OFFICE OF
THE COMMISSIONER

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D.C. 20549

July 25, 2017

Timothy D. Hauser
Deputy Assistant Secretary for Program Operations
Office of Exemption Determinations
Employee Benefits Security Administration
Attn: D-11933
U.S. Department of Labor
Suite 400, 200 Constitution Avenue, NW
Washington, D.C. 20120

VIA ELECTRONIC MAIL: EBSA.FiduciaryRuleExamination@dol.gov

Re: Department of Labor (the "**Department**") Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions (RIN 1210-AB82)

Dear Mr. Hauser:

I am grateful for the opportunity to comment—on my own behalf and representing my own views—on the Department's final rule (the "**Fiduciary Rule**"),[1] defining the term "fiduciary" for purposes of the Employee Retirement Income Security Act of 1974 ("**ERISA**")[2] and the Internal Revenue Code (the "**Code**")[3] with respect to the provision of investment advice for a fee or other compensation in connection with an ERISA plan or individual retirement account ("**IRA**").

In my capacity as a Commissioner of the Securities and Exchange Commission (the "**Commission**"), I have had ample opportunity to consider the role of both conflict of interest disclosures and fiduciary standards in the context of registered broker-dealers and investment advisers. I have many concerns with the Fiduciary Rule and write to convey three of the most salient:

- First, the Fiduciary Rule is dismissive of the efficacy of conflict of interest disclosure, a view that runs contrary to decades of Commission experience.
- Second, the Fiduciary Rule fails sufficiently to distinguish "selling" activities from "advice" activities, undermining the Commission's longstanding approach to regulation of broker-dealers and investment advisers.
- Third, the effects of the Fiduciary Rule will extend beyond retirement accounts and will be disruptive of the broker-client relationship in general.

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[1] 81 Fed. Reg. 20946 (Apr. 8, 2016).
[2] 29 U.S.C. § 1002(21)(A)(ii) (2012).
[3] 26 U.S.C. § 4975(e)(3)(B) (2012).

1. **The Fiduciary Rule dismisses disclosure as ineffective, in stark contrast to the Commission's long experience with the regulation of conflicts of interest.**

Broadly, the concern motivating the Fiduciary Rule is that unsophisticated consumers of financial services are easily confused as to whether the providers of such financial services are obligated to act in a consumer's best interests. This concern is not surprising given that companies offering the execution of securities transactions and provision of investment advice often hold themselves out as "financial advisors/advisers" or any of a variety of trade names that skirt the legal categories set forth in the Commission's regulations. Indeed, the Commission's own staff has issued a study finding that "many retail investors do not understand and are confused by the roles played by investment advisers and broker-dealers," and noting that "'many investors are also confused by the standards of care that apply to investment advisers and broker-dealers' when providing personalized investment advice about securities."[4]

The Commission has historically sought to ensure the accuracy of disclosures in the interests of informing investors. In fact, the Commission has carefully weighed the effectiveness of disclosure throughout the course of its eight decades of existence. Many commenters on the Fiduciary Rule have noted the Department's apparent dismissal of disclosure-based remedies to the very real conflicts of interest that arise in the financial services industry. In the final rule release of April 8, 2016, the Department variously states that "disclosure alone has proven ineffective to mitigate conflicts in advice";[5] "some research suggests that even if disclosure about conflicts could be made simple and clear, it could be ineffective—or even harmful";[6] "the Department . . . is not prepared to conclude that written disclosures, including models developed by the Department, are sufficient to address investor confusion about financial conflicts of interest";[7] and "a disclosure regime, standing alone, would not obviate conflicts of interest in investment advice even if it were possible to flawlessly disclose complex fee and investment structures."[8] The Department characterizes disclosure requirements as mere "fine print" or "boilerplate," drawing "fine legal distinctions" that are "often completely lost on plan participants and IRA owners who receive investment advice."[9]

I would suggest that the Department's view of the efficacy of disclosure is excessively dour. As one group of scholars stated in critiquing the White House report on which the Department largely drew in promulgating the Fiduciary Rule, the report—and by extension, the Fiduciary Rule—is "contrary to standard economic theory which typically indicates that disclosure and full-information is a solution to conflict problems and that 'sunshine is the best disinfectant.'"[10]

