TESTIMONY OF JOHN TAFT
CHAIRMAN, SECURITIES INDUSTRY
AND FINANCIAL MARKETS ASSOCIATION
AND
HEAD OF U.S. WEALTH MANAGEMENT
RBC WEALTH MANAGEMENT

BEFORE THE
U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON CAPITAL MARKETS
AND GOVERNMENT SPONSORED ENTERPRISES

HEARING ON: THE REGULATION AND OVERSIGHT OF
BROKER-DEALERS AND INVESTMENT ADVISERS

SEPTEMBER 13, 2011

Introduction

Chairman Garrett, Ranking Member Waters, and members of the Committee: My name is John Taft. I am the Chairman of the Securities Industry and Financial Markets Association ("**SIFMA**").[1] I am also the Head of U.S. Wealth Management, RBC Wealth Management, which has over 2,000 financial advisers operating in 200 locations in 42 states who serve over 800,000 client accounts. Thank you for the opportunity to testify at this important hearing.

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

Today I will present SIFMA's views:

(i) in support of establishing a uniform fiduciary standard for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers; [2] and

(ii) in support of ensuring uniform examination, oversight and enforcement of the uniform standard.

We believe that a uniform fiduciary standard for brokers and advisers is consistent with current best practices in our industry, and we hope that it will ultimately result in a heightened, industry-wide focus on serving the best interest of our retail customers.

Our support for this objective, however, is predicated upon our collective willingness to achieve it in a manner that protects investors, preserves investor choice, is cost-effective and business model neutral, and avoids regulatory duplication or conflict. We will succeed only if we perform the necessary cost-benefit analysis that supports and compels us to pursue fiduciary rulemaking consistent with these requirements. Further, it is our strong view that the Department of Labor's ("**DOL's**") proposed, expansive, new definition of fiduciary under the Employee Retirement Income Security Act ("**ERISA**"), absent any mandate from Congress, is, among other things, in direct conflict with Section 913 ("**Section 913**") of the Dodd-Frank Wall

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[2] SIFMA's position is limited to retail customers, *i.e.*, natural persons who use investment advice for personal, family or household purposes.

Street Reform and Consumer Protection Act ("**Dodd-Frank**"). Absent a re-proposal and subsequent coordination with any Securities and Exchange Commission ("**SEC**") fiduciary proposal, the DOL proposal will directly conflict with the goals of protecting investors and preserving investor choice while avoiding undue increase in costs to investors. In short, while the SEC should methodically and deliberately approach its authority to write a new uniform fiduciary standard of care, the DOL's approach to date has been to charge ahead absent sufficient study and analysis.

Since 2009, SIFMA has publicly expressed support for establishing a uniform fiduciary standard, including in our testimony before Congress on two separate occasions during 2009.[3] Since the enactment of Dodd-Frank, SIFMA has remained equally engaged with the SEC, the Financial Industry Regulatory Authority ("**FINRA**"), and Congress on all aspects of the SEC's authorization to implement Section 913 of Dodd-Frank. SIFMA has created a robust public record on the fiduciary topic that includes several regulatory comment letters, economic and market research, and our proposed framework for rulemaking under Section 913.[4] SIFMA has

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[3] *See, e.g.*, *Hearing Before the H. Comm. on Financial Servs.*, 111th Cong. 2-3 (2009) (statement of John Taft, Head of U.S. Wealth Management, RBC Wealth Management on behalf of SIFMA), available at http://financialservices.house.gov/media/file/hearings/111/taft_testimony.pdf; *Hearing Before the H. Comm. on Financial Servs.*, 111th Cong. 21 (2009) (statement of Randolph C. Snook, Executive Vice President, SIFMA), available at http://financialservices.house.gov/media/file/hearings/111/snook.pdf.

[4] *See, e.g.*, SIFMA comment letter to SEC re: Section 913 Study (Aug. 30, 2010), available at http://www.sifma.org/issues/item.aspx?id=22263 ("**SIFMA Section 913 Comment Letter**");

also engaged in numerous meetings and discussions with SEC and FINRA senior staff and leadership on the fiduciary topic.

A. The critical need to pursue a carefully considered and balanced approach.

As we are all keenly aware, Dodd-Frank has placed both the securities industry and securities regulators in unchartered waters, facing an unprecedented number of rulemakings over the coming years. The stakes are high. Poorly crafted regulations could result in unintended consequences that harm economic growth, stifle job creation, and result in capital markets "winners and losers." It is imperative that we get these regulations right.

The fiduciary issue is among our industry's greatest concern in this regard. During the debate on Dodd-Frank, SIFMA consistently asserted that Congress should authorize the SEC to write the new uniform fiduciary standard as opposed to prescriptively legislating it through statute, particularly given the issue's complexity and the varying historical and legal precedents. That said, this is a complex undertaking that must be well thought-out and reflective of both the statute and

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SIFMA economic study prepared by Oliver Wyman re: Section 913 (Oct. 27, 2010), available at http://www.sifma.org/issues/item.aspx?id=21999 **("Oliver Wyman Study")**; SIFMA letter to SEC re: Oliver Wyman Study (Nov. 17, 2010), available at http://www.sifma.org/issues/item.aspx?id=22336 **("Oliver Wyman Study Supplemental Letter")**; SIFMA comment letter on FINRA RN 10-54 (Dec. 3, 2010), available at http://www.sifma.org/issues/item.aspx?id=22482; SIFMA comment letter to DOL re: fiduciary rule proposal (Feb. 3, 2011), available at http://www.sifma.org/issues/item.aspx?id=23239; SIFMA letter to SEC re: framework for rulemaking under Section 913 (Jul. 14, 2011), available at http://www.sifma.org/issues/item.aspx?id=8589934675 ("**SIFMA Framework Letter**").

Congressional intent. We believe strongly that Congress explicitly intended for the SEC to craft a uniform fiduciary standard that not only *protects investors*, but also *preserves investor choice and access* to cost-effective financial products and services and is adaptable to the substantially different operating models of broker-dealers and investment advisers. Congress expressly provided the SEC with the statutory tools necessary to achieve these inextricably linked goals.

Specifically, Section 913 of Dodd-Frank requires that the uniform fiduciary standard be "no less stringent than" the general fiduciary duty implied under the Advisers Act, thus granting the SEC the latitude and ability to establish a separate, unique uniform fiduciary standard that is appropriately tailored to the business models of broker-dealers. The plain language of Section 913, together with the legislative history of Dodd-Frank, makes clear that the "no less stringent" language does *not* require the SEC to impose the Advisers Act standard on broker-dealers.[5] As Congressman Barney Frank stated in a recent letter to SEC Chairman Mary Schapiro,

> If Congress intended the SEC to simply copy the [Advisers] Act and apply it to broker-dealers, it would have simply repealed the broker-dealer exemption – an approach Congress considered but rejected. The new standard contemplated by Congress is intended to recognize and appropriately adapt to the differences between broker-dealers and registered investment advisers.[6]

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[5] Letter from Congressman Barney Frank to Chairman Mary Schapiro (May 31, 2011) ("'no less stringent' … was not intended to encourage the SEC to impose the … Advisers Act… standard on broker-dealers…").

[6] *Id.*

A mere overlay of the Investment Advisers Act of 1940 ("**Advisers Act**") onto broker-dealers would negatively affect client choice, product access, and affordability of customer services and, thus, by definition, would *not* be in the best interest of retail customers. Imposing the Advisers Act standard would also be problematic for broker-dealers from a commercial, legal, compliance, and supervisory perspective, thereby undercutting the SEC's stated intent to take a "business model neutral" approach. The Dodd-Frank Act authorizes, the SEC's Section 913 Study[7] supports, and principles of investor protection warrant taking a fresh approach by establishing, through SEC rulemaking under Section 913 of Dodd-Frank, a uniform fiduciary standard for broker-dealers and investment advisers that is separate from that implied under Section 206 of the Advisers Act.

Investment advisers are generally engaged in the business of providing advice about securities for a fee or managing assets on a discretionary basis. Broker-dealers engage in the former activity on occasion (advice about securities), but also provide a broad range of other products and services. Broker-dealers provide, for example, initial and follow-on public offerings and other underwritten offerings, and market fixed-income and affiliated products, all of which contribute to the capital raising, liquidity, best execution, and portfolio balancing functions of our securities markets.

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[7] *See* Commission Study on Investment Advisers and Broker-Dealers, as required by Section 913 (Jan. 2011), available at http://www.sec.gov/news/studies/2011/913studyfinal.pdf ("**SEC Section 913 Study**").

Yet these services, which are beneficial to both individual investors and the economy in general, often carry inherent (though generally accepted and well-managed) conflicts of interest.

The general fiduciary duty implied under the Advisers Act, as developed through case law, regulatory guidance, and other legal precedent, however, provides incompatible and insufficient guidance for broker-dealers on how to manage, disclose, or, where necessary, obtain consents to these conflicts. Again, Congress explicitly recognized this in the statute when it limited the reference of the Advisers Act to sections 206(1) and (2), thereby preserving the ability of brokers to engage in principal transactions on behalf their clients and receive commissions under any new uniform fiduciary standard.

These issues are important because failure of any new uniform standard of care to recognize and adjust for them, while possibly increasing investor protection, will certainly limit investor choice at a far greater cost than we believe was intended by Congress. SIFMA commissioned an economic study by Oliver Wyman in October 2010 that clearly demonstrates this point.[8] This study, which we submitted to the SEC, shows that the vast majority of retail investors prefer commission-based accounts at a lower cost factor. If the new standard is not appropriately crafted to reflect broker-

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[8] *See* Oliver Wyman Study, and Oliver Wyman Study Supplemental Letter. Copies of both documents are being filed together with SIFMA's written testimony.

dealers' business models and investors' needs, it could force the majority of these investors into fee-based managed accounts at a higher cost factor. We do not believe this is what Congress intended or, frankly, what the SEC proposed in their Section 913 Study, but it should be a concern.

In light of these issues, we believe that appropriately robust and rigorous cost-benefit analyses are essential to inform and shape any SEC rulemaking, especially for the type of "sea change" reform envisioned by Section 913. We support the cost-benefit and other empirical analyses that we understand the SEC is currently undertaking on Section 913, as well as any other analyses that may help inform the optimal approach for implementing a uniform fiduciary standard. We are also willing, as an industry, to facilitate such studies or analyses by providing appropriate data, feedback, or other information that would result in the most accurate and meaningful findings and conclusions. In sum, SIFMA stands ready and willing to further engage with the SEC and others to help perform the due diligence and lay the foundation necessary to support fiduciary rulemaking.

B. Establishing a uniform fiduciary duty for broker-dealers and investment advisers.

Consistent with our intent to move forward on the fiduciary front, on July 14, 2011, SIFMA filed a detailed letter with the SEC that offers a framework and principles for rulemaking under Section 913 of Dodd-Frank.[9] As we explain in our Framework Letter, the guiding principle that underpins the uniform fiduciary standard is to act in the best interest of the customer. The rulemaking to articulate the standard would address the following five key components:

1. Enunciate the core principles of the uniform fiduciary standard;
2. Articulate the scope of obligations under the uniform fiduciary standard;
3. Define "personalized investment advice;"
4. Provide clear guidance regarding disclosure that would satisfy the uniform fiduciary standard; and
5. Preserve principal transactions and proprietary products.

The standard, and its key components, would be articulated through comprehensive SEC rulemaking as a uniform standard of conduct that is "no less stringent than" the general fiduciary duty implied under the Advisers Act.

