

Opening Statement of Karen L. Barr
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SEC Investor Advisory Committee Meeting
Discussion of the Commission's Proposed Regulation Best Interest and Proposed
Restriction on the Use of Certain Names or Titles
June 14, 2018

Good morning Chairman Clayton, Commissioners Stein, Piwowar, Jackson and Peirce, members of the Investor Advisory Committee, and my fellow panelists. Thank you for inviting me to speak today.

The Investment Adviser Association represents the interests of a broad range of SEC-registered investment advisers. Our 650 member firms collectively manage more than \$20 trillion in assets for a wide variety of individual and institutional investors. Since its founding in 1937, the IAA has been the leading voice in promoting high standards of ethical and fiduciary responsibility for the investment advisory profession.

Investment advisers stand in a special relationship of trust and confidence with, and are fiduciaries to, their clients. This fiduciary duty – which includes the duty of loyalty and the duty of care – serves as the bedrock principle of investor protection for clients of investment advisers. Put simply, this duty requires advisers to act in the best interest of their clients at all times and not to put their own interests ahead of their clients' interests. The IAA has advocated for the past two decades that the principles underlying this fiduciary duty should apply to all financial professionals providing investment advice about securities.

Chairman Clayton, thank you for your leadership in launching this package of proposals for comment. We appreciate the Commission's thoughtful consideration of this complex and critically important investor protection issue. These proposals will impact the millions of investors who seek advice from financial professionals to secure their financial futures. We commend the Commission for taking action intended to enhance investor understanding and strengthen the standard of conduct for broker-dealers in their relationships with retail customers. We share these important goals.

While we are still working through all aspects of the package, I will offer some preliminary observations. At the outset, we are pleased that the Commission preserved the fiduciary duty standard for investment advisers under the Advisers Act, while drawing on those principles to articulate a heightened standard of conduct for broker-dealers in Regulation Best Interest.

Today, broker-dealers are required to determine that their recommendation is suitable for the customer based on the customer's investment objectives and profile, and they must "observe high standards of honor and just and equitable principles of trade." Virtually all commentators, including this Committee, have advocated for a heightened standard that is as robust as the fiduciary standard.

Proposed Reg BI is a significant step in the right direction. Under Reg BI, a broker-dealer would be required to act in the best interest of a retail customer when making a recommendation. Reg

BI would also enhance the disclosure obligations of broker-dealers with respect to retail customers.

We have some concerns, however, with respect to the scope and certain aspects of the proposed requirements. For example, Reg BI would apply only at the time of and to a specific recommendation. This differs from an investment adviser's fiduciary duty, which applies to the entire advisory relationship agreed to by the adviser and client, even where that relationship is limited in scope or duration. The duty owed in the context of that agreed-upon relationship cannot be turned on and off and cannot be waived. The client may reasonably expect that its adviser is acting in its best interest throughout the relationship and the adviser is under an obligation to do so.

In contrast, Reg BI does not appear to apply when a broker-dealer provides ongoing advice or ongoing monitoring of investments or creates a reasonable expectation that it will do so. We are concerned that this may constitute a gap in the standard of conduct. It is critically important to resolve any ambiguity regarding what standard of conduct would apply where a broker, whether through agreement, course of conduct or by virtue of holding out, has something other than an episodic relationship with an investor. We continue to analyze whether Reg BI would sufficiently protect investors under these and various other scenarios.

The concept of how ongoing monitoring is treated under Reg BI relates to the other topic of this panel – the way in which some broker-dealers market themselves as providing ongoing advice to customers. We have raised concerns with the Commission over the years about the potential for investor confusion resulting from broker-dealers holding themselves out as having a relationship of trust and confidence with their customers but then disclaiming that they are subject to a fiduciary duty. We are pleased that the Commission is proposing to restrict stand-alone broker-dealers from using the term “adviser” or “advisor” when communicating with retail investors. This is a good first step. But we are concerned that firms will simply switch to other titles that could lead investors to believe that their financial professional owes them an ongoing duty when that may not be the case.

We also continue to believe that factors in addition to the use of titles contribute to investor confusion. How is a firm marketing itself and how would a reasonable investor interpret that marketing? Is that marketing or other course of conduct consistent with the applicable legal duty or with the services the firm actually offers? And would those services still be solely incidental to the firm's brokerage business, or should the firm be subject to the Advisers Act when offering those services?

This last question relates to a request for comment in the Reg BI Release on the definition of “solely incidental.” We fully agree with earlier positions taken by the Commission that discretionary advice cannot be solely incidental to the business of a broker-dealer, and that broker-dealers providing discretionary advice should be treated as investment advisers.

Let me now turn to the proposed Reg BI disclosures. We are pleased that Reg BI would require disclosure of material facts regarding the scope and terms of the relationship as well as material conflicts of interest associated with a recommendation. The proposed disclosure requirements, however, are somewhat vague, and do not prescribe any particular format or type of disclosure. This is in contrast to the apples-to-apples disclosure that investment advisers provide in Form

ADV, Part 2A and certain of their employees provide in Part 2B. These disclosures must address specific issues and must be provided in a consistent format. Further, as the Commission notes, this proposed Reg BI disclosure is closely connected with proposed Form CRS and the proposed Regulated Status Disclosure. These three disclosure components of the rulemaking package are critically important to addressing investor understanding and confusion.

In this regard, we commend the Commission for conducting investor testing to assess one of these components - the efficacy of the proposed Form CRS. However, it is not clear that the results of this testing will be made public by the Commission with sufficient time to allow for analysis and comment. Therefore, we have asked the Commission to extend the comment deadline to provide commenters with time to fully consider and incorporate the results of the testing. We have significant concerns regarding many aspects of Form CRS, including that it may cause additional investor confusion. The investor testing results will assist us in developing alternative examples of more effective disclosure to share with the SEC and its staff.

Though not the subject of this panel, I will note that we concur with the general principles outlined in the proposed interpretive guidance on the investment adviser fiduciary duty. We will, however, provide comments to address any areas of potential ambiguity and identify aspects of the release that do not work or need clarification for institutional clients. We will also be responding to the Commission's request for comment on certain additional areas of investment adviser regulation.

We are committed to working constructively with the Commission on these and other aspects of the package of proposals. We recognize and appreciate the substantial efforts of the Commissioners and SEC staff in issuing the proposals and the opportunity to engage on these critically important issues. Thank you again for inviting me to speak today.