

August 21, 2017

The Honorable Jay Clayton  
US Securities and Exchange Commission  
100 F Street NE  
Washington, D.C. 20549

Subject: Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisors and Broker-Dealers

Dear Commissioner Clayton,

The diverse organizations listed below are united in the view that all financial professionals should be required to act in their customers' best interests when providing personalized investment advice. We all have been strong supporters of the Department of Labor's fiduciary rule, and we support SEC rulemaking to extend that same pro-investor standard to non-retirement accounts. We are concerned, however, that a weak SEC disclosure-based rule could be used to undermine the DOL rule to the detriment of hard-working Americans saving to afford a secure and independent retirement.

The long-overdue DOL rule closes previous regulatory loopholes in the definition of fiduciary investment advice under ERISA that had enabled sales-based "advisers"—including broker-dealers and insurance producers—to avoid their fiduciary obligations when providing services that retirement savers clearly perceived and relied on as independent fiduciary advice. The same problem exists under the securities laws where broker-dealers have been permitted to market themselves as advisers, offering extensive advisory services, without triggering regulation under the Investment Advisers Act. As a result, they remain free to recommend those products that are most profitable for them, rather than those that are best for the customer, as long as the investments are generally suitable for the customer.

As the Department of Labor meticulously documented in its Regulatory Impact Analysis, investors suffer real financial harm as a result of conflicted advice. They may find themselves steered toward higher cost, less liquid, or riskier products, or they may be steered into proprietary funds when better alternatives are available. Many unsophisticated investors will never know they have been harmed, although the long-term costs can be substantial. This holds true whether the investor is saving for retirement or for a down-payment on their first home. Accordingly, any SEC rulemaking in this area must reduce the harm from conflicted advice.

Industry rule opponents would have you believe that a strong rule—one that combines a best interest standard with restrictions on conflicts of interest—would hurt the very investors it is intended to help. For example, they continue to maintain that the DOL rule is particularly harming retirement savers with smaller accounts by denying them access to valued products and services. Nothing could be further from the truth. Since the rule was finalized, a growing number of companies have come forward with product innovations and implementation plans that prove that the rule is both workable and working as intended to reduce conflicts of interest, reduce investment costs, and preserve both access to affordable fiduciary advice and the choice of

whether to pay for that advice through fees or commissions. Indeed, by transforming biased sales recommendations into fiduciary advice, the rule has dramatically expanded access to genuine advice for the small account holders who are disproportionately likely to be served by non-fiduciary salespeople masquerading as advisers. The only thing preventing retirement savers from receiving the full benefits of the DOL fiduciary rule is uncertainty over its ultimate fate.

The SEC could help to end that uncertainty by pledging to extend the central DOL rule requirements—in particular the requirement to act in customers’ best interests and to rein in conflicts of interest that undermine that goal—to all personalized investment recommendations. Toward that end, the SEC should ensure that any rule it adopts meets the following basic requirements:

- **It must apply broadly to the full range of services investors reasonably rely on as investment advice.** So, for example, if brokers continue to be permitted to hold themselves out as financial advisors and financial consultants (or other similar titles), their personalized investment recommendations should be held to the fiduciary standard appropriate to that role. Because DOL relied on FINRA guidance with regard to what constitutes a recommendation, the SEC could simply adopt that same definition for its own rulemaking purposes.
- **It must impose a true best interest standard.** DOL rule opponents have sought to water down the best interest standard to the point where it is virtually indistinguishable from the existing suitability standard. For an SEC rule to provide meaningful protections to investors, it must include an obligation to identify the best available option, from among what may be many available suitable alternatives, and recommend that best option to the customer. Brokers should be required to engage in a prudent process to identify the best available option and to document the basis on which they concluded that their recommendation was in the customer’s best interest. As with the DOL rule, the broker need not be required to identify the best option among all options available in the market, but simply the best of what the broker has available to recommend. However, the SEC should also consider whether certain product menus are so limited that they preclude the broker from meeting his or her best interest obligations.
- **It must include real limits on conflicts of interest.** Like the DOL, the SEC should seek to develop a rule that permits certain high-level conflicts, such as the receipt of commissions or sale from a limited menu of investment products, as long as those conflicts are clearly disclosed prior to the engagement. But other practices that encourage and reward advice based on factors other than the best interests of the customer should be banned or tightly limited. That includes practices such as paying advisers more to sell certain investment products, setting sales quotas for the sale of proprietary products, basing bonuses on success in meeting those quotas, and similar practices identified in the DOL Regulatory Impact Analysis. Experience since the DOL rule was adopted has shown that it is possible to rein in such conflicts. The result has been numerous pro-investor innovations, helped along by the SEC’s approval of “clean shares,” among other things.