The SIFMA Framework Letter explains in detail why a wholesale extension to broker-dealers of the case law, regulatory guidance, and other legal precedent under the Advisers Act would result in a host of adverse consequences for retail customers. The SIFMA Framework Letter not only explains what won't work and why, but also offers a simple, straightforward, and integrated solution. Under our framework, the general

[9] *See* SIFMA Framework Letter. A copy of the SIFMA Framework Letter is also being filed together with SIFMA's written testimony.

fiduciary duty implied under Section 206 of the Advisers Act, which derives from the traditional, generally understood, and accepted common law,[10] would be newly articulated through SEC rulemaking under the Advisers Act, and through parallel, consistent, and equally stringent rulemaking under the Securities Exchange Act of 1934 ("**Exchange Act**"), as contemplated by Section 913.[11]

The fiduciary standard of conduct would apply equally to broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers. The SEC would also issue rules and regulatory guidance to provide the structure and detail necessary to enable broker-dealers and investment advisers to apply the uniform fiduciary standard of conduct to their distinct operational models.[12]

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[10] *See SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 195 (1963) ("…Congress codified the common law 'remedially' [in the Advisers Act] … to prevent[] fraudulent securities transactions by fiduciaries"). *See also* Restatement of Agency (Third) (agency is the fiduciary relationship that arises when one person (the principal) manifests assent to another person (the agent) that the agent shall act on the principal's behalf and subject to the principal's control, and the agent manifests assent or otherwise consents so to act). It is critical to note, however, that existing case law regarding the fiduciary duty of investment advisers was developed in the context of a business model which is inapplicable to broker-dealers, and applying such case law in the broker-dealer context could have legal and regulatory consequences that would undermine the broker-dealer business model, with no corresponding benefit to retail customers.

[11] Thus, the uniform fiduciary standard of conduct would conclusively satisfy Dodd-Frank's requirement that the standard be "no less stringent than" the standard implied under Section 206 of the Advisers Act.

[12] Our proposed approach is consistent with that historically followed in agency and trust contexts. The precise contours of the fiduciary obligation are molded to particular fiduciary fields or contexts. Thereafter, common sets of facts are addressed through implementing rules that apply the duties of loyalty and care to those circumstances. "The ... rules simplify application of the fiduciary obligation to cases that fall within their terms, reducing decision

The uniform fiduciary standard of conduct would begin with the core principle mandated by Dodd-Frank that all broker-dealers and investment advisers, when providing personalized investment advice about securities to retail customers, shall "act in the best interest of the customer …."[13] Thus, the principle of "acting in the best interest of the customer" would serve as the bedrock cornerstone of the SEC rules promulgated under the Advisers Act and the Exchange Act.

Existing case law, guidance, and other legal precedent developed under the Advisers Act would continue to apply to investment advisers. Thus, SIFMA does not propose to modify the current Advisers Act standard applicable to the delivery of investment advice to the institutional clients of investment advisers, or the existing legal precedent developed under Section 206 of the Advisers Act. While there would be many parallels, Section 206 legal precedent would *not* apply to broker-dealers, because: (i) broker-dealers provide a different range of products and services and operate under an operational model distinct from that of investment advisers;[14] and (ii) the uniform standard would be separate and distinct from the Advisers Act precedent.

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costs." *See* Robert H. Sitkoff, *The Economic Structure of Fiduciary Law*, 91 B.U. Law Rev. 1039, 1044-45 (2011).

[13] Section 913(g) of Dodd-Frank.

[14] While broker-dealers and investment advisers may at times provide similar services, there are many substantive differences in the products, services, conflicts, and traditional compensation practices between the two well-established and highly regulated business models.

Advisers Act precedent, therefore, would not apply to broker-dealers under a new, but no less stringent, uniform fiduciary standard of conduct established under the Advisers Act and the Exchange Act.

We believe that our framework for implementing a uniform fiduciary standard is the optimal one. It would protect investors, preserve their choice of – and access to – financial products and services, and would reflect the substantially different business models of broker-dealers and investment advisers. Thus, we continue to urge the SEC to newly articulate a uniform fiduciary standard of conduct, rather than attempting to apply Advisers Act legal precedent to the broker-dealer business model with resulting significant negative effects for investor protection and choice.

C. The problematic DOL rule proposal on who is a fiduciary.

Another area of deep concern to SIFMA is DOL's proposed amendments to its regulations that redefine – and significantly expand – who is considered a fiduciary for retirement plans and their participants under ERISA. The amendments would also affect individual retirement accounts ("**IRAs**") owned by millions of retail investors. The DOL proposal would effectively upend a long-established and well-understood definition that retirement plans and plan service providers have relied upon for over thirty-five years.

The consequences of a broker-dealer being deemed a fiduciary under ERISA include potential prohibitions on engaging in principal transactions, as well as difficulty receiving fees or commissions. In addition, the expanded definition of fiduciary may cause broker-dealers to limit the advice, recommendations and information they provide to investors regarding their retirement accounts. These consequences would directly translate into a dramatic change in the manner in which products and services are provided to plans, plan participants, and IRA account holders.

The DOL proposal also conflicts with Section 913 of Dodd-Frank. We understand that the staffs of the DOL and SEC intend to work to harmonize the DOL rulemaking with the standard under Section 913. But neither the DOL nor the SEC has articulated how it envisions the two standards would work together, and the DOL continues to move forward without waiting to see what the SEC will propose. Absent regulatory clarity and coordination, brokers and advisers could be subject to multiple and conflicting regimes when dealing with their retail customers, and again, retail customers could suffer reduced choice and higher costs.

The DOL has not yet undertaken a comprehensive cost-benefit analysis in connection with its proposal, and the cost estimates the DOL has made focus on costs to service providers as a result of the amendments – not the costs to investors. As we have stated in our previous comments to the DOL and Congress,[15] we believe that the

[15] *See, e.g.*, Testimony of Kenneth E. Bentsen, EVP, Public Policy and Advocacy, SIFMA, before DOL on the definition of fiduciary (Mar. 1, 2011), available at http://www.sifma.org/issues/item.aspx?id=23700; SIFMA supplemental comment letter to

DOL has greatly underestimated the costs to service providers and, more importantly, has not sufficiently examined the costs of its proposal on retirement plans and IRAs or the effects of the proposal on retirement savings. We believe that this insufficient analysis has led to a proposal that ultimately will harm investors by raising the costs of saving, which would seriously undercut the ability of millions of investors to efficiently save for retirement.

As noted previously, we have submitted several comment letters to this effect to the DOL, and testified before both DOL and Congress on this matter.[16] Based on our extensive discourse with DOL, we strongly believe that the DOL proposal should be withdrawn and re-proposed in a manner that, at a minimum, avoids prospective conflicts with Section 913. Otherwise, we expect that the DOL proposal will likely have a significant negative impact on millions of accountholders.

D. A uniform fiduciary standard necessarily calls for uniform examination, enforcement, and oversight.

To be sure, the challenges are many to implementing smart fiduciary regulations. But we should make every effort to meet those challenges for the benefit

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DOL on proposed definition of fiduciary (Apr. 12, 2011), available at http://www.sifma.org/issues/item.aspx?id=24650.

[16] *See, e.g., Id.*; SIFMA comment letter to DOL on proposed definition of fiduciary (Feb. 3, 2011), available at http://www.sifma.org/issues/item.aspx?id=23239; Testimony of Kenneth E. Bentsen, EVP, Public Policy and Advocacy, SIFMA, before a U.S. House Committee on "Redefining Fiduciary" (Jul. 26, 2011), available at http://www.sifma.org/issues/item.aspx?id=8589934878.

of our clients and the integrity of our industry.

So, let us assume that we succeed in:

(i) conducting reasonable cost-benefit analysis to set the foundation for fiduciary rulemaking;

(ii) establishing a uniform fiduciary standard that is business model neutral and protects investors without depriving them of choice of products and services at low cost;

(iii) avoiding an Advisers Act “overlay” on the broker-dealer business model; and

(iv) removing the conflicts between the DOL proposal and Section 913.

Where do we go from there? We think that is one of the central questions raised by Section 914 of Dodd-Frank, which requires the SEC to “review and analyze the need for enhanced examination and enforcement resources for investment advisers.”

The SEC’s Division of Investment Management (“**IM**”) completed their Section 914 Study in January 2011.[17] In the study, IM recommends that Congress consider three approaches: 1) authorize the SEC to impose user fees on investment advisers to fund their examination by the SEC; 2) authorize FINRA to examine dual-

[17] SEC, Division of Investment Management, Study on Enhancing Investment Adviser Examinations, as required by Section 914 (Jan. 2011), available at http://sec.gov/news/studies/2011/914studyfinal.pdf (“**SEC Section 914 Study**”). The Commission has expressed no view regarding the analysis, findings or conclusions in the study.

registrants for compliance with the Advisers Act; and 3) authorize a self-regulatory organization ("**SRO**") to examine investment advisers.

With respect to the first option (SEC examination), we believe that SEC budgetary and resource constraints will continue into the foreseeable future, resulting in a continuing decline in the number and frequency of investment adviser examinations by the SEC. Thus, we do not believe that the SEC is a viable or practical candidate to fill the "examination enhancer" role contemplated by Section 914. With respect to the second option (FINRA examination of dual-registrants), we believe such an approach would be inconsistent with a uniform, harmonized approach to examination and oversight, because it would not provide any enhanced oversight or examination of retail, stand-alone advisory firms. Moreover, this approach could represent a risk to retail investors, as it might encourage even more brokers to flee from the highly-regulated broker-dealer environment – which is subject to rigorous FINRA and SEC oversight – in favor of a once-a-decade check-up by an overworked and underfunded SEC with no FINRA scrutiny whatsoever.

We believe that the third option, the SRO option, is the most practical and prudent approach. As we explain in greater detail in our comment letter to the SEC on Section 914,[18] oversight of broker-dealers is bolstered by the examination and

[18] SIFMA comment letter to SEC re: Section 914 (Jan. 12, 2011), available at http://www.sifma.org/issues/item.aspx?id=22972.

enforcement activities of SROs like FINRA, particularly with respect to conduct directed toward retail customers. Consistent with the establishment of a uniform fiduciary standard, we ought to uniformly hold broker-dealers and investment advisers to that standard by ensuring uniform examination, oversight, and enforcement of the standard. In the case of broker-dealers and independent investment advisers who provide personalized investment advice to retail customers, we believe comparable examination, oversight, and enforcement is most practically and readily achievable through use of an SRO.

At the same time, and as we noted in our comment letter, our SRO recommendation is limited to investment advisers that focus on providing personalized investment advice to retail customers, which present different concerns than do institutional advisers. Thus, we would not support legislation that extends SRO oversight to institutional advisers. Finally, any SRO examination program should be carefully tailored to investment adviser practices and to avoid regulatory duplication or additional oversight costs where not necessary for improving investor protection.

Conclusion

Thank you, Chairman Garrett, Ranking Member Waters, and members of the Subcommittee, for allowing me to present SIFMA's views. SIFMA and its members remain committed to being constructive participants in the process of establishing a uniform fiduciary standard for broker-dealers and investment advisers, and ensuring uniform examination, oversight, and enforcement of that standard. We stand ready to provide any further assistance requested by this Subcommittee on these critically important topics.

