already seeking recommendations from the industry. See Memo to Investor Advisory Committee,</p> <p><a href="http://www.sec.gov/spotlight/inadvcomm/iacmemofiduciaryduty.pdf">http://www.sec.gov/spotlight/inadvcomm/iacmemofiduciaryduty.pdf</a>.</p>
<p><b>SEC. 913. STUDY AND RULEMAKING REGARDING OBLIGATIONS OF BROKERS, DEALERS, AND INVESTMENT ADVISERS.</b>  <i>[section (a) omitted]</i>                  (b) IN GENERAL.—The Commission shall conduct a study to evaluate—</p>	

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<p>(1) the effectiveness of existing legal or regulatory standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice and recommendations about securities to retail customers imposed by the Commission and FINRA, and other Federal and State legal or regulatory standards; and</p> <p>(2) whether there are legal or regulatory gaps or overlap in legal or regulatory standards in the protection of retail customers relating to the standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice about securities to retail customers that should be addressed by rule or statute.</p>	<p>SEC policy staff in the Division of Investment Management and Division of Trading &amp; Markets are aware of the effectiveness of investment adviser and broker-dealer regulation, as well as the gaps and overlap in standards for investment advisers and broker-dealers. In addition, as appropriate, the SEC seeks out and reviews independent analysis. See Speech by SEC Commissioner Elisse Walter: Regulating Broker-Dealers and Investment Advisers: Demarcation or Harmonization?  <a href="http://www.sec.gov/news/speech/2009/spch050509ebw.htm">http://www.sec.gov/news/speech/2009/spch050509ebw.htm</a>.</p>
<p>(c) CONSIDERATIONS.—In conducting the study required under subsection (b), the Commission shall consider—</p>	<p style="background-color: black; color: black;">[REDACTED]</p>
<p>(1) the regulatory, examination, and enforcement resources devoted by the Commission and FINRA to enforce the standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers when providing personalized investment advice and recommendations about securities to retail customers, including—</p>	<p>SEC examination and enforcement information and statistics are available in the SEC’s 2009 Performance and Accountability Report, <a href="http://www.sec.gov/about/secpar/secpar2009.pdf#performancesummary">http://www.sec.gov/about/secpar/secpar2009.pdf#performancesummary</a>; the SEC Congressional Justification FY 2011, <a href="http://www.sec.gov/about/secfy11congbudjust.pdf">http://www.sec.gov/about/secfy11congbudjust.pdf</a>; and Select SEC and Market Data, Fiscal 2009, <a href="http://www.sec.gov/about/secstats2009.pdf">http://www.sec.gov/about/secstats2009.pdf</a>.</p> <p>FINRA statistics are available on the FINRA website at <a href="http://www.finra.org/Newsroom/Statistics/">http://www.finra.org/Newsroom/Statistics/</a>.</p>
<p>(A) the frequency of examinations of brokers, dealers, and investment advisers; and</p>	<p>Information on the SEC’s exam program, including frequency of exams is available on the SEC website at: <a href="http://www.sec.gov/about/offices/ocie/ocieoverview.pdf">http://www.sec.gov/about/offices/ocie/ocieoverview.pdf</a>.</p> <p>The SEC’s examination program was also recently studied by its Office of Investigator General: <a href="http://www.sec-oig.gov/Reports/AuditsInspections/2009/470.pdf">http://www.sec-oig.gov/Reports/AuditsInspections/2009/470.pdf</a>.</p>