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[4] Press Release, Commission, SEC Releases Staff Study Recommending a Uniform Fiduciary Standard of Conduct for Broker-Dealers and Investment Advisers (Jan. 22, 2011), https://www.sec.gov/news/press/2011/2011-20.htm.
[5] 81 Fed. Reg. at 20950.
[6] *Id*. at 20951.
[7] *Id*. at 20981.
[8] *Id*. at 20982.
[9] *Id*. at 20955.
[10] Jeremy Berkowitz, Renzo Comolli, and Patrick Conroy, *Review of the White House Report Titled 'The Effects of Conflicted Investment Advice on Retirement Savings*', at 2,

As it has throughout its history, the Commission continues to examine and consider whether changes to its disclosure are warranted to address current issues in the ever-evolving securities markets. Indeed, pursuant to an initiative of the Commission's Office of the Investor Advocate—the Policy Oriented Stakeholder and Investor Testing for Innovative and Effective Regulation ("**POSITIER**")—the agency is currently engaged in a state-of-the-art, evidence-based study to inform the rulemaking process with evidence obtained from surveys and tests of the potential impacts of proposed policy changes, prominently including disclosure-oriented policies.[11] Congress clarified the Commission's authority to engage in such consumer testing in the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**"),[12] and the committee report of the Senate Committee on Banking, Housing, and Urban Affairs makes clear legislators' continued emphasis on disclosure-based regulation.[13]

Rather than dismiss out of hand the role of disclosure in policing conflicts of interest, I would strongly encourage the Department to redouble its efforts to work with the Commission and its expert staff, who may bring to bear our decades of experience in enforcing multiple disclosure-based regimes. As I recently stated in my remarks before the 2017 SEC Speaks conference, "our system of disclosure comports well with American traditions of self-reliance, pioneering spirit, and rugged individualism."[14]

Moreover, I remind the Department that this commitment to disclosure-based regulation also comports with the legislative intent of Congress. The Department's suggestion that disclosures—no matter how clear or transparent—may actually cause *harm* to investors runs contrary to, *inter alia*, (i) Sections 206(1) and 206(2) of the Investment Advisers Act of 1940 (the "**Advisers Act**"),[15] as interpreted by the Supreme Court;[16] (ii) Congress's grant of authority to the Commission to consider the establishment of a "best interest" standard of conduct applicable to broker-dealers;[17] and (iii) Section 913 of the Dodd-Frank Act, which amended both the Advisers Act and the Securities Exchange Act of 1934 (the "**Exchange Act**") to require that the Commission "facilitate the provision of simple and clear disclosures to investors regarding

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http://www.nera.com/content/dam/nera/publications/2015/PUB_WH_Report_Conflicted_Advice_Retirement_Savings_0315.pdf.

[11] *See* Press Release, Commission, SEC's Office of the Investor Advocate to Hold Evidence Summit, Launch Investor Research Initiative (Mar. 2, 2017), https://www.sec.gov/news/pressrelease/2017-59.html.

[12] Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[13] *See* S. Rep. No. 111-176, at 104 ("The AARP told the Committee that it 'supports the explicit authority granted to the [Commission] to test rules or programs by gathering information and communicating with investors and other members of the public. This type of testing has the very real potential to improve the clarity and usefulness of the disclosures that our securities regulatory scheme relies upon.'"). *See also id.* at 107 ("The Committee believes that investors must be provided with relevant, meaningful, and timely disclosures about financial products and services from which they can make better informed investment decisions. The Committee encourages the SEC to use . . . consumer testing . . . to inform its scope of disclosures.").

[14] Commissioner Michael S. Piwowar, Remarks at the "SEC Speaks" Conference 2017: Remembering the Forgotten Investor (Feb. 24, 2017), https://www.sec.gov/news/speech/piwowar-remembering-the-forgotten-investor.html.

[15] 15 U.S.C. § 80b-6(1) and (2) (2012).

[16] *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191-2 (1963) (holding that the duty to disclose all material information is intended "to eliminate, or at least expose, all conflicts of interest which might incline an investment adviser—consciously or unconsciously—to render advice which is not disinterested").

[17] *See* 15 U.S.C. § 78o(k)(1) (2012); *see also* 15 U.S.C. § 80b-11(g)(1) (2012).

the terms of their relationships with brokers, dealers, and investment advisers, including any material conflicts of interest."[18]

2. The Fiduciary Rule fails sufficiently to distinguish "selling" activities from "advice" activities, undermining the Commission's longstanding approach to regulation of broker-dealers and investment advisers.

