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Battle Lines Continue to Form Over the DOL's Fiduciary Proposal

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Earlier this month, the ***Securities Industry and Financial Markets Association*** ("SIFMA") released its "Proposed Best Interests of the Customer Standard for Broker-Dealers" – an alternative to the U.S. Department of Labor's ("DOL") proposed regulation addressing the standard of care for broker-dealers and other financial professionals who provide retirement investment advice. Unlike the DOL's proposed rule, which we wrote about here, SIFMA's across-the-board proposal emphasizes disclosure and investor consent as mechanisms to promote a *uniform* "best interest" standard.

In remarks accompanying SIFMA's announcement, Kenneth E. Bentsen, the organization's President and CEO, reiterated SIFMA's support for a uniform standard to govern broker-dealers and investment advisers providing investment advice to retail customers. Mr. Bentsen highlighted a number of issues with the current DOL proposal, expressing specific concern that it would limit access to affordable retirement services and result in investor confusion. Mr. Bentsen explained that, given the increased liability risk and compliance costs associated with the current DOL proposal, firms have indicated that, if enacted, they plan to shift their commission-based brokerage accounts to (more expensive) fee-based accounts. Because, according to Mr. Bentsen, most firms are willing to provide fee-based services only for higher-balanced accounts, this could potentially leave millions of consumers with "no option for advice or guidance." In addition, Mr. Bentsen said that "it is hard to see how investors won't be confused" by the DOL's proposed rule, which will apply different standards to broker-dealers when they provide retirement-related investment advice than when they provide investment advice that is not retirement related.

Mr. Bentsen's remarks echo recent criticism from FINRA CEO Richard Ketchum (which we blogged about here and here) and members of the U.S. House of Representatives. In a hearing before the House Subcommittee on Health, Employment, Labor, and Pensions earlier this week, committee members voiced their concern that the DOL proposal "would make it harder for working families to save and plan for retirement." During the hearing, Representative Phil Roe, the committee chair, asked U.S. Secretary of Labor Thomas Perez to withdraw the DOL proposal and to "work with this committee on a responsible, bipartisan approach that will strengthen protections for investors and preserve robust access to financial advice." Going even further, the House Appropriations Committee this week inserted language in the FY2016 Labor, Health and Human Services funding bill that would prohibit the DOL from using appropriated funds “to finalize, implement, administer, or enforce” the proposed rule.

In place of the DOL proposal, SIFMA maintains that the ideal rule would involve a uniform standard – implemented by the U.S. Securities and Exchange Commission (“SEC”) – that applies “across all investment recommendations made to individual retail customers in all brokerage accounts.” In addition, SIFMA argues that stakeholders should “follow the traditional securities regulatory approach of establishing a rules-based heightened standard, including robust disclosure, coupled with robust examination, oversight, and enforcement by the SEC, FINRA and state securities regulators, as well as a private right of action for investors.” According to SIFMA, the standard should include the following core elements:

1. A legal and enforceable best interests obligation,
2. Consideration of investment-related fees,
3. Efforts to mitigate material conflicts of interest, and
4. Various disclosure requirements.

SIFMA’s proposal, which includes a mark-up of FINRA Rule 2111, would define a “best interests recommendation” as one that demonstrates “the care, skill, prudence, and diligence . . . that a prudent person would exercise based on the customer’s investment profile,” *e.g.*, his or her age, financial situation, and investment objectives. The SIFMA proposal also would require broker-dealers to “appropriately disclose and manage investment-related fees” and “avoid, or otherwise appropriately manage, disclose, and obtain consents to, material conflicts of interest.”

Since its release, SIFMA’s proposal has been criticized by investor advocates, who argue that it is too narrow and fails to align broker-dealer incentives with those of their customers. The Consumer Federation of America (“CFA”) has noted that the regulatory authority of FINRA and the SEC extends to securities markets only – thus, it would not apply to advice relating to insurance products and non-securities, like art and gold, that are frequently marketed to retirees. The CFA has emphasized that “SIFMA’s proposal also would apply only to retail accounts” and would “not cover investment advice provided to employer retirement plans.” The CFA’s Director of Investment Protection, Barbara Roper, criticized the SIFMA proposal in a recent Wall Street Journal article. She questioned the efficacy of managing conflicts through disclosure and consent, arguing that “if you tell advisers that they have to act in the customer’s best interest, but you still pay or reward them for acting against their customer’s best interest, disclosing you have a conflict isn’t going to solve that problem.”

What is clear is that the battle lines have formed and there is certainly more debate and jockeying for position to occur. What remains to be seen is whether the SEC will puts its finger on the scale. Stay tuned.

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