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<p>(B) the length of time of the examinations;</p>	<p>Statistics on the length of exams are known by the SEC and are available in the SEC’s 2009 Performance and Accountability Report,  <a href="http://www.sec.gov/about/secpar/secpar2009.pdf#performancesummary">http://www.sec.gov/about/secpar/secpar2009.pdf#performancesummary</a>.</p>
<p>(2) the substantive differences, compared and contrasted in detail, in the regulation of brokers, dealers, and investment advisers, including the differences in the amount of resources devoted to the regulation and examination of brokers, dealers, and investment advisers, by the Commission and FINRA;</p>	<p>Having considered these issues for many years, SEC staff are familiar with the substantive differences and the resources devoted to regulation and examination by regulatory authorities.</p> <p>Statistics are also available in the SEC’s 2009 Performance and Accountability Report,  <a href="http://www.sec.gov/about/secpar/secpar2009.pdf#performancesummary">http://www.sec.gov/about/secpar/secpar2009.pdf#performancesummary</a></p>
<p>(3) the specific instances, where in the determination of the Commission—</p>	<p style="background-color: black; color: black;">[REDACTED]</p>
<p>(A) the regulation and oversight of brokers and dealers provide greater protection to retail customers than the regulation and oversight of investment advisers; and</p>	<p>This is known by the Division of Trading &amp; Markets staff at the SEC.</p> <p>Information on broker-dealer regulatory requirements is also available on the SEC website at:  <a href="http://www.sec.gov/divisions/marketreg/bdguide.htm">http://www.sec.gov/divisions/marketreg/bdguide.htm</a>.</p>
<p>(B) the regulation and oversight of investment advisers provides greater protection to retail customers than the regulation and oversight of brokers and dealers;</p>	<p>This is known by the Division of Investment Management staff at the SEC.</p> <p>Information on investment adviser regulatory requirements is also available on the SEC website at:  <a href="http://www.sec.gov/divisions/investment/advoverview.htm">http://www.sec.gov/divisions/investment/advoverview.htm</a>  and  <a href="http://www.sec.gov/about/offices/oia/oia_investman/rplaze-042006.pdf">http://www.sec.gov/about/offices/oia/oia_investman/rplaze-042006.pdf</a>.</p>
<p>(4) the role and effectiveness of State securities regulators and other regulators in protecting retail customers;</p>	<p>See Massachusetts Secretary of State William Galvin testimony and recommendations:  <a href="http://www.house.gov/apps/list/hearing/financialsvcs_dem/galvin.pdf">http://www.house.gov/apps/list/hearing/financialsvcs_dem/galvin.pdf</a>.</p> <p>The SEC also regularly communicates with and coordinates its resources with state securities regulators and other regulators as required under Section 19(d) of the Securities Act of 1933.</p>
<p>(5) the potential impact of imposing upon brokers, dealers, and persons associated with brokers or dealers—</p>	<p style="background-color: black; color: black;">[REDACTED]</p>

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<p>(A) the standard of care applied under the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) for providing personalized investment advice about securities to retail customers of investment advisers; and</p> <p>(B) other requirements of the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.), including the potential impact on access of retail customers to the range of products and services offered by brokers and dealers;</p>	<p>Imposing the Investment Advisers Act of 1940 on broker-dealer reps who are providing investment advice to retail investors would benefit investors by ensuring consistent application of the fiduciary standard, increasing the level of disclosures, requiring proper management of conflicts of interest, and ensuring investors' interests are placed above those of the professional.</p>
<p>(6) the potential impact of imposing on investment advisers the standard of care applied by the Commission and FINRA under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) for providing recommendations about securities to retail customers of brokers and dealers and other Commission and FINRA requirements applicable to brokers and dealers;</p>	<p>The overall impact of lowering the legal requirements of the standard of conduct on investment advisers would harm investors because they would not receive the same level of disclosures and would not be protected from all conflicts of interest that their financial professional encounters. It should also be noted that investment advisers are already subject to the same suitability requirement as brokers, plus the higher Investment Advisers Act requirement of fiduciary duty to their clients. See <a href="http://www.sec.gov/about/offices/oia/oia_investman/rplaze-042006.pdf">http://www.sec.gov/about/offices/oia/oia_investman/rplaze-042006.pdf</a>.</p>
<p>(7) the potential impact of eliminating the broker and dealer exclusion from the definition of "investment adviser" under section 202(a)(11)(C) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(11)(C)), in terms of—</p>	<p style="background-color: black; color: black;">[REDACTED]</p>
<p>(A) the number of additional entities and individuals that would be required to register under, or become subject to, the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.), and the additional requirements to which brokers, dealers, and persons associated with brokers and dealers would become subject, including—</p>	<p>The statistics on additional entities may already exist internally at the SEC.</p> <p>The additional requirements for brokers under the Advisers Act would already be known by the Division of Investment Management and the Division of Trading &amp; Markets.</p>
<p>(i) any potential additional associated person licensing, registration, and examination requirements; and</p>	<p>This would already be known by SEC policy and exam staff in the Division of Investment Management, Division of Trading &amp; Markets, and Office of Compliance Inspections and Examinations.</p>
<p>(ii) the additional costs to the additional entities and individuals;</p>	<p>The cost of registration and compliance may already be known by the SEC.</p>