Encl 1

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Invested in America

Financial Services

October 2010

Standard of Care Harmonization
Impact Assessment for SEC

NYC-FMJ001-001

Contents

Section 1

Executive summary

Summary findings (1)

- Oliver Wyman collected data from a broad selection of retail brokerage firms to assess the impact of significant changes to the existing standard of care for broker-dealers and investment advisors
  – A total of 17 firms provided data
  – These institutions serve 38.2MM households and manage $6.8TN in client assets
  – The survey captures approximately 33% of households and 25% of retail financial assets in the US
- The primary issue at stake in the SEC ‘standard of care’ study is how to better protect the investor while preserving choice of relationship, product access, and affordability of advisory services
- The key insight from the survey is that broker-dealers play a critical role in the financial services industry that cannot be easily replicated with alternative services models
- Wholesale adoption of the Investment Advisers Act of 1940 for all brokerage activity is likely to have a negative impact on consumers (particularly smaller investors) across each of the following dimensions
  – Choice
  – Product access
  – Affordability of advisory services

Continued…

Summary findings (2)

Potential impact of rulemaking on retail investors

Choice	▪ Reduced access to the preferred 'investment and advisory model' for retail investors – 95% of households hold commission-based brokerage accounts today – The fee-based advisory platform is far less popular (only 5% of households) – The 'preference' for brokerage accounts is evident across all wealth segments but strongest for smaller investors with less than $250K in assets
Product Access	▪ Reduced access to products distributed primarily through broker-dealers – Municipal and corporate bonds represent ~15% of assets held by retail investors – These products (among others) are generally offered on a 'principal basis' – Restricting principal or proprietary offerings will limit investor access to these products and possibly limit financing options for municipalities or corporates at current pricing
Affordability of Advisory Service	▪ Reduced access to the most affordable investment options – Fee-based services are 23-37 bps more expensive than brokerage[1] – For an investor with $200K in assets, this translates to $460 in additional fees – The cost of shifting to fee-based pricing alone would reduce expected returns by more than $20K over a 20 year horizon (assuming 5% annual returns) ▪ And the indirect costs of additional compliance, disclosure, and surveillance may have an even greater impact on consumers → we estimate that 12-17MM small investors 'at the margin' could lose access to current levels of advisory service if even 2 additional hours of coverage and support is required per client

1. Cost expressed as a percentage of assets under management in basis points (1bp = 0.01%)

Section 2

Methodology and source data

Oliver Wyman collected data from 17 SIFMA member firms to support the impact assessment

Purpose of study

- The impact assessment that follows was designed in response to the SEC request for comment on the upcoming study of the standard of care obligations for broker-dealers and investment advisers
- Oliver Wyman gathered data from 17 SIFMA member firms to provide relevant market data for the SEC study
- The study is intended to help
  - Identify the investor segments most likely to be affected by changes to the standard of care
  - Understand the cost to the consumer (choice, product access, transaction costs) of potential changes
  - Understand the one-time and ongoing costs of compliance for advisory and brokerage firms
  - Estimate the broader market / economic impact of any changes, particularly for capital formation

Note on survey methodology

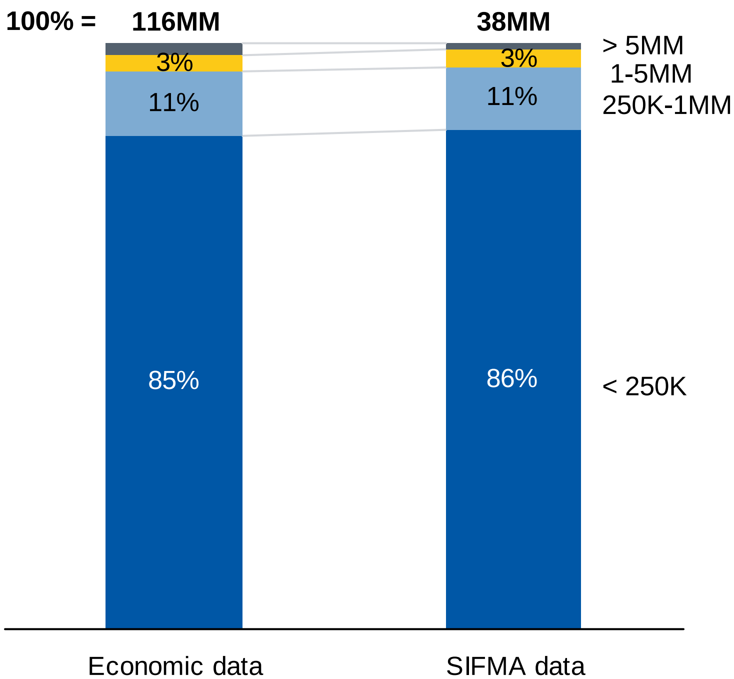
- 17 member firms participated, representing $6.8TN in assets (approximately 27% of total U.S. household financial assets) across 38.2MM households
- To obtain a fairly representative sample of the industry, data on asset management accounts, investor profiles, and cost structure was gathered from a diverse set of brokerage firms

Note on confidentiality

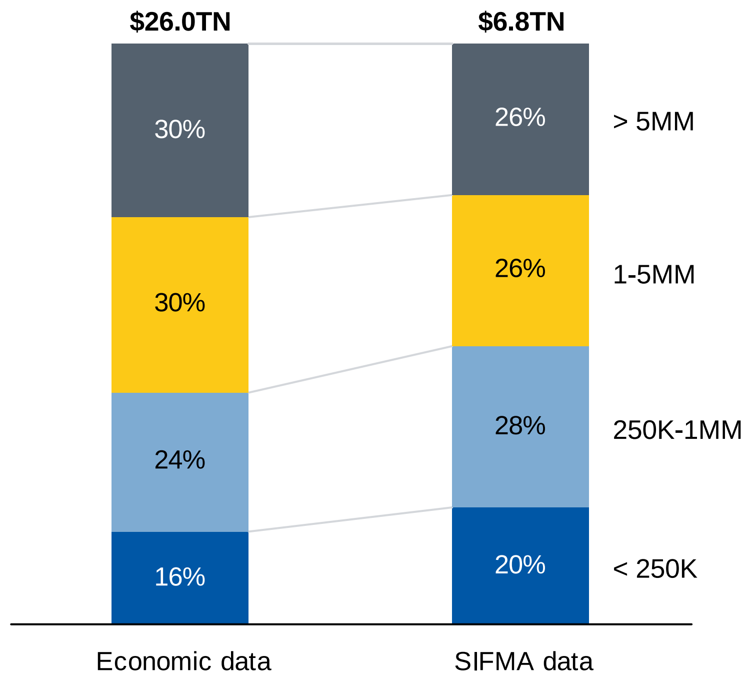
- Due to the highly sensitive nature of firm-specific information, all data is presented in aggregated form

The survey proved to be highly representative of the investor population as a whole, capturing 33% of households and 27% of financial assets

Investors by wealth segment[1]
Number of U.S. households, 2009



Assets by wealth segment
Investable assets, 2009



Note: Economic data includes all investable assets whereas SIFMA data refers to managed assets, SIFMA data skews toward investors with <$1MM in assets

1. Wealth segments based on client assets under management

Source: SIFMA member data, 2007 Federal Reserve Survey of Consumer Finances, Oliver Wyman analysis

Section 3

Background and context

Regulators have wide discretion in establishing a uniform ‘standard of care’ for the IABD industry

- Regulators have a range of options in establishing a uniform ‘standard of care’ for broker-dealers and investment advisers in the United States
  - Limited changes to current model
  - A ‘standard of care’ with disclosure / consent to conflicts that preserves commission-based brokerage
  - Wholesale adoption of the Advisers Act of 1940 for all broker-dealers and investment advisers
- A major shift in the ‘standard of care’ will impact individual investors in several ways
  - Choice of advisory model
  - Access to investment products
  - Cost of investment and advisory services
- Beyond these direct costs to the consumer, we also anticipate broader economic costs to the industry as a whole
  - Broker-dealers and investment advisory firms will all face one-time and ongoing costs to comply with new fiduciary, disclosure, and surveillance requirements → these may be passed on to investors
  - Potential limitations on product accessibility for retail investors will place constraints on capital formation and issuers’ ability to finance at attractive rates

Our analysis will focus on the relative impact of two possible scenarios for harmonization of the standard of care

Activity	Rule making scenarios		
	STATUS QUO WITH GREATER DISCLOSURE *Harmonized standards that preserve existing practices but require greater disclosure*	**FIDUCIARY DUTY WITH CONSENT TO CONFLICTS** *Fiduciary standard for advisory activity that preserves commission-based brokerage model*	**ADOPTION OF ADVISERS ACT OF 1940** *Fiduciary standard for advisory activity with fees based on assets under management*
Investment planning	▪ Suitability for resultant securities transactions	▪ Best interest of the client with disclosure / consent to conflicts	▪ Best interest of the client
Asset allocation advice	▪ Suitability for resultant securities transactions	▪ Best interest of the client with disclosure / consent to conflicts	▪ Best interest of the client
Advice on client holdings	▪ Best interest of the client (advisory services) <u>or</u> suitability (brokerage services)	▪ Best interest of the client, at point of sale or ongoing depending on relationship	▪ Best interest of the client
Proprietary product sales	▪ Best interest of the client (advisory services) <u>or</u> suitability (brokerage services)	▪ Best interest of the client with disclosure / consent to conflicts	▪ Not available
Principal transactions	▪ Best interest of the client (advisory services) <u>or</u> suitability (brokerage services)	▪ Best interest of the client with disclosure / consent to conflicts	▪ Trade-by-trade prior consent required
IRA / retirement accounts	▪ Best interest of the client (advisory services) <u>or</u> suitability (brokerage services)	▪ Best interest of the client <u>or</u> solely in the interest of the client, depending on relationship	▪ Solely in the interest of the client

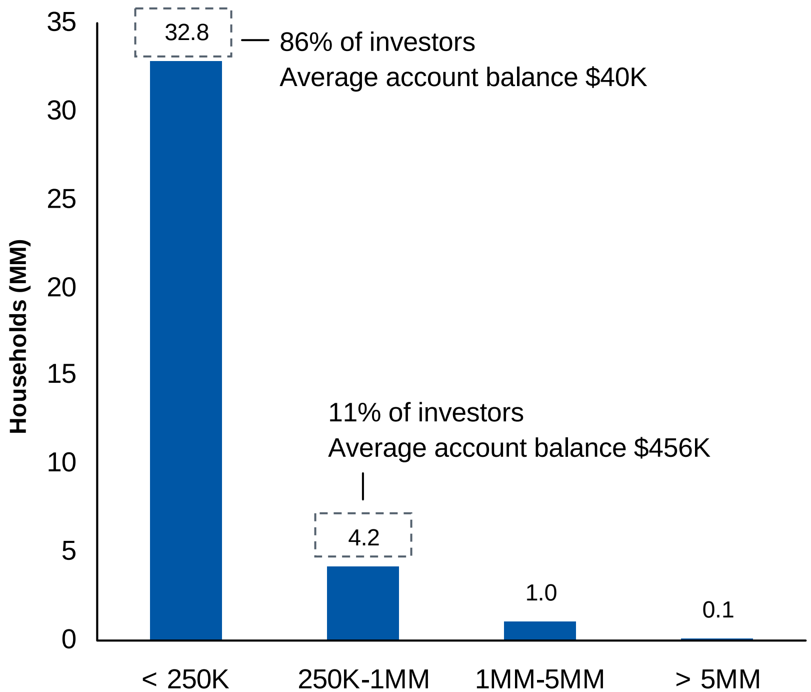
Baseline for impact analysis

Section 4

Impact on choice

The vast majority (97%) of the US investor population holds less than $1MM in assets with a broker-dealer or investment adviser

Investor landscape (survey population)
Number of investors by wealth segment[1], 2009



