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SEC Investor Advisory Committee to Vote Friday on Fiduciary Plan.

While SIFMA 'strongly supports' some recommendations, others are 'incongruous' with Dodd-Frank's intent, says SIFMA's Carroll

The SEC's Investor Advisory Committee plans to vote Friday on one of its subcommittee's recommendations on how the SEC should craft its fiduciary rule for brokers.

The draft proposal by the Investor as Purchaser Subcommittee, which is headed by Barbara Roper, director of investor protection for the Consumer Federation of America, was scheduled to come up for a vote at the Investor Advisory Committee's Oct. 10 meeting, but that was postponed because of the government shutdown.

Roper told ThinkAdvisor that the subcommittee's hope is that "by weighing in early in the [fiduciary rulemaking] process, we can help to shape the form that commission rulemaking takes."

The subcommittee says that a fiduciary duty for investment advice should include, "first and foremost, an enforceable, principles-based obligation to act in the best interest of the customer."

In approaching this issue, the subcommittee says that the SEC's goal "should be to eliminate the regulatory gap that allows broker-dealers to offer investment advice without being subject to the same fiduciary duty as other investment advisors but not to eliminate the ability of broker-dealers to offer transaction-specific advice compensated through transaction-based payments."

The subcommittee adds that "Though it may require both regulatory flexibility to permit the existence of conflicts of interest and some regulatory changes to reduce the most severe conflicts of interest in the broker-dealer business model, the Committee believes that advisory services offered as part of a transaction-based securities business can and should be conducted in a way that is consistent with a fiduciary standard of conduct."

While the SEC is not bound by any recommendations of the Investor Advisory Committee, which was created under Section 911 of the Dodd-Frank Act, Section 911 does require the SEC to "review the findings and recommendations of the committee" and "each time the committee submits a finding or recommendation to the commission, promptly issue a public statement assessing the finding or recommendation of the committee; and disclosing the action, if any, the commission intends to take with respect to the finding or recommendation."

While fiduciary advocates have voiced their support of the recommendations in comment letters to the subcommittee, some other groups have not. For instance, while the Securities Industry and Financial Markets Association says that "many if not most" of the subcommittee's recommendations "are in accord" with SIFMA's views on how to implement Section 913 of Dodd-Frank, some recommendations are "incongruous with the intent and requirements" of Section 913.

Kevin Carroll, SIFMA's managing director, told the subcommittee in his comment letter that the “incongruities” exist in preserving the broker-dealer business model and in the “intent to maintain forward progress under Section 913.” These incongruities, he said, “may be attributable to the fact that the subcommittee (and indeed, the committee) does not have a single broker-dealer representative.”

SIFMA “strongly agrees” with the subcommittee’s recommendation that brokers should provide investors with up-front disclosures, similar to Form ADV, Part 2, about potential conflicts of interest, compensation arrangements, the scope of services, and other important details about the customer relationship, Carroll said.

However, SIFMA and the subcommittee “diverge” in their beliefs that investors can be harmed under the broker-dealer suitability standard, Carroll said.

“The subcommittee states that it is essential that the SEC’s Section 913 cost-benefit analysis acknowledge the harms that can result from advice delivered under the current, broker-dealer suitability standard,” he wrote.

The subcommittee’s list of “alleged harms” include: an investor mistakenly believing that a financial advisor is acting in his best interest, when that is not the case, and thereby receiving advice that carries additional costs and risks; and failure to receive ongoing account supervision.

Carroll countered, however, that “there is no evidence that investors are being harmed by the current suitability standard,” and that “there could never be an empirical showing of whether or not suitability-based advice harms investors because there are too many independent variables, including investors’ choice to follow the advice or not, and the quality of the advice given, regardless of the best intentions of the giver.”

Thus, he argued, “imposing a ‘harm’ requirement would only serve as an insurmountable obstacle to implementing Section 913 — which seems contrary to the subcommittee’s stated goal.”

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