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(B) the impact on Commission resources to—	
<p>(i) conduct examinations of registered investment advisers and the representatives of registered investment advisers, including the impact on the examination cycle; and</p> <p>(ii) enforce the standard of care and other applicable requirements imposed under the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.);</p>	<p>The SEC is considering this as there are several potential legislative changes that may affect SEC resources. For example, if the threshold for investment adviser registration is raised to \$100 million assets under management, then approximately 4,000 investment advisers will no longer be subject to SEC oversight. Therefore, this decrease would offset any increase in the number of professionals who must register if the broker exemption is removed from the Advisers Act</p>
<p>(C) the specific benefits or harm to retail customers that could result from such a change, including any potential impact on access to personalized investment advice and recommendations about securities to retail customers or the availability of such advice and recommendations; and</p>	<p>The overall impact of raising the legal requirements of the standard of conduct would benefit investors by ensuring their interests are placed first and that any conflicts of interest are properly disclosed and managed in favor of the investor by the investment professional.</p>
<p>(D) the types of exclusions or exceptions that would be necessary or appropriate to address any potential adverse impacts on retail customers that are not warranted by any qualitative changes in retail customer protections;</p>	<p>The SEC is aware of the types of exclusions/exceptions that would be needed. For example, the SEC issued an interim final rule that allows investment advisers registered as broker-dealers to engage in principal trading with modified disclosure requirements so they can effectively comply with fiduciary requirements. See <a href="http://www.sec.gov/rules/final/2009/ia-2965fr.pdf">http://www.sec.gov/rules/final/2009/ia-2965fr.pdf</a>.</p>
<p>(8) whether retail customers understand the differences in terms of regulatory oversight and examinations between brokers, dealers, and investment advisers;</p>	<p>The reality of consumer confusion has already been established. All the more reason to establish consistent and uniform fiduciary standards for anyone providing investment advice to retail investors. See SEC Report: “Investor Perspectives on Investment Advisers and Broker-Dealers” <a href="http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf">http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf</a>.</p> <p>SEC’s Office of Investor Education and Advocacy may also have data on investor perceptions.</p>

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<p>(9) the varying level of services provided by brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers to retail customers and the varying scope and terms of retail customer relationships of brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers with such retail customers;</p>	<p>The SEC has been regulating broker-dealers and advisers for decades and has extensive knowledge of the types of services they provide.</p>
<p>(10) any specific benefits or harm to retail customers that could result from any potential changes in the regulatory requirements or legal standards affecting brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers relating to their obligations to retail customers, including any potential impact on—</p>	<p>Investors will specifically benefit from a fiduciary standard and the related requirement for an investment adviser to disclose conflicts of interest and to manage those conflicts in favor of the investor. At present, there is more harm to investors because of the inconsistent application of the fiduciary standard.</p>
<p>(A) access to personalized investment advice, and recommendations about securities to retail customers; or (B) the availability of such advice and recommendations;</p>	<p>Because registered investment advisors already provide advice, investors will have similar access moving forward. To the extent that investor access or the availability of advice and recommendations is hampered, the SEC would be able to address access and availability by providing guidance on regulatory requirements and where necessary provide exemptive or other relief.</p>
<p>(11) the additional costs and expenses resulting from potential changes in the regulatory requirements or legal standards affecting brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers relating to their obligations to retail customers; and</p> <p><i>[subsection (c)(12) and Section d omitted]</i></p>	<p>To date there have been no demonstrated costs or expenses related to changing the standard of care. The costs of registration and compliance for broker-dealers and investment advisers are known and should not substantially increase as a result of the fiduciary standard being extended to all of those who provide advice.</p>