Client assets under management				
	$1.3TN	$1.9TN	$1.8TN	$1.8TN

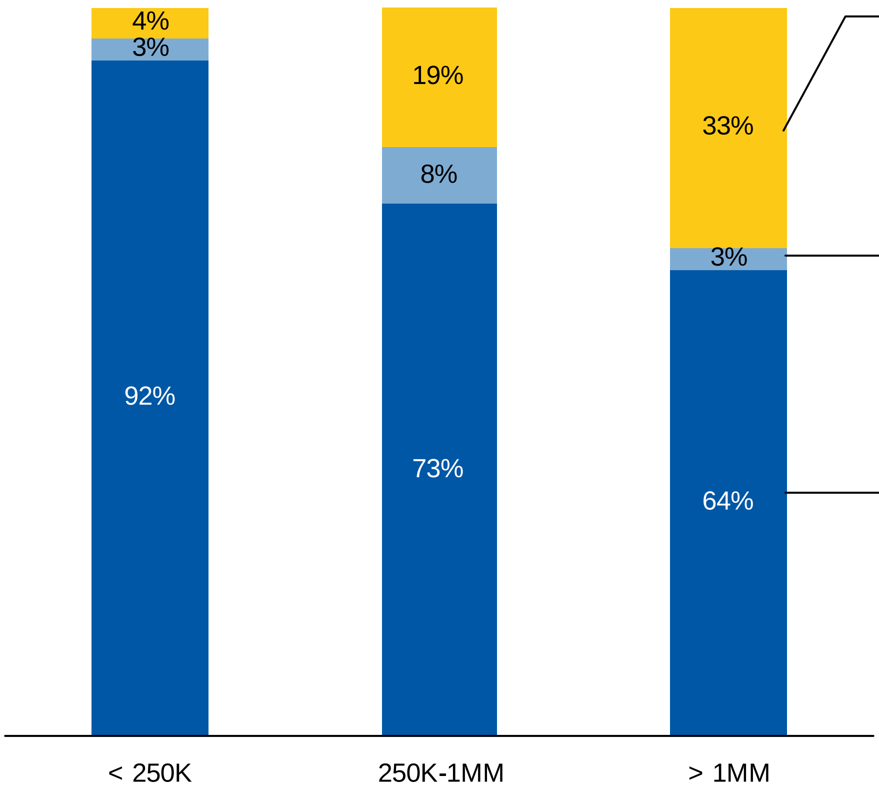
Key observations

- 97% of investors in the survey (37.0MM) hold less than $1MM in assets with broker-dealers or investment advisers
- Despite the heavy skew toward small clients, total assets are evenly distributed across the wealth spectrum ($1.3-1.9TN in all groups)
- Average account balance for investors in the lowest wealth segment is $40K → this is the segment most likely to be affected by a significant increase in costs

1. Wealth segments based on client assets under management
Source: SIFMA member data, 2007 Federal Reserve Survey of Consumer Finances, Oliver Wyman analysis

Across wealth segments, less than 5% of investors use fee-based accounts alone to serve their investment needs

Channel preference (survey population)
Number of households by relationship model, 2009



1 Mix of commission- and fee-based accounts

- As wealth increases, more investors use a hybrid model of fees and commissions-based management

2 Fee-based accounts

- Only 1.3MM investors (4% of total) hold AUM solely under fee-based management
- Fees-only management is the least common channel across all wealth segments

3 Commission-based accounts

- Over 30MM households hold assets solely in commission-based accounts; 27MM of these are from the lowest wealth segment
- Investors in the lowest wealth segment have a much stronger skew towards commissions-only management than any other wealth segment

Source: SIFMA member data, 2007 Federal Reserve Survey of Consumer Finances, Oliver Wyman analysis

The current model offers investors a wide range of advisory service, product access, and pricing options

Key Attributes	Account Types			
	Fee-Based	**Fees and Commissions**	**Commission-Based** *Advised*	**Commission-Based**[1] *Non-Advised*
Share of population	4%	7%	← 88% →	
Advisory needs	▪ Broad, portfolio-based financial planning and investment advice	▪ Broad, portfolio-based financial planning and investment advice plus product-specific advice	▪ Product-specific advice, access to principal products	▪ Uncertain
Investment activity	▪ Combination of active and passive, depending on client needs	▪ Active investment	▪ Combination of active and passive, depending on client choice	▪ Combination of active and passive, depending on client choice
Level of service	▪ Highest → ongoing advice and account surveillance	▪ Highest → ongoing advice and account surveillance	▪ Balanced → point in time advice on specific products	▪ Limited service
Typical holdings	▪ Investable assets only	▪ Investable assets ▪ Cash and equivalents ▪ Concentrated positions with special requirements	▪ Investable assets ▪ Cash and equivalents ▪ Concentrated positions with special requirements	▪ All investable assets ▪ Cash and equivalents
Cost	▪ Highest cost ▪ Range = 67-117 bps[2]	▪ Balanced cost ▪ Range = 43-99 bps[2]	▪ Balanced cost ▪ Range = 38-94 bps[2]	▪ Lowest cost, depending on trading activity
Common investors	▪ Affluent and HNW	▪ Affluent and HNW	▪ All investors	▪ Predominantly lower net worth investors

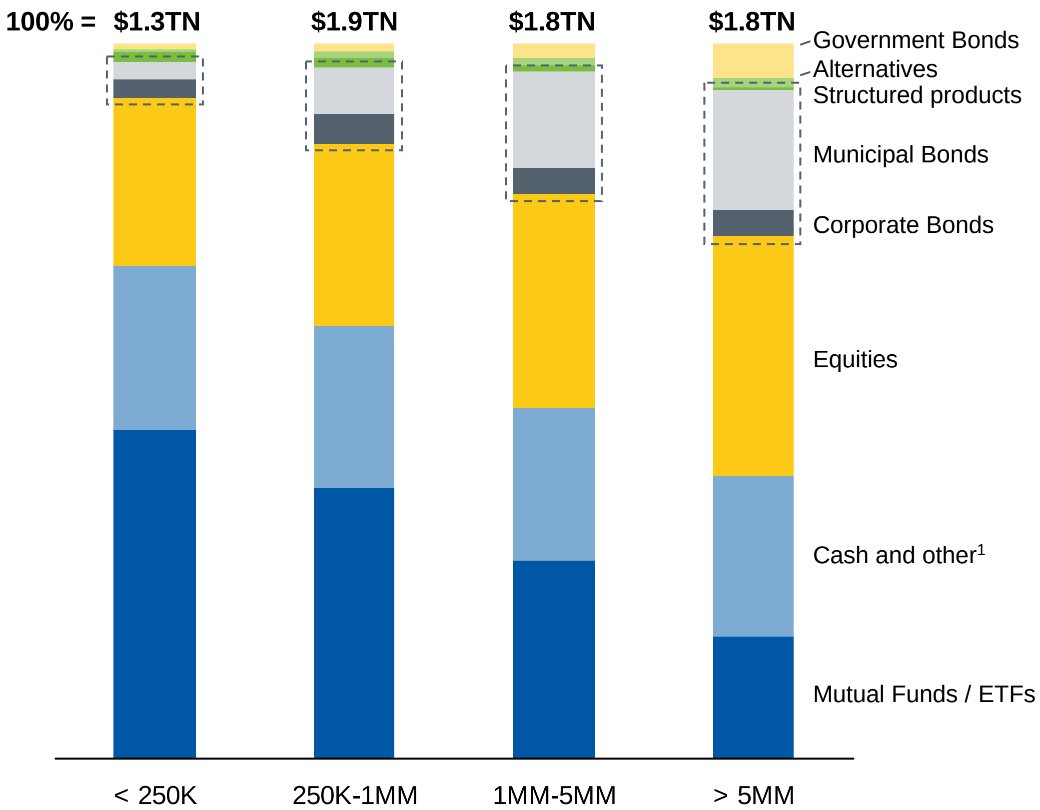
1. Non-advised accounts (e.g. self-directed online) were not targeted in this study but represent a significant subset of commission-based accounts
2. Range dependent on wealth segment (high end of the range reflects pricing for lowest wealth segment)

Section 5

Impact on product access

Direct holdings of individual securities (such as municipal bonds) represent an important element of investment strategy across all wealth segments

Asset allocation (survey population)
Allocation of assets (%) by wealth segment, 2009



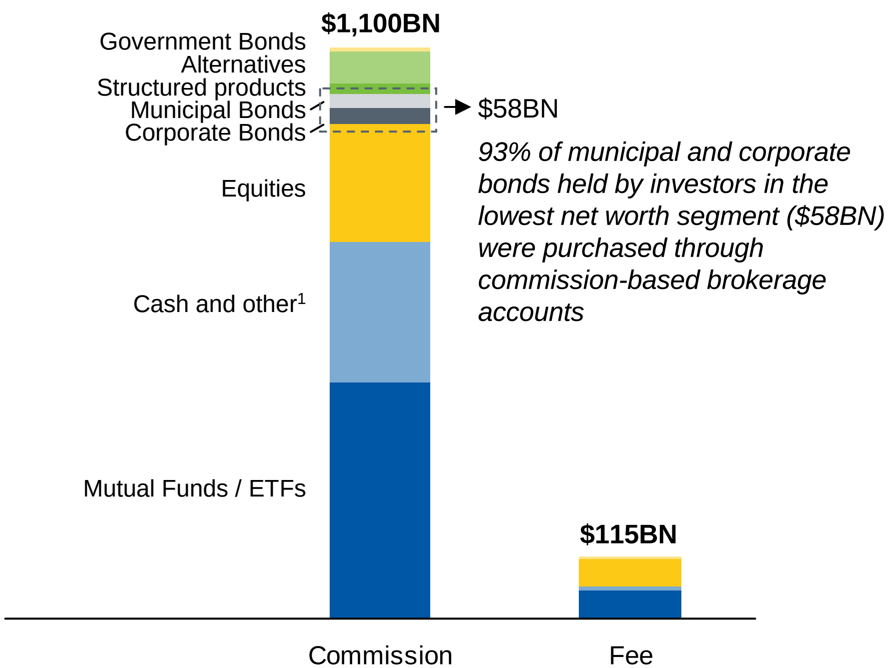
1. Includes cash, currencies, money market funds, etc
Source: SIFMA member data, Oliver Wyman analysis

Key observations

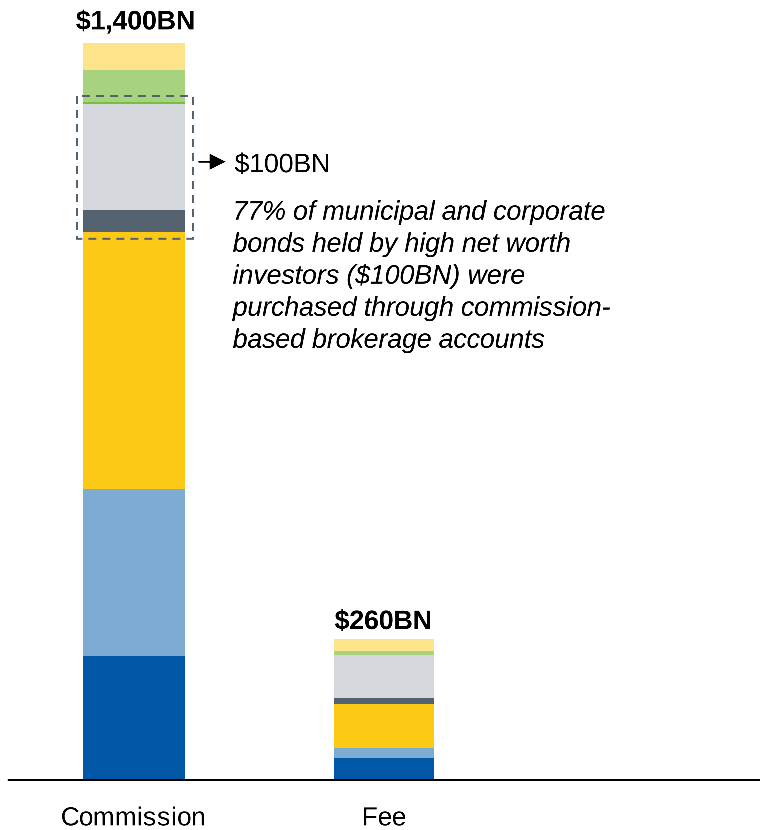
- Investors across all wealth segments have at least 30% of their portfolio in direct holdings of individual securities
- Municipal and corporate bonds offer tax and diversification benefits that investors may be unable to access via funds
- Across all investors, municipal and corporate bonds represent 13% of total wealth and 18% of invested assets (excluding cash)
- Allocations to municipal and corporate bonds range from 7% of investable assets for low net worth accounts to as high as 26% for high net worth accounts