The Fiduciary Rule fails to distinguish the securities *selling* activities that have traditionally been the province of broker-dealers under the U.S. system of market regulation and the *advice* activities in which regulated investment advisers engage. This distinction was created by Congress over 70 years ago when it enacted distinct regulatory frameworks for selling activities (*i.e*., in the Exchange Act) and advice activities (*i.e*., in the Advisers Act).[19]

Under these frameworks, an investment adviser is a fiduciary with a duty to serve the best interests of its clients, including the obligation not to subordinate clients' interests to its own. As a fiduciary, an investment adviser owes a duty of loyalty and care to its clients. By contrast, a broker-dealer generally is not considered a fiduciary. Broker-dealers are required to deal fairly with their customers, pursuant to Commission and self-regulatory organization rules, such as those of the Financial Industry Regulatory Authority ("**FINRA**"). This duty of fair dealing includes the key customer protections of "suitability" and "best execution." The suitability obligation requires a broker-dealer to make recommendations that are consistent with the investment profile of its customer, while best execution requires a broker-dealer to provide the best execution reasonably available for client trades. Broker-dealers are also required to disclose material conflicts of interest to their customers when making a recommendation.

Each of these two regimes provides effective oversight of the specific activities they were designed to address. However, in the ongoing debate as to the creation of a uniform fiduciary duty for broker-dealers and investment advisers, it is sometimes asserted that a broker-dealer's duties have less "bite" than an investment adviser's obligations. This claim overlooks the robust regulatory scrutiny to which broker-dealers' selling activities are subject by both the Commission and FINRA.[20] The substantive regulation of broker-dealers and the tailored

[18] 15 U.S.C. § 80b-11(h)(1) (2012); 15 U.S.C. § 78o(l)(1) (2012).
[19] The regulatory framework recognizes that the same person or entity might engage in both selling and advice activities and specifies that the type of activity the entity is engaged in determines the applicable regulatory scheme. For example, Section 202(a)(11)(C) of the Advisers Act provides an exemption from the definition of an investment adviser and thus from applicability of the Adviser Act, for a broker-dealer that for compensation engages in the business of advising others if such service is solely incidental to the conduct of his business as a broker or dealer and he receives no special compensation for those services. 15 U.S.C. § 80b-2(a)(11)(C). However, if a broker-dealer's advice is not merely incidental to the broker-dealer's selling activity the broker's advisory activity is subject to regulation under the Advisers Act, while the broker's selling activities remain subject to regulation under the Exchange Act. This dual application of both the Exchange Act to the broker-dealer's selling activities and the Advisers Act to the broker-dealer's advisory activities results in the dual registration of some entities as both broker-dealers and investment advisers. As of July 10, 2017, there were approximately 370 entities dually registered as broker-dealers and investment advisers with the Commission.
[20] According to FINRA statistics, from January 1, 2016 through June 30, 2017, approximately 85 actions brought by FINRA against broker-dealers and associated persons included violations of suitability rules. These actions have resulted in a total of approximately $29 million in fines assessed against approximately 14 firms and 55 registered

regulation of "selling" and "advice" activities are core principles of our securities regulatory regime that should not be overlooked.

3. **The effects of the Fiduciary Rule will extend beyond retirement accounts and will be disruptive of the broker-client relationship in general.**

While ostensibly targeted narrowly to the ERISA plan and IRA account markets under the Department's supervision, the Fiduciary Rule will have significant, unintended consequences for the broader relationship between the consumers and the providers of financial services. These consequences stem from the fact that many broker-dealers provide financial services to clients for *both* their ERISA and IRA retirement portfolios *and* their non-retirement securities accounts.

Under the Fiduciary Rule, a broker-dealer performing the same type of service for a single client's retirement and non-retirement securities accounts would be subject to separate obligations based on the regulatory status of each account. It is highly likely that when confronted with this compliance challenge, a broker-dealer subject to the Fiduciary Rule with respect to a client with an ERISA or IRA account will feel compelled to apply the same standard to that client's other securities accounts. Similarly, compliance burdens may drive a broker-dealer subject to the Fiduciary Rule for some accounts to apply the same standard to all of the accounts the broker administers. In short, the Fiduciary Rule will have a dramatic impact on the provision of financial services to retail clients throughout the financial services industry.

Thank you very much for your consideration.

Respectfully submitted,

Michael S. Piwowar
Commissioner

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representatives. In addition, approximately 30 registered representatives were barred, 55 were suspended, and 4 firms were expelled. More than $38 million in restitution was ordered to be paid to investors.