



Consumer Federation of America

Position Paper

The Need for a Fiduciary Duty Standard for All Financial Advisers

Background – the Problem for Investors

Most investors choose to rely on a professional – a broker, a financial planner, or an investment adviser – to help them make investment decisions. In doing so, investors rely heavily, if not exclusively, on the recommendations they receive from these financial intermediaries. Surveys show, for example, that the typical mutual fund investor does little if any additional research on the funds that are recommended; instead, they do exactly what their broker or financial planner or investment adviser suggests without second-guessing that recommendation. This makes investors extremely vulnerable, particularly given the conflicts of interest that pervade the securities industry and investors' difficulty in distinguishing between sales- and advice-based services.

Although the services they provide are often virtually indistinguishable to the average investor, investment advisors and broker-dealers are regulated under different statutory and regulatory frameworks. Brokers are required to make recommendations that are generally “suitable” for the investor; investment advisers are subject to an overarching fiduciary duty under the Investment Advisers Act of 1940. As fiduciaries, investment advisers have an affirmative duty to act in the best interests of their clients and to make full and fair disclosure to clients regarding conflicts of interest. Brokers do not. As a result, brokers are free to receive higher compensation for recommending a particular product, even if another would be better for the customer, without having to disclose this fact to the customer. Meanwhile, though brokers are regulated and conduct themselves as salespeople, they have encouraged investors to rely on them as advisers, by rebranding their salespeople as financial advisers, offering extensive advisory services, such as investment planning, and marketing their services based on the advice offered.

The Securities and Exchange Commission (SEC) has, but has failed to use, existing authority to apply the Advisers Act to what are clearly advisory activities performed by broker-dealers. In fact, the current investor confusion is the direct result of the SEC's repeated refusal to use that authority. Instead, every time the SEC has had to choose between protecting investors and protecting the broker-dealer business model, it has chosen to protect brokers at the expense of investors.

The Solution for Investors: a Fiduciary Duty for All Investment Advice

Brokers and advisers should be held to the same high standards depending not on the statute under which they are registered, but upon the services they are providing to clients. If the service being offered bears the core characteristics of investment advisory

services from the investor's perspective, it should be subject to the same high standards and duties that apply to other investment advisers.

To accomplish this goal, Congress should apply the Advisers Act fiduciary duty to all financial professionals who give investment advice regarding securities – broker-dealers, financial planners, and investment advisers alike. This step will enhance investor protection, eliminate confusion, and promote regulatory fairness by establishing conduct standards according to the nature of the services provided, not the licensing status of the provider.

Under such an approach, all those who offer investment advice would be required to act solely in their clients' best interests without regard to their own interests, to disclose material information including conflicts of interest, and to take steps to avoid and minimize those potential conflicts. Once triggered, that fiduciary duty should govern the entire relationship. Specifically, brokers must not be allowed to provide financial planning or investment planning services under a fiduciary duty only to shed that duty when implementing their recommendations, the point at which conflicts of interest are at their highest.

At the same time, those who choose to offer solely sales-based services should not be permitted to adopt titles that imply that they are advisers. Either they should be prohibited from using titles, such as financial adviser or financial consultant, designed to mislead the investor into thinking they are in an advisory relationship, or use of such titles should automatically carry with it a fiduciary duty to act in clients' best interests.

Congress should impose a fiduciary duty to act in the client's best interests on all who provide investment advice. President Obama's financial reform plan includes a strong set of proposals to do just that by subjecting all those who give investment advice a fiduciary duty and by proposing an examination and reform of the securities industry compensation practices that encourage financial professionals to act in ways that do not benefit their clients. To ensure that the draft legislation to implement the plan achieves its intended goals, however, we believe some fairly simple changes to the legislative language are needed. We suggest that the legislation should be revised to require, rather than simply permit, the SEC to act, to unambiguously impose a fiduciary duty in the statutory language, and to clarify that no weakening of the fiduciary duty that exists under the Investment Advisers Act is permitted.