Commission-based brokerage is the primary channel for accessing these products today, especially for investors in the lowest wealth segment

Low Net worth investors (<250K AUM)
Product access by account type[2]



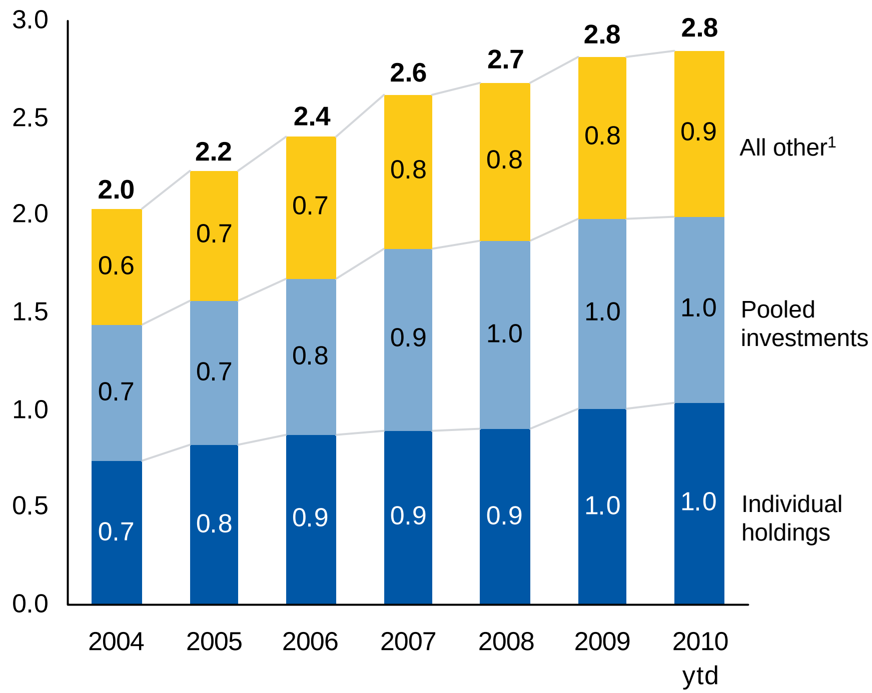
High Net Worth Investors (>5MM AUM)
Product access by account type



1. Cash and other includes cash, currencies, money market funds, etc.
2. Non-discretionary, commission accounts and discretionary, fee accounts
Source: SIFMA member data, Oliver Wyman analysis

Individual investors hold 70% of municipal debt in the US today, both through direct and pooled investments

Investor demand for Municipal Securities
Holdings of Municipal Securities by segment, $TN



Individual holdings (% of total outstanding)							
Direct	37%	37%	36%	34%	34%	36%	36%
Indirect	34%	33%	34%	36%	36%	35%	34%

1. Other sectors include corporates, financial institutions, broker-dealers, and foreign entities
Source: Federal Reserve

Key observations

- The municipal securities market has grown steadily over the past several years and now provides nearly $3TN in financing for state and local governments
- Municipalities in the U.S. have issued ~$400BN debt annually over the past five years through these instruments
- The market is dominated by individual investors who hold ~ 70% of outstanding debt, split across direct exposures and pooled investments
- Financial institutions are relatively minor players in the space, collectively holding less than 30% of total assets (including broker-dealer inventories)
- A significant shift in the 'standard of care' required for origination and distribution of investments sold on a principal basis (as Munis are) could have a significant market impact along 2 dimensions
  - Access and cost for retail investors
  - Low cost financing for municipalities

Broker-dealers play a key role in the Munis market, providing individual investors with direct and cost effective access to new issuances of these securities

Channels

Retail Investors

Primary market

- Transaction costs are built into the 'discount' or underwriting fees paid by the issuer
- Investors have access to securities with no explicit mark-up during limited retail order periods

Secondary market

- Securities trade on the secondary market and prices fluctuate to reflect supply and demand
- Investors have access to securities through broker-dealers who act as principals and build inventory (mark-up paid by investors)

Pooled investment funds

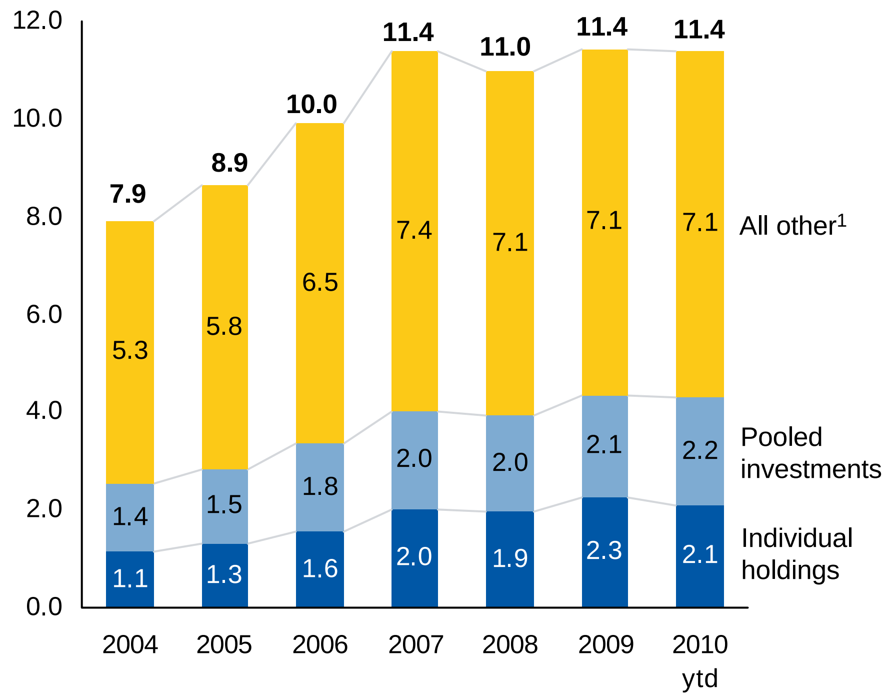
- Securities are bought and sold by broker-dealers on behalf of pooled investment funds
- Investors pay the funds' asset management / advisory fees in addition to transaction costs / sales loads passed on by the fund

Role of the broker-dealer

- Direct, affordable access to municipal bonds for retail investors via primary and secondary principal trading desks → mutual funds are an alternative channel to Munis but at higher cost as management fees erode returns (~1% management fees vs. 4-5% average yield)

Individual investors are also important participants in the corporate bond market

Investor demand for Corporate and Foreign Bonds
Holdings of Corporate and Foreign Securities by segment, $TN



Individual holdings (% of total outstanding)

Direct	14%	15%	16%	18%	18%	20%	18%
Indirect	18%	17%	18%	18%	18%	18%	19%

1. Other sectors include corporates, financial institutions, broker-dealers, and foreign entities
Source: Federal Reserve

Key observations

- Corporations and foreign entities rapidly increased issuance of new debt between 2004-2007 and have maintained annual new bond issuance of ~ $11TN since the financial crisis
- Individual investors (via direct holdings or pooled investments) are the largest single class of investor in the corporate and foreign bond market
- Individual investors hold $4.3TN or nearly 40% of outstanding debt today
- In absolute terms, individual investors' share of the corporate securities market is larger than municipal securities
- Capital formation for US corporates is driven in large part by individual investment

Broker-dealers anticipate retail demand for corporate bonds and hold inventory to quickly, efficiently, and cost effectively meet client needs in the secondary market

Channels

Channels	Retail Investors	
Primary market		▪ Predominantly institutional market ▪ Retail investors have little to no access to primary issuance
Secondary market		▪ Primarily over-the-counter market → broker-dealers provide main point of access for retail investors to these securities ▪ Investors pay upfront mark-ups but no ongoing management fees that are likely to erode returns
Pooled investment funds		▪ Securities are bought and sold by broker-dealers on behalf of pooled investment funds ▪ Investors pay the funds' asset management / advisory fees in addition to transaction costs / sales loads passed on by the fund

Role of the broker-dealer

- Direct, affordable access to corporate bonds for retail investors via secondary principal trading desks → principal traders anticipate retail demand and build inventory that meets specific investment needs of clients

Section 6

Impact on cost

We have profiled three typical investors within each wealth segment to evaluate the potential costs of broad application of the Advisers Act of 1940[1]

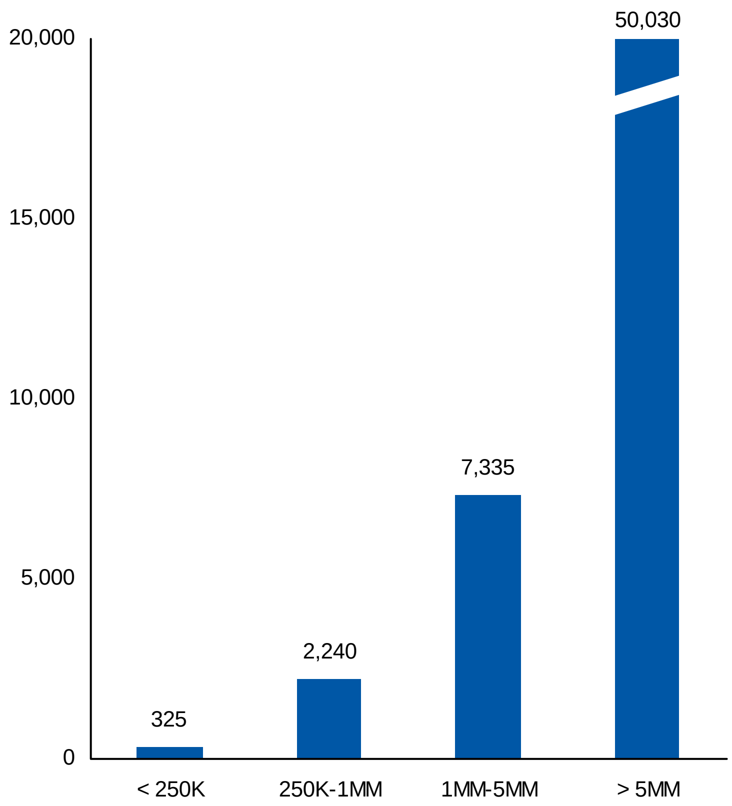
A	**'Small Investor' with commission-based accounts** *77% of all investors*	▪ $200K in assets held exclusively in commission-based accounts ▪ Passive investor with less than 10 trades per year (~50% of investors in <$250K segment) ▪ Pays 94 bps or $1,890 in commissions per year ▪ Holds $132K (68% of assets) in mutual funds and cash / cash equivalents ▪ Significant direct holdings (31% of assets), mainly in equities ▪ Limited investments in alternatives, fixed income, and structured products
B	**'Affluent Investor' with commission-based accounts** *7% of all investors*	▪ $500K in assets held in commission-based accounts ▪ Active investor with more than 10 trades per year (~75% of investors in $250K-1MM segment) ▪ Pays 53 bps or $2,650 in commissions per year ▪ Holds $292K (59% of assets) in mutual funds and cash / cash equivalents ▪ Holds $117.5K (23% of assets) in equities ▪ Hold $90.5K (18% of assets) in fixed income, structured products and alternatives
C	**'High Net Worth Investor' with commission-based accounts** *2% of all investors*	▪ $10MM in assets held in commission-based accounts ▪ Active investor with more than 10 trades per year (~75% of investors in >$1MM segment) ▪ Pays 38 bps or $38,000 in commissions per year ▪ Mutual funds and cash / cash equivalents together are $4.1MM (41% of assets) ▪ Equities are largest part of portfolio, with $3.3MM invested (33% of assets) ▪ Fixed income, structured products and alternatives represent $2.6MM (26% of assets)

