July 25, 2013

Elizabeth Murphy
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

RE: Duties of Brokers, Dealers and Investment Advisers
SEC Release No. 34-69013; IA-3558; File No. 4-606

Dear Ms. Murphy:

AARP[1] submits this comment letter in response to the request for data and other information ("Request for Information" or "RFI") concerning a potential uniform fiduciary standard of conduct for both broker-dealers and investment advisers when providing personalized investment advice to retail customers. We believe this Request is an important step forward in accomplishing one of the most important reforms the SEC can undertake to benefit retail investors: ensuring that all financial industry participants who provide clients with advice about securities are held to a fiduciary standard. A rule imposing the fiduciary duty on brokers providing investment advice to clients is long overdue, and the SEC should act as quickly as possible to close this regulatory gap.

As you move forward in drafting rules to extend the fiduciary duty standard of care to broker-dealers, AARP urges you to adopt a uniform standard that would apply to both broker-dealers and investment advisers when providing personalized investment advice to retail customers, as contemplated by Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). The fiduciary standard should be no less stringent than the existing fiduciary duty standard under the Investment Advisers Act of 1940 (the "Advisers Act"). The standard should be based on the core principle that when providing personalized investment advice to retail customers, a financial adviser – no matter how they market themselves, what their business model is, or what their registration status is - must always act in the best interests of those customers.

While we are encouraged that the SEC has taken the step of requesting additional information from interested parties, we are concerned that the assumptions contained in

[1] AARP is a nonprofit, nonpartisan membership organization that helps people 50+ have independence, choice, and control in ways that are beneficial and affordable to them and society as a whole. AARP advocates for policies that enhance and protect the economic security of individuals.

the RFI fail to include key elements of the fiduciary standard, such as the obligation to act in the best interest of the customer. If the fiduciary duty rulemaking going forward is based on the RFI assumptions, it would be weaker than that originally set forth in the Section 913 Study and less rigorous than that currently imposed under the Advisers Act. Indeed, the RFI seems to contemplate little more than the existing suitability standard supplemented by conflict of interest disclosures. If the SEC were to adopt this approach, it would significantly weaken the fiduciary standard for investment advisers while adding few new protections for investors who rely on broker-dealers for investment advice. AARP opposes this backwards approach that would have negative consequences for investors.

We are hopeful that this public comment period will assist the Commission in crafting a fiduciary rulemaking that calls for an enforceable, principles-based obligation on brokers and advisers to act in the best interests of their clients, without regard to the financial or other interests of the broker or adviser.

Why the fiduciary standard matters

Many broker-dealers are not subject to a fiduciary duty when they provide personalized investment advice to their clients. Instead, they are required only to make suitable investment recommendations. There is no obligation under the suitability rule to have reasonable grounds to believe that a recommendation is in the best interest of the customer. If a security recommended by a broker-dealer is suitable for a customer, but a different security would be a better choice for the customer, there is no obligation to recommend the better-suited security. The broker-dealer is free to recommend the security that pays the broker-dealer the highest compensation, as long as it is suitable, and the broker-dealer is not necessarily obligated even to disclose the conflict of interest that the differential compensation represents

While the duty to make suitable recommendations prohibits many abusive practices, it does not require, as a fiduciary duty would, that broker-dealers or their representatives give advice that is in the best interest of their clients. The higher fiduciary standard of care would make a substantial difference in the quality of investment advice, and thus enhance the retirement security of individual investors.

This issue is of keen interest to AARP for the simple fact that individuals today shoulder a significant responsibility to make appropriate investment choices so that they have adequate income to fund their retirement years. According to one industry observer in remarks before financial services executives, “The boomers who retire over the next 20 years are going to roll over their 401(k)s, downsize their houses and sell their small businesses. The result will be a mass movement of money from retirement plan assets, personal assets and other illiquid assets to investable assets. As financial service professionals, almost all of you are dealing investable assets. So your business will be a very good one to be in over the next 20 years."[2] Given the increasing number of Americans preparing for and reaching retirement who will need investment advice and guidance, rulemaking to extend the fiduciary duty of care to all financial professionals who offer investment advice may be the single most important step the SEC can take to promote retirement security for average Americans.

A recent report for the AARP Public Policy Institute summarized why the fiduciary standard benefits all investors, but is of particular importance to older investors:

> The law has long held that investment advisory relationships involve the kind of technical knowledge and trust and confidence that warrant imposing a fiduciary duty, the importance of which is heightened for older investors. People over 50 have less time to make up for losses, and retired investors are less likely to be able to find a paying job to offset financial reversals. As people age, their resistance to abusive sales practices may decline; conversely, their appeal to fraudsters as targets may increase.
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> Older investors therefore are at greater risk under fraud-based standards where a *caveat emptor* defense that the victim chose the inappropriate investment can be sufficient to defeat a claim. This defense often fails where the fiduciary duty affirmatively requires that the adviser act in the best interest of the client. It is therefore with respect to vulnerable investors that the fiduciary duty is likely to have the greatest effect, because it is designed to protect investors who may be less able to protect their own interests. This vulnerability is greatest when broker-dealers' and investment advisers' compensation depends not on the quality of their services or the performance of the products that they recommend, but on the product the client purchases. The fiduciary duty requires avoidance of such conflicts of interest and full disclosure of conflicts when avoidance is not practicable. … Imposing a fiduciary duty on persons who provide retail investment advice is no panacea, but it does not need to be. It is simply good policy that will enhance Americans' financial security.[3]

