

**MEMO# 31320**

August 7, 2018

## **ICI Files Comment Letter with SEC on Standards of Conduct Proposals**

[31320]

August 7, 2018 TO: ICI Members  
Investment Company Directors  
Bank, Trust and Retirement Advisory Committee  
Broker/Dealer Advisory Committee  
Investment Advisers Committee  
Operations Committee  
Pension Committee  
Pension Operations Advisory Committee  
Sales and Marketing Committee  
SEC Rules Committee  
Small Funds Committee  
Transfer Agent Advisory Committee  
Variable Insurance Products Advisory Committee  
SUBJECTS: Compensation/Remuneration  
Compliance  
Disclosure  
Distribution  
Fees and Expenses  
Fund Accounting & Financial Reporting  
Fund Governance  
Intermediary Oversight  
Investment Advisers  
Operations  
Pension  
Portfolio Oversight  
Risk Oversight  
State Issues  
Trading and Markets  
Transfer Agency RE: ICI Files Comment Letter with SEC on Standards of Conduct Proposals

On August 7th, ICI filed a comment letter with the Securities and Exchange Commission on the SEC's proposals on standards of conduct for investment professionals.[\[1\]](#) Our comment letter is attached and is summarized briefly below.

The letter supports the SEC—the primary regulator of broker-dealers and investment

advisers—taking the lead to ensure that retail investors, regardless of whether they are investing for retirement or other important goals, are afforded strong protections when they receive recommendations from a broker-dealer or an investment adviser. The letter asserts that, in an area such as this, that is overseen by more than one regulatory body, coordination is crucial. We therefore strongly encourage the SEC to continue to coordinate closely with the Department of Labor so that DOL explicitly recognizes the SEC’s best interest standard of conduct (once adopted in final form) in a new, streamlined prohibited transaction exemption for financial professionals that are subject to an SEC-governed standard of conduct. Likewise, we urge the SEC, in any final rule on Regulation Best Interest, to explicitly affirm that SEC standards of conduct would preempt any standards under state law that are inconsistent with SEC regulation.

Our comments focus on the Proposals’ implications for registered investment companies (“funds”) and their shareholders, reflecting the important role funds play in helping retail investors achieve their investment goals. Many of our comments are intended to enhance the clarity of any final SEC rules, others are intended to preserve for investors the ability to choose the type of investment professional and product that can best help them pursue their investing goals, and a few recommend refinements to assure consistency with existing law.

We comment on the scope of a broker-dealer’s obligation to disclose and consider fund fees. We recommend that the SEC confirm that it would permit a broker-dealer to direct customers to the fund prospectus for detailed, standardized information about fund fees and expenses, and would not require a broker-dealer to separately calculate fund-level fees and expenses, provide individualized cost disclosure at the outset of the customer relationship, or consider only costs to the exclusion of other relevant factors in making recommendations. Specifically, we explain that: (i) funds producing comprehensive, comparable, standardized fee disclosure, as they do now, is better than requiring brokers to independently calculate fund fees, which would compromise comparability and potentially confuse investors; (ii) it would be challenging and extremely costly for broker-dealers to provide individualized cost disclosure at the outset of the customer relationship; and (iii) overemphasizing cost may discourage broker-dealers from recommending funds that offer investors other important benefits.

We then comment on SEC statements in the Proposals that are likely to discourage broker-dealers from recommending proprietary products or a limited range of products, when such a recommendation may be in the customer’s best interest. Specifically, we recommend that the SEC tailor proposed Regulation Best Interest’s Conflict of Interest Obligations to require broker-dealers to have policies and procedures reasonably designed to: (i) identify and disclose material conflicts of interest associated with a recommendation; and (ii) mitigate, or eliminate, those material conflicts of interest associated with the recommendation that create a financial incentive for the broker-dealer representative that is making the recommendation to put his or her interests ahead of the customer’s interests. We point out that this approach would be consistent with the DOL’s approach in the fiduciary rule and would appropriately focus the mitigation obligation on incentives that create a material conflict of interest for the *representative* that may influence the recommendation to the customer.

We reply to the SEC’s request for comment on the proposed definitions of retail investor/customer for purposes of Regulation Best Interest and Form CRS and recommend that the SEC adopt a single definition of “retail investor” for purposes of both rulemakings, limited to natural persons. We explain that: (i) using a single definition of “retail investor”

in both rules would provide important administrative efficiencies, facilitate compliance, and avoid confusion; and (ii) treating natural persons that are retirement plan participants, beneficiaries, or IRA owners, as “retail investors” is critical to provide consistent protections to retail brokerage customers, whether they are saving for retirement or other important goals.

We next address the SEC’s proposed interpretation of an investment adviser’s fiduciary duty. We urge the SEC to refine the interpretation so that it is more consistent with existing law regarding an adviser’s fiduciary duty. Specifically, we request that the SEC: (i) acknowledge that institutional advisory relationships may differ in important ways from retail advisory relationships, which are the focus of the proposed interpretation; and (ii) confirm that the standard for client consent under the Advisers Act is whether the adviser has provided full and fair disclosure of material conflicts and obtained informed client consent.

Finally, we reply to the SEC’s requests for comment on incorporating certain broker-dealer rules into the investment adviser regulatory framework. We recommend that the SEC not pursue these changes. We explain that the SEC has neither articulated why these potential changes would be beneficial, nor has it addressed key concerns and questions they raise.

Dorothy M. Donohue  
Deputy General Counsel - Securities Regulation

Sarah A. Bessin  
Associate General Counsel

Linda M. French  
Assistant General Counsel

## [Attachment](#)

### **endnotes**

[1] The proposals include proposed Regulation Best Interest, proposed Form CRS, and a proposed interpretation of an investment adviser’s fiduciary duty (together, “Proposals”). For a summary of the Proposals, please see ICI Memorandum No. 31185 (Apr. 26, 2018), available at [https://www.ici.org/my\\_ici/memorandum/memo31185](https://www.ici.org/my_ici/memorandum/memo31185).