1. Asset allocation based on observed average asset allocation for each wealth segment
Source: SIFMA member data, Oliver Wyman analysis

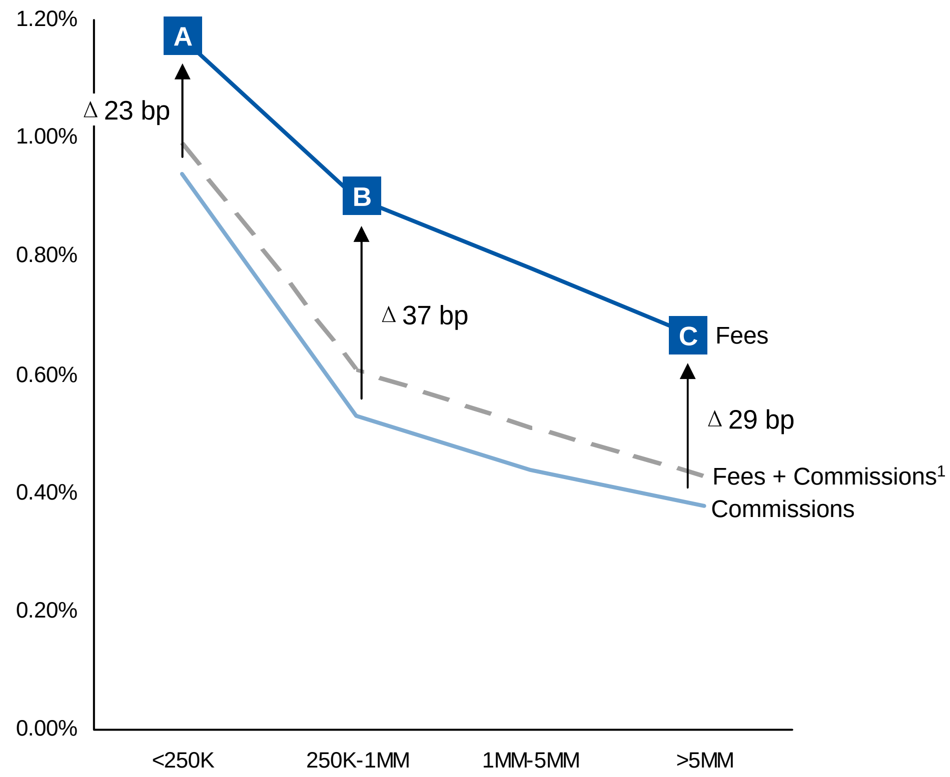
Commission-based accounts provide the most cost effective option for investors across the wealth spectrum today

Financial cost to consumer

Average annual fees and commissions, 2009



Average annual fees and commissions as % of AUM, 2009



1. Based on existing balance of assets between fee-based and commission-based accounts

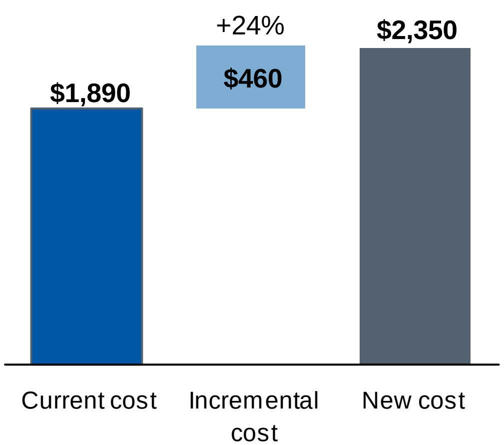
Source: SIFMA member data, Oliver Wyman analysis

A broad shift to fee-based advisory would substantially increase costs across all wealth segments

Potential impact on advisory fees and expected returns

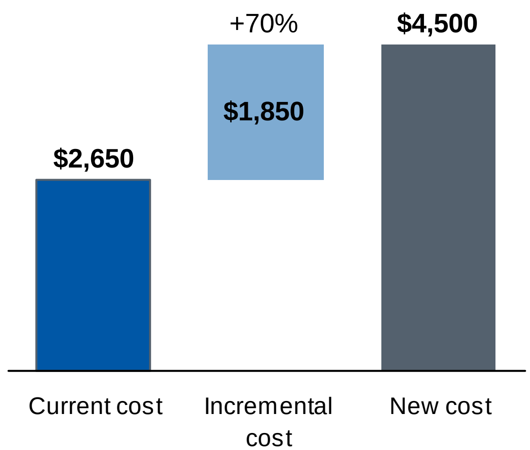
Pro forma impact of transition to fee-based accounts at current pricing, annual advisory costs[1]

A Small Investor



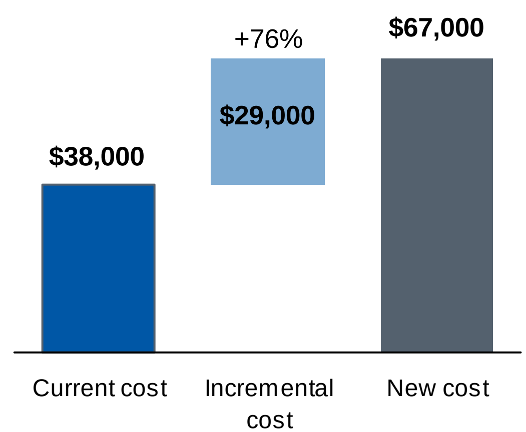
Gross Expected Return[1]	5.00%
- Current Cost	0.94%
Current Expected Return	4.06%
- Incremental Cost	0.23%
New Expected Return	**3.83%**

B Affluent Investor



Gross Expected Return[1]	5.00%
- Current Cost	0.53%
Current Expected Return	4.47%
- Incremental Cost	0.37%
New Expected Return	**4.10%**

C High net worth Investor



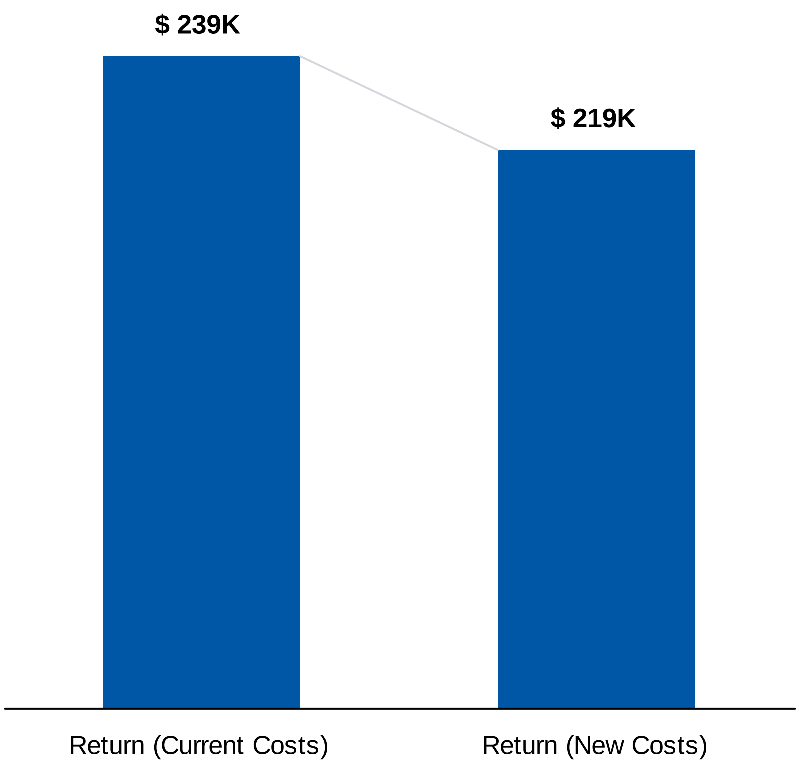
Gross Expected Return[1]	5.00%
- Current Cost	0.38%
Current Expected Return	4.62%
- Incremental Cost	0.29%
New Expected Return	**4.33%**

1. Assumes current pricing for commission- and fee-based accounts hold for all investors
2. Illustrative, not based on observed annual returns

Sources: SIFMA data, Oliver Wyman analysis

The shift to a fee-based model would reduce cumulative returns to 'small investor' (with $200K in assets) by $20K over the next 20 years

Impact of cost on investor returns
Expected investment gains on $200K portfolio, 2010-2030[1]



Key observations

- The average investor in the lowest wealth segment trades relatively infrequently over the course of the year
- As a result, a fee-based cost structure is generally more costly for these 'passive investors' and the incremental costs (+23 bps) erode returns
- For 'small investor,' a fee-based model results in a cumulative reduction in investment gains of $20K over 10 years, roughly 10% of the initial investment
  - 'Small investor' would pay ~ $59K in commissions over the course of 20 years through commission-based brokerage accounts
  - Under a fee-based advisory model, 'small investor' would pay an additional $13K in fees and lose $7K in investment gains as a result of lower principal balances each year

1. Assumes initial investment of $200K in a balanced portfolio reflecting typical, balanced asset allocation for lower net worth investors with <$250K AUM; based on constant annual returns of 5%, not adjusted for inflation; commissions deducted from principal balance starting at year end

However, the costs of complying with and / or demonstrating compliance with the new standard of care will place additional pressure on pricing

Increased activities required by shift in 'standard of care'

- Adviser training
- Increased legal and compliance
- Increased risk management and oversight
- Production and mailing of additional disclosures
- Initial client consultation
  - Review relationship
  - Obtain formal consent for existing strategy
- Investment strategy and plan
  - Evaluate portfolio
  - Assess investment objectives
  - Agree on new investment plan for client
- Documentation of client discussions
- Ongoing account surveillance

Incremental cost of compliance
Annual costs expressed as bps over assets

Additional hours	1	2	3	4	5
Estimated cost	**$200**	**$400**	**$600**	**$800**	**$1,000**
A Small investor ($200K)	10bps	20bps	30bps	40bps	50bps
B Affluent investor ($500K)	4bps	8bps	12bps	16bps	20bps
C HNW investor ($10MM)	2bps	4bps	6bps	8bps	10bps

Focus of analysis on following slides (conservative estimate)

Methodology for calculating hourly rate

- Median income for investment advisers estimated at $173K[1]
- Adviser compensation represents 42% of fully loaded costs based on SIFMA member data
- Given 2,000 working hours per year, average hourly rate of service is $200 / hour

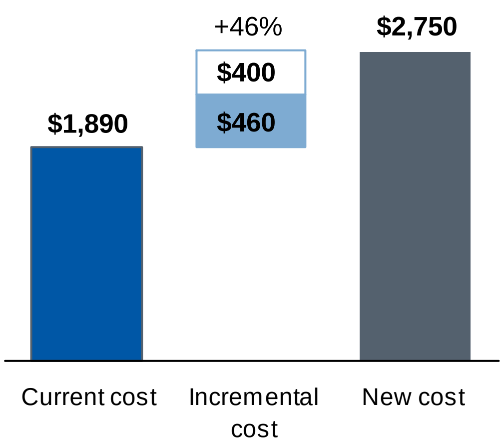
1. Based on 2010 annual compensation survey by Registered Rep
Source: SIFMA member data, Oliver Wyman analysis

These incremental costs will disproportionately impact investors with smaller investment portfolios