AARP's research indicates that investors do not understand the different legal standards that apply to brokers and investment advisers. They simply expect financial intermediaries to be required to act in their (the customer's) best interest. Further, older Americans may not be able to tell you the precise legal definition of fiduciary, but they do have clear views on what they expect from financial professionals. In six state-specific opinion polls conducted by AARP during consideration of the Dodd-Frank Act,

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[2] "Retiring boomers fuel surge in planning, investments," Warren S. Hersch, LifeHealth Pro, April 9, 2013, accessed at http://www.lifehealthpro.com/2013/04/09/retiring-boomers-fuel-surge-in-planning-investment

[3] "Protecting Investors— Establishing the SEC Fiduciary Duty Standard", Mercer Bullard, Associate Professor, University of Mississippi School of Law, a research report prepared on behalf of the AARP Public Policy Institute, September 2011, accessed at http://assets.aarp.org/rgcenter/ppi/cons-prot/rr2011-02.pdf

AARP asked residents at least 50 years old questions related to the various investor and consumer reforms under consideration. Overwhelmingly, respondents favored requiring financial professionals to put the clients interest ahead of their own when making recommendations, as well as disclosing upfront any fees or commissions they earn, and any conflicts of interest that potentially could bias that advice. The level of support for this reform ranged from a low of 88 percent (Arkansas) to a high of 95 percent (Indiana)[4].

The SEC should close the regulatory gap

The regulatory imbalance between the duties of brokers and investment advisers has persisted for many years, even as evidence demonstrating that brokers have transformed themselves from salesmen into advisers has grown. Brokers today call themselves "financial advisers," offer services that clearly are advisory in nature, and market themselves based on the advice offered. As a result, retail investors are routinely lured into believing that a broker is acting as a trusted adviser. Not surprisingly, the average investor cannot distinguish between brokers and advisers and certainly does not recognize that their "financial adviser" operates under a lower legal standard than that to which an investment adviser is held.

Research has found that investors typically rely heavily on the recommendations they receive from brokers and investment advisers alike, and generally do not second-guess those recommendations even if they understand, although most do not, the significant conflicts that may bias those recommendations. The trust most investors place in financial professionals is actively encouraged by industry marketing, leaving investors vulnerable not only to fraud, but also to those who would take advantage of that trust in order to profit at their expense.

Investors deserve a regulatory system for investment professionals that is designed to promote the best interests of the investor and that imposes comparable standards on investment professionals who are performing essentially the same function. Ensuring that all securities professionals who offer investment advice to retail investors are subject to a fiduciary standard is a necessary component of a rationale, pro-investor system of regulation.

Principles for a Uniform Fiduciary Standard for Brokers and Advisers

There is general agreement that personalized investment advice should be subject to a fiduciary standard regardless of whether that advice is offered by a broker-dealer or an investment adviser. Section 913 of the Dodd-Frank Act provides a framework for

[4] To view the state-specific surveys, go to http://www.aarp.org/money/scams-fraud/info-04-2010/finprotect_states.html.

rulemaking that, if properly implemented, would significantly improve protections for investors while preserving different business models and methods of compensation.

The main rationale for adopting a uniform fiduciary standard is not simply to reduce or eliminate investor confusion, but rather to reduce or eliminate the real harm that investors suffer as a result of costly and less appropriate advice delivered under a suitability standard.

SEC action to close the regulatory gap with respect to the obligations of broker-dealers and their representatives offering personalized investment advice is long overdue. Armed with results of the study of this issue (the so-called Section 913 Study) mandated under the Dodd-Frank Act, the Commission has a solid basis of evidence for moving forward to rulemaking in this area. It is critically important that SEC rulemaking be consistent with the principle clearly stated in Section 913 of the Dodd-Frank Act that any new standard for broker-dealers must require them to act in the best interests of the customer and that it must be no weaker than the existing standard under the Advisers Act.

As such, AARP offers these comments on the assumptions contained in the RFI:

The fiduciary standard must be a true fiduciary duty. The Commission must include as a central component of its fiduciary standard a broad, principles-based requirement that those providing personalized investment advice to retail customers act in the best interest of the customer without regard to their own financial interest. It is not enough to simply disclose conflicts of interest. The Commission must require that brokers, like advisers, have a reasonable basis for believing that their recommendations are in the best interest of their customer and are prepared to demonstrate the basis on which they reached that conclusion.