One way for the SEC to proceed is to clarify that those firms that offer advisory services, or hold themselves out as offering such services, cannot take advantage of the existing broker-dealer “solely incidental to” exemption from the Investment Advisers Act. Permitting brokers to rely on this exemption when engaged in advisory activities has had the effect of exempting them from the fiduciary duty appropriate to that advisory role. Adopting this approach would require the SEC to determine what constitutes “holding out” as an adviser, addressing marketing practices, as well as job titles, that create the reasonable expectation among investors that they will receive advice and not just sales recommendations. It will also require the adoption of rules under the Advisers Act to address the sales-related conflicts embedded in the broker-dealer business model. Alternatively, the SEC could adopt a separate standard under the ’34 Act and FINRA rules. Here again, the SEC and FINRA would need to develop strong rules governing conflicts, as discussed above.

If the SEC is either unwilling or unable to adopt a strong rule, based on the DOL model, for broker-dealer recommendations, it should refrain from adopting a watered down rule in its place. A rule that allows brokers to claim they are acting in customers’ best interests without requiring them to rein in the practices that conflict with that standard would end up doing more harm than good. Determining what is in the best interest of customers requires a subjective judgement, and the SEC is likely to be reluctant to second-guess brokers’ decisions in any but the most egregious cases. If firms remain free to pay and reward their sales representatives in ways that encourage recommendations that promote the firm’s financial interests over the best interests of the customer, rampant abuses are likely to persist.

At a minimum, if the SEC is unable to adopt a strong pro-investor standard, it should take steps to prevent broker-dealers from marketing themselves as advisers. If that were supplemented by pre-engagement disclosures that briefly and clearly describe the sales nature of the broker’s services, i.e. that they are not held to a fiduciary best interest standard, that they have financial incentives that conflict with the interests of the customer, and that there are other providers of financial advice that are legally required to act in the customer’s best interests, investors would be modestly better off than they are today. They would have better tools at their disposal to make an informed choice among different types of financial professional.

In closing, we urge the SEC to adopt a strong pro-investor standard that requires all financial professionals to act in their customers’ best interests when providing personalized investment advice. Further, it is equally important that the SEC do nothing to undermine the strong standard already protecting Americans’ retirement savings, thanks to the DOL. It would be a gross disservice to the numerous unsophisticated retirement investors if the SEC were to undermine those protections in the name of promoting uniformity.

Sincerely,

AFL-CIO  
AFSCME  
Alliance for Retired Americans  
American Association for Justice  
Americans for Financial Reform

Arizona PIRG  
Better Markets  
CALPIRG  
Center for American Progress  
Center for Economic Integrity  
Center for Economic Justice  
Colorado Public Interest Research Group (CoPIRG)  
Committee for the Fiduciary Standard  
ConnPIRG  
Consumer Action  
Consumers for Auto Reliability and Safety  
COPIRG  
CtW Investment Group  
Economic Policy Institute  
Florida Alliance for Consumer Protection  
Florida Consumer Action Network  
Florida PIRG  
Fund Democracy  
Georgia PIRG  
Illinois PIRG  
Indiana PIRG  
International Association of Machinists & Aerospace Workers  
International Brotherhood of Electrical Workers  
Iowa PIRG  
Kentuck Equal Justice Center  
Maryland PIRG  
Massachusetts Consumers Council  
MASSPIRG  
MontPIRG  
MoPIRG  
NAACP  
National Consumer League  
National Employment Law Project  
National Organization for Women  
NCPIRG  
NHPIRG  
NJPIRG  
NMPIRG  
Ohio PIRG  
Oregon PIRG (OSPIRG)  
PennPIRG  
Pension Rights Center  
PIRG in Michigan (PIRGIM)  
Public Citizen  
RIPIRG  
Service Employees international Union

Tennessee Citizen Action  
Texas Public Interest Research Group  
TexPIRG  
The Center for Popular Democracy  
The Midas Collaborative  
U.S. PIRG  
U.S. PIRG  
UnidosUS  
UNITE HERE  
United Mine Workers of America  
United Policyholders  
WASHPIRG  
WISPIRG  
Woodstock Institute  
Worker Owner Council of the Northwest