Potential impact on advisory fees and expected returns

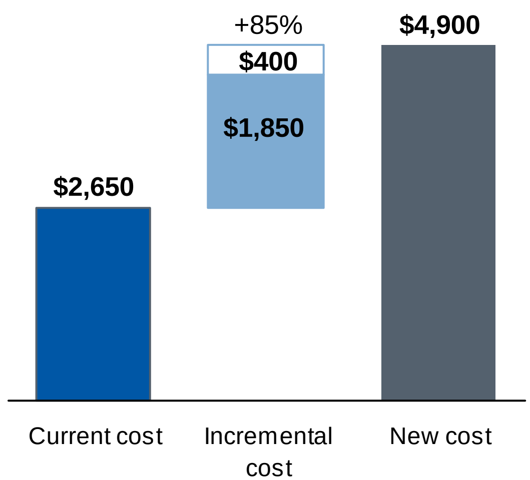
Pro forma impact of transition to fee-based accounts at new pricing, annual advisory costs

A Small Investor



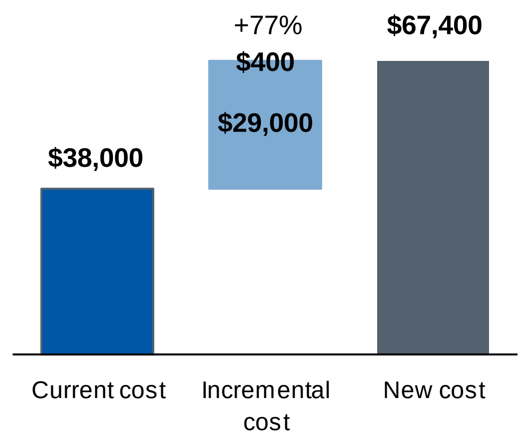
Gross Expected Return[1]	5.00%
- Current Cost	0.94%
Current Expected Return	4.06%
- Incremental Cost	0.43%
New Expected Return	**3.63%**

B Affluent Investor



Gross Expected Return[1]	5.00%
- Current Cost	0.53%
Current Expected Return	4.47%
- Incremental Cost	0.45%
New Expected Return	**4.02%**

C High net worth Investor



Gross Expected Return[1]	5.00%
- Current Cost	0.38%
Current Expected Return	4.62%
- Incremental Cost	0.29%
New Expected Return	**4.33%**

1. Assumes pricing for commission- and fee-based accounts rises to account for additional activity
2. Illustrative, not based on observed annual returns

Sources: SIFMA data, Oliver Wyman analysis

Consumers may also face significant adviser capacity constraints that will limit the availability of service under the new standard of care

Capacity analysis

Current state

Investors with <$250K in commission accounts	28.4MM
Average commissions/investor	$268
Hourly rate for asset management services	$200
Time spent per investor	1.3 hours
Time spent on all investors with <$250K AUM	38.1MM hours
Minimum number of required advisers	19K

Impact of additional service requirements
+ 2 hours per investor

Current utilization levels	70%	80%	90%	100%
Implied capacity (MM hours)	54.4	47.6	42.3	38.1
Implied capacity (total investors, MM)	16.3	14.3	12.7	11.4
Coverage gap (total investors, MM)	12.1	14.2	15.8	17.0
Additional advisers needed	20K	24K	26K	28K

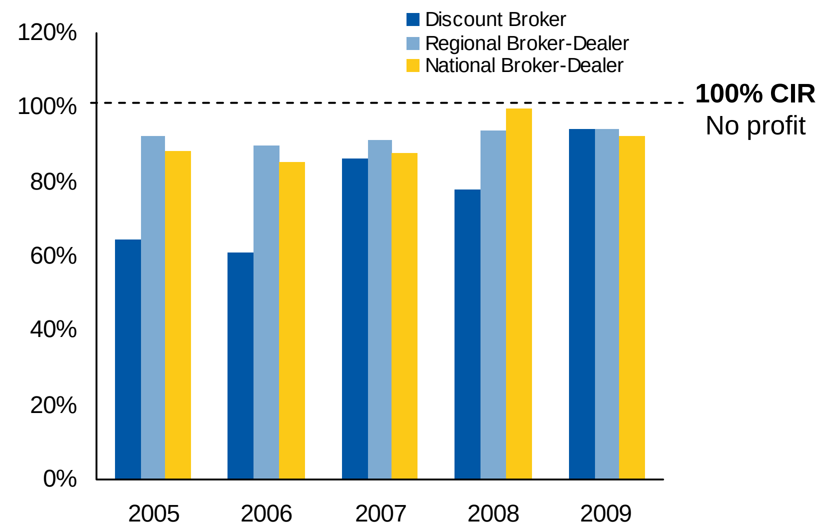
Implications

- Given current resources, we estimate that 40-57% of investors in the lowest wealth segment can be covered if advisers are required to spend 2 additional hours with each investor
- We estimate that 20-28K additional advisers will be needed to serve the 'uncovered' investors in our sample population → our sample population is 33% of US investors, which suggests that 60-84K new advisers may be needed
- Faced with this, the brokerage and investment advisory industry can respond in one of three ways
  - Increase workforce and raise prices
  - Increase workforce and absorb new costs
  - Reduce coverage for lower net worth investors whose 'personalized investment' advisory needs will exceed capacity
- While the autonomy provided by self-directed accounts is desirable for certain investors, market data suggests that investors with advised accounts
  - Make more sophisticated investment decisions
  - Achieve higher average investment returns

Source: SIFMA member data, Oliver Wyman analysis

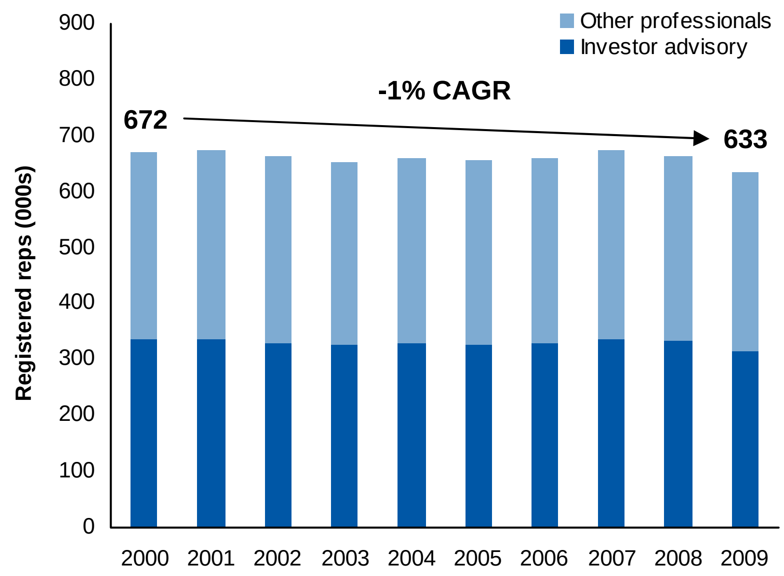
Current economics of the IA/BD industry suggest that investors will need to accept higher costs or turn to alternative service models for investment

Industry profitability
Total costs before tax over total revenues[1]



Operating margins across the industry are thin and have deteriorated since 2005, leaving little room to absorb additional cost

Industry capacity
FINRA registered representatives (000s)[2]

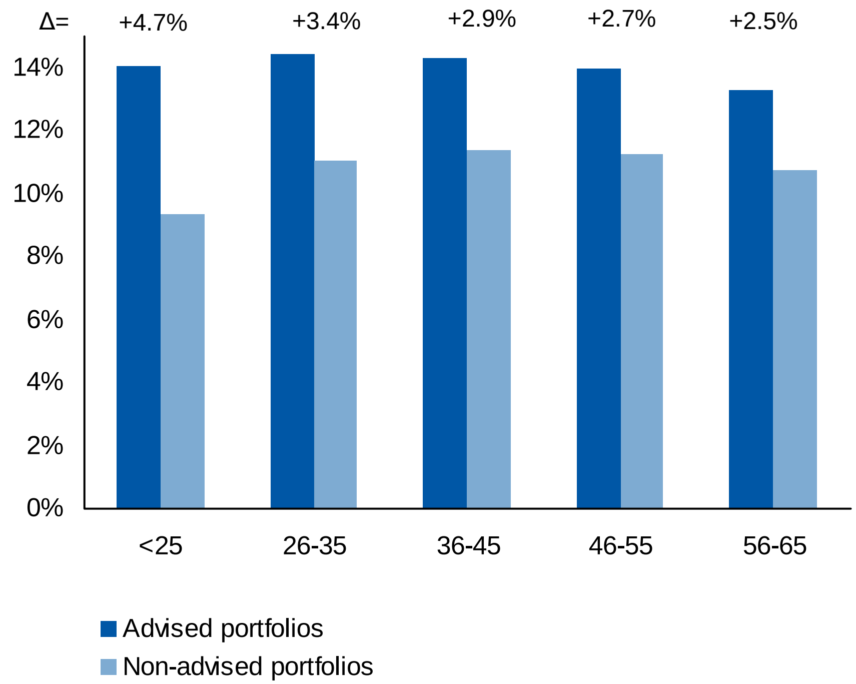


Industry headcount has been flat to negative over the past ten years; the additional capacity required to cover small clients would be difficult to provide (at least in the near term)

1. Public data for companies within the SNL National Broker-Dealer, Regional Broker-Dealer, and Discount Broker indices
2. Figures overstate actual industry capacity (approximately 50-60% of individuals who hold Series 7 licenses do not advise investors, but serve in other capacities e.g. legal, compliance, etc.)
Sources: SNL Financial, FINRA

And several recent studies suggest that investors without access to advisory services may be disadvantaged and fail to realize investment goals

Impact of professional financial advice[1] on portfolio returns
401k returns by age segment, 2006 data



Key observations

- Participants in 401k plans administered by Schwab achieved returns that were 3.3% higher on average if some level of financial advice was provided
- In addition to higher portfolio returns, professional financial advice had an impact on several dimensions
  - Savings rate → 70% of participants who received financial advice doubled their saving rates from an average of 5% to 10% of pre-tax income
  - Portfolio diversification → Participants who received financial advice held positions across 8 asset classes on average vs. self-directed investors who held positions in 3.7
  - Investor confidence → Of participants who received advice, 29% were confident of having adequate funds to retire vs. 16% of investors who did not

1. Use of advisory services for >1 year, 'advisory services' include personalized investment advice online, via phone, or in person
Source: Charles Schwab studies on 401(k) portfolio returns (2007) and impact of professional advisory relationships in 401(k) plans (2010)

Appendix

MiFID Investor Protection

In 2007, the Markets in Financial Instruments Directive (MiFID) made significant provisions for 'investor protection'

MiFID provisions

- Regulation of alternative trading systems
  - Regulation of multi-lateral trading facilities
  - Treatment of systemic internalisers, or principal traders, as mini-exchanges
- Increased pre and post trade transparency for all trading facilities
- Passporting or development of a single market for transactions in financial instruments across a number of European Union member states
- Requirement to enhance corporate governance structures to accommodate an independent compliance function
- Investor protection
  - Appropriate client categorization and client order handling
  - Best execution requirement for all trades on behalf of clients
  - Robust record keeping systems for periodic statements, transaction reporting, and client contracts and agreements

MiFID relative to Advisers Act of 1940

- MiFID provisions covered a narrower range of activities and imposed a less onerous standard of care than the 'best interest' standards that would be required if the Advisers Act were adopted

	MiFID	
	Suitability	**Best interest**
Investment planning	✓	×
Asset allocation advice	✓	×
Advice on client holdings	✓	×
Proprietary product sales	✓	×
Underwriting	Not covered	
Principal trading	✓	×
IRA / retirement accounts	✓	×

Although less onerous than the 'standard of care' currently under consideration in the US, MiFID studies nonetheless show the impact of similar compliance costs on asset management firms