"Personalized investment advice" should be broadly defined. Section 913 of Dodd-Frank frames the SEC's authority to impose a fiduciary standard on brokers in terms of "personalized investment advice." Defining this term is key in determining when the fiduciary duty will apply to brokers and, as a result, whether it will afford meaningful new protections for investors. The SEC should clearly establish that it will interpret the term "personalized investment advice" in a manner that is consistent with its long history and usage in the Advisers Act. As such, the SEC must broadly define the term by making clear that advice will be deemed personalized if it is personalized in substance and reality. The RFI assumption that personalized advice would include recommendations, as that term is interpreted under existing broker-dealer regulation, plus any other actions or communications that would be considered investment advice under the Advisers Act generally satisfies our concerns.

Exception for a continuing duty of care should be limited. Section 913(g) of the Dodd-Frank Act states that a uniform fiduciary standard will not always require a broker-dealer or its representative to have a continuing fiduciary duty to a customer after providing them with investment advice. While that section of Dodd-Frank is concerning, we believe the RFI generally suggests a reasonable approach to this issue. Importantly, the RFI acknowledges that the "totality of the circumstances of the relationship and course of dealing between the customer and the firm," and not contract language alone, would determine the scope and nature of the duty. The RFI further suggests that marketing documents and "reasonable customer expectations" also are factors that would determine whether an on-going duty exists. When drafting rules, the Commission should make it abundantly clear that brokers cannot "contract away" an on-going duty of care when their marketing materials and other representations to clients are designed to create a reasonable expectation of on-going account management. The reasonable expectation of the customer, based on the totality of the circumstances, should be the determining factors as to whether there is an on-going obligation to monitor and adjust the account, and thus an ongoing duty of care.

Commission-based compensation and sales of proprietary products should be conditioned on protective measures. Section 913 of Dodd-Frank provides that the receipt of commission-based compensation or other standard forms of compensation for the sale of securities, and the sale of proprietary products, shall not, "in and of itself," be considered a violation of the fiduciary standard. As such, the Commission should include as part of a fiduciary rule a requirement that brokers and advisers have policies and procedures in place to ensure that conflicts are identified, appropriately managed, and that they do not result in advice that subverts the best interests of the customer.

At the same time, Section 913 directs the Commission to "examine and, where appropriate, promulgate rules prohibiting or restricting certain sale practices, conflicts of interest, and compensation schemes for brokers, dealers and investment advisers that the Commission deems contrary to the public interest and the protection of investors." This language in Section 913 is a recognition that in many instances, disclosure of conflicts of interest will not provide sufficient protection for investors and that some practices simply must be prohibited.

Disclosure and consent alone do not meet the fiduciary test. The various assumptions of the RFI suggest that the Commission does not intend to require broker-dealers to eliminate most conflicts of interest (with the exception of sales contests), but rather that those conflicts will have to be disclosed. AARP wants to clearly emphasize disclosure and consent alone are not consistent with a fiduciary standard. The Commission's own financial literacy study casts doubt on the likely effectiveness of conflict disclosure alone in protecting investors from recommendations that fail to put their interests first.

Development of a uniform pre-engagement disclosure document for brokers and advisers. While we disagree that disclosure alone is sufficient when it comes to minimizing conflicts of interest, we do think investors will benefit from the development of a uniform pre-engagement disclosure document for brokers and advisers. The Commission generally has done a good job of identifying the key issues that should be addressed in such a document. We encourage the Commission to adopt a format for disclosures by brokers and investment advisers that are uninform to the greatest extent possible given the differences in their basic business models. The goal should be to promote easy comparisons of different types of financial professionals. The disclosures should be brief and clear. Design experts should be engaged to develop and test the documents for effectiveness in conveying key information and promoting investor understanding.

Conclusion

Over the years, brokers have been permitted to call themselves financial advisers and offer extensive investment advisory services without having to meet the best interest standard included as part of the fiduciary duty that applies to all other investment advisers. As a result, many investors erroneously believe they are dealing with a trusted adviser when, in fact, they are dealing with a salesperson – a salesperson who is free to put his or her own financial interests ahead of the interests of the investor. Investors who place their trust in these salespersons can end up paying excessively high costs for higher risk or underperforming investments that only satisfy a suitability standard, but not a fiduciary duty. That is money most middle income investors can ill afford to waste.

AARP is pleased to see the Commission moving forward to implement a fiduciary standard for all financial professionals who provide personalized investment advice to retail investors. However, we are concerned that the RFI signals a far weaker approach to fiduciary rulemaking than what is needed to update the rules to reflect the realities of the marketplace today, and to provide investors with the protections they need and deserve as they save and invest for retirement. We urge the Commission to more closely follow its own Section 913 Study, which provides a clear roadmap to effective rulemaking.

We appreciate your consideration of our views. If you need more information or have questions, please feel free to contact Mary Wallace at (202) 434-3954 or mwallace@aarp.org.

Sincerely,

David Certner

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