

MEMO# 27355

July 5, 2013

Comment Letter to SEC in Response to RFI on Possible Fiduciary Duty for Broker-Dealers and IA-BD Harmonization

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TO: BROKER/DEALER ADVISORY COMMITTEE No. 32-13
OPERATIONS COMMITTEE No. 29-13 RE: COMMENT LETTER TO SEC IN RESPONSE TO RFI ON
POSSIBLE FIDUCIARY DUTY FOR BROKER-DEALERS AND IA-BD HARMONIZATION

In March, the Securities and Exchange Commission published a request for data and other information to assist it in considering whether to make new rules about the standards of conduct and regulatory obligations for broker-dealers and investment advisers when they provide personalized investment advice about securities to retail customers (the “RFI”). [\[1\]](#) ICI has submitted a comment letter in response to the RFI, which is attached and briefly summarized below.

The letter notes at the outset that nothing in the RFI is specific to the recommendation or sale of shares issued by registered investment companies. The RFI is product-neutral—its questions relate to the provision of advice about any security to retail investors, and are not limited to advice about mutual funds and other registered investment companies. The letter points out, however, that the fund industry has a significant interest in this topic because investors in nearly 30 million U.S. households own funds purchased through or with the help of financial professionals such as broker-dealers and investment advisers.

The letter has four sections. The first section outlines ICI’s position on whether, as a policy matter, the SEC should adopt a fiduciary standard of conduct for broker-dealers when they are providing personalized investment advice about securities to retail investors. The second section of the letter provides data and other information on the ownership of funds by retail customers in the United States. The final two sections address the potential impact of a fiduciary duty on broker-dealers with respect to their recommendation and sale of fund shares and the concept of harmonization of the investment adviser and broker-dealer regulatory regimes.

1. ICI’s Position on Fiduciary Duties for Broker-Dealers

The letter reiterates positions ICI has expressed in earlier testimony [\[2\]](#) on the concept of

imposing a fiduciary duty on broker-dealers when providing personalized investment advice to retail customers about securities, namely:

- That the SEC should establish a fiduciary standard for broker-dealers in that context;
- That the SEC should adopt rules establishing the new uniform fiduciary standard for advisers and broker-dealers as an “overlay” to supplement, and not supplant, the existing investment adviser and broker-dealer regimes; and
- That in crafting implementing rules, the SEC must take care to apply the fiduciary standard in a way that will not chill legitimate practices by broker-dealers, such as maintaining a commission-based business, selling proprietary investment products, servicing orphaned accounts, and engaging in trading as principal (subject to appropriate limitations, disclosure, and customer consent).

The letter also reiterates two other points made in our 2011 testimony. First, the letter encourages the SEC, as it considers the impact of a fiduciary duty on principal trading by broker-dealers, to revisit its interpretations under Section 206(3) for registered investment advisers. Second, it argues that as the standard of care for broker-dealers and advisers is harmonized, the label applied to the type of compensation they receive should no longer be relevant and advisers and broker-dealers providing personalized investment advice or recommendations should equally be permitted to receive—and share—both asset-based fees and commissions.

2. The Ownership of Funds by Retail Customers in the United States

The second section of the draft letter provides an overview of fund ownership in the United States. It includes a narrative description on the history of fund distribution and the evolution of intermediary compensation, a description of common types of fund share classes, and statistical information and trends with respect to share class ownership. The data in this section is drawn from the 2013 Investment Company Fact Book and a recent ICI Research Perspective. [\[3\]](#)

3. The Potential Impact of a Fiduciary Duty on Broker-Dealers with Respect to their Recommendation and Sale of Fund Shares

Part III of the RFI seeks data and other information on the potential implications for the marketplace with respect to establishing a uniform fiduciary standard of conduct for broker-dealers and investment advisers. Section 3 of our letter addresses this point.

The letter suggests that it is impossible to predict how imposing a fiduciary duty on broker-dealers would affect the sale of fund shares. It notes that, regardless of the approach ultimately taken by the Commission, we expect that fund sponsors will continue to design share classes to meet the needs of their various distribution partners. It also notes that certain assumptions in the RFI might suggest that the imposition of a fiduciary duty may have little or no impact on the sale of fund shares.

4. Harmonization of the IA and BD Regulatory Regimes

The RFI seeks data and other information on potential areas, other than the standard of conduct, where the Commission might consider harmonizing the regulatory obligations of broker-dealers and investment advisers. The last section of the letter addresses harmonization. It expresses the view that the Commission’s consideration of harmonization issues, at least in the near term, should be linked to its consideration of a fiduciary duty and limited to the same context. [\[4\]](#) That said, the letter suggests that the Commission

wait until markets have had a chance to adjust to any new fiduciary standard and then determine whether the imposition of the new standard has resulted in greater convergence of business models. If so, the letter suggests that further consideration of additional harmonization might be warranted.

Robert C. Grohowski
Senior Counsel
Securities Regulation - Investment Companies

[Attachment](#)

endnotes

[1] Duties of Brokers, Dealers, and Investment Advisers, SEC Release No. 34-69013 and IA-3558 (March 1, 2013), available at <http://www.sec.gov/rules/other/2013/34-69013.pdf>.

[2] See Statement by Paul Schott Stevens to the Subcommittee on Capital Markets and Government Sponsored Enterprises (Sept. 13, 2011), available at http://www.ici.org/pdf/11_house_fiduciary_stndrd_tmny.pdf.

[3] Schrass, Daniel, "Ownership of Mutual Funds Through Investment Professionals, 2012," ICI Research Perspective 19, no. 2 (February 2013), available at <http://www.ici.org/pdf/per19-02.pdf>. The Fact Book is available at <http://www.icifactbook.org/>.

[4] Unlike the rest of the RFI, this section is not expressly limited to those instances in which broker-dealers and investment advisers perform the same or substantially similar functions while providing personalized investment advice about securities to retail customers.