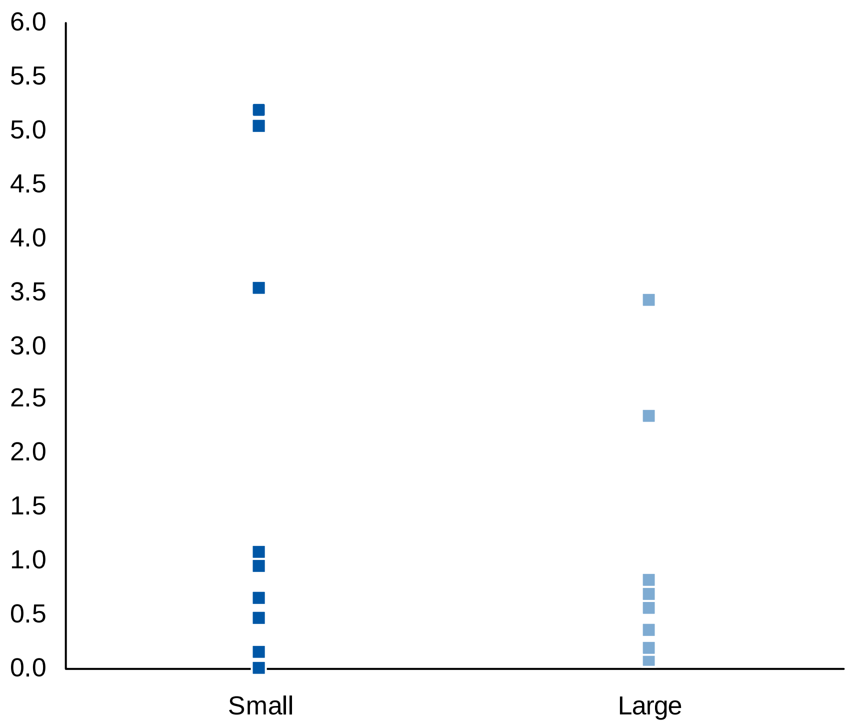
The FSA's impact studies on MiFID identified investor protection provisions as the greatest contributors to compliance costs

	Activity	Objective	Cost Factors	Cost Drivers
Client Acquisition	**Classifying client base**	Categorizing clients according to size of portfolio, # trades, etc.	System/process to capture client data Client data collection	Fixed cost # clients, length of client discussions
	Suitability/ Appropriateness	Understanding needs, objectives, risk profiles, experience and expertise of clients	System/process to capture client data Client data collection Updated risk information on products	Fixed cost # clients, level of existing data # products offered
Client Management	**Consent/ Disclosure**	Disclosing information on suitability, best execution policy, conflicts of interest policy, principal trading, etc.	One time client agreements/contracts Routine disclosure	Response rate, # of clients # clients, frequency of disclosure
	Maintenance of client portfolios	Upholding suitability requirement to maintain AUM in appropriate investments	Monitoring client accounts	# clients, # products offered
Order Execution	**Best execution**	Achieving optimal mix of price, speed and likelihood of execution	Regular reviews of execution venues Disclosure to prove best execution policy	# monitored execution venues # clients, frequency of disclosure
	Conflict of Interest	Identifying/addressing conflicts, actively managing potential issues before they become conflicts	Maintaining Chinese Walls Documentation/database	# departments, level of principal trading # products offered
	Documentation of trades	Demonstrating compliance with suitability and best execution requirements	Electronic/voice storage Paper document storage	# trades, # clients, required level of detail # trades, # clients, required level of detail

Source: Implementing MiFID for Firms and Markets, FSA Consultation Paper 2006

Smaller firms with a large retail client base incurred higher one-off costs of compliance as a percentage of operating costs

One-off compliance costs of MiFID by firm size[1]
One-off costs as a percentage of operating costs, 2007



Determinants of one-off costs

- The study found that client profile is the most important determinant of costs, with retail clients incurring significantly more costs than institutional clients
- The biggest one-off costs arose from investment in IT and revisions of CRM systems to reflect new data points, especially for certain retail segments
- A significant portion of one-off costs were fixed, irrespective of firm size and number of clients
- Impact studies indicated that small firms would be unable to sustain large fixed costs of compliance and exit the industry
- In absolute terms, average one-off costs were ~€1 MM for a small firm and ~€4 MM for a large firm
- There is high variability in the level of one-off costs amongst smaller firms depending upon
  - Extent to which firms serve retail clients
  - Ability of firms to make large upfront investments

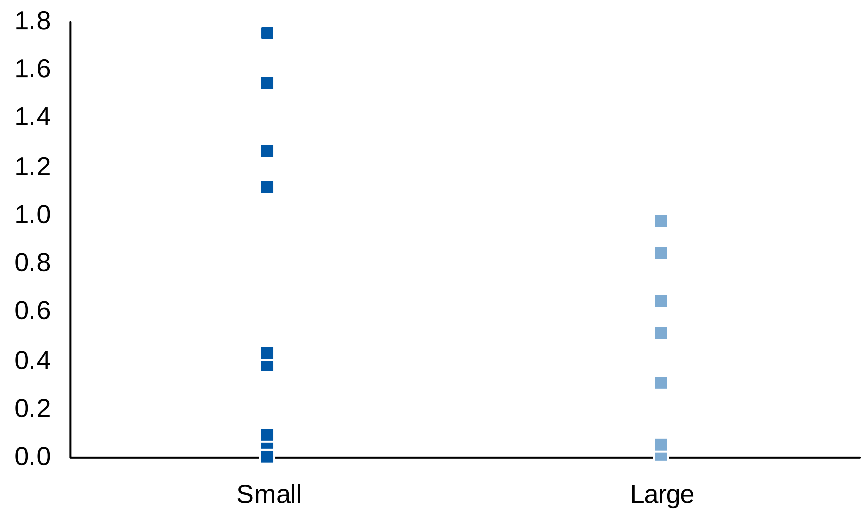
1. Firms with fewer than 100 employees were classified as “Small”
Source: Europe Economics Study, 2007

Due to their inability to make sizeable upfront investments, smaller firms typically also sustained higher ongoing costs of compliance as a percent of operating costs

On-going compliance costs of MiFID
European asset managers by firm size[1], 2007

	Small	Large
Additional staff	70%	18%
Internal reporting	9%	12%
IT	4%	30%
External reporting	12%	17%
Training	2%	7%
Audit	2%	16%

Ongoing compliance costs of MiFID by firm size
Ongoing costs as a percentage of operating costs, 2007



- Whereas larger asset managers complied with MiFID by investing in automated systems, smaller firms increased headcount
- There is a trade-off between one-off and on-going costs, e.g. for smaller firms the option of updating IT systems might have been too expensive, thus on-going costs of sustaining a larger workforce are much higher
- The smallest firms in the study had no specialist compliance functions prior to MiFID, and required significant resources to cover compliance activities

1. Firms with fewer than 100 employees were classified as "Small"
Source: Europe Economics Study, 2007

Encl 2

Invested in America

November 17, 2010

Via email to: rule-comments@sec.gov and IA-BDStudy@sec.gov

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Study Regarding Obligations of Brokers, Dealers, and Investment Advisers; Exchange Act Release No. 62577; Investment Advisers Act Release No. 3058; File No. 4-606

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association (SIFMA)[1] would like to thank you for the opportunity to meet with representatives of the Securities and Exchange Commission (SEC) on November 10th to review our analysis of potential changes to the standard of care for investors served by our member firms.[2] As noted in our previous public statements, SIFMA supports harmonization of broker-dealer and investment adviser regulations for those who provide personalized investment advice to retail investors. We believe this can be accomplished in a way that does not restrict customer choice or product access. We commend the SEC for the depth of review it is undertaking in its current study.

The key findings from our study show that broker-dealers play an important role in retail brokerage, which cannot be easily replicated with alternative service models. Among the findings are:

- 95% of the households served by the firms participating in our survey use commission-based brokerage accounts to meet their investment objectives today;

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[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

[2] Our study, filed with the SEC on October 27, 2010, is available at http://www.sec.gov/comments/4-606/4606-2824.pdf.

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- Access to investment products traditionally offered on a principal basis (corporate and municipal securities) is more common and more affordable through commission-based accounts, particularly for small investors; and

- The realized cost of investment for investors under fee-based advisory accounts is consistently higher (23-27 bps on average) than the commission-based brokerage accounts used by the 38MM+ households covered by our study.

We recognize that the legislation does not prohibit commission-based compensation or other common elements of the broker-dealer service model. Our survey results bear out the relative value of commission-based accounts, particularly for smaller investors. If these same brokerage services had to be provided under the existing provisions of the Investment Advisers Act of 1940, however, it would negatively affect client choice and access to products, such as those now available on a principal basis. Thus, we continue to support a uniform federal fiduciary standard for broker-dealers and investment advisers who provide personalized investment advice to retail clients, yet that new standard must be "operationalized" to reflect the many different business models currently in effect serving investors.

We have drafted this letter to respond to SEC staff requests for additional detail on the methodology used to complete the study, the robustness of the data gathered, and several exhibits contained in the original submission. Accordingly, our response is organized as follows:

- Methodology for impact assessment
- Robustness of data gathered
- Additional data

We are grateful for the opportunity to respond to SEC staff questions and your consideration of the findings from our study.

I. Methodology for impact assessment

SIFMA commissioned Oliver Wyman[3] to analyze the impact of potential changes to the standard of care for investors served by our member firms. Oliver Wyman

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[3] With more than 2,900 professionals in over 40 cities around the globe, Oliver Wyman is an international management consulting firm that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, organizational transformation, and leadership

designed a standard template (see appendix 2) that was distributed to ~30 member firms to collect aggregated data on investment activity, asset allocation, and 'realized investment costs' across different client wealth segments and account types. Due to restrictions on disclosure of personal financial data and operational constraints, client-level data was not requested as part of the survey. Oliver Wyman supplemented the aggregated member data with publicly available information in preparing the study.

In total, 17 firms provided SIFMA with sufficient data for analysis. These firms represent a broad cross-section of SIFMA's membership serving retail investors, including global, national and regional full service broker-dealers, bank brokerages, and discount brokers.

II. Robustness of data gathered

The data gathered to support the analysis covered 38.2MM households with $6.8TN invested with member firms. To put these figures in context:

- The 38.2MM households included in the data represent 33% of households in the United States today, according to the most recent survey of consumer finances by the Federal Reserve.[4] However, not all U.S. households hold investment accounts, implying that the true percentage of investors covered by the data is higher than 33%.

- The $6.8TN in client assets captured in the data represents 27% of financial assets held by investors in the United States. A significant share of the financial assets identified by the Federal Reserve includes 'investments' that are not generally held in brokerage or advisory accounts (e.g. pension assets), implying that the true percentage of investor assets covered by the data is higher than 27%.

The objective of this study is to analyze the impact of potential changes to the standard of care for investors served by our member firms – not necessarily to draw conclusions on the broader investor population. This population of 38MM+ households represents

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development. The firm helps clients optimize their businesses, improve their operations and risk profile, and accelerate their organizational performance to seize the most attractive opportunities. Oliver Wyman is part of Marsh & McLennan Companies [NYSE: MMC]. For more information, visit www.oliverwyman.com.

[4] Federal Reserve Board Survey of Consumer Finances 2007

a meaningful share of the US investor population, which should be considered carefully in the SEC study.

To our knowledge, this information set is unique in that it provides a window into the underlying economics of different models for serving retail investors and is exceptional both in its breadth of coverage and its usefulness in comparing realized investment costs across different firms.

III. Additional data

The SEC staff attending the meeting on November 10th also requested additional detail on asset allocation (provided in summary form on page 17 of the original submission). A breakdown of asset allocation across different client wealth segments and account types is provided in appendix 1 below.

Please let us know if we have adequately addressed your questions and requests for additional information, or if there is anything more we may provide that would be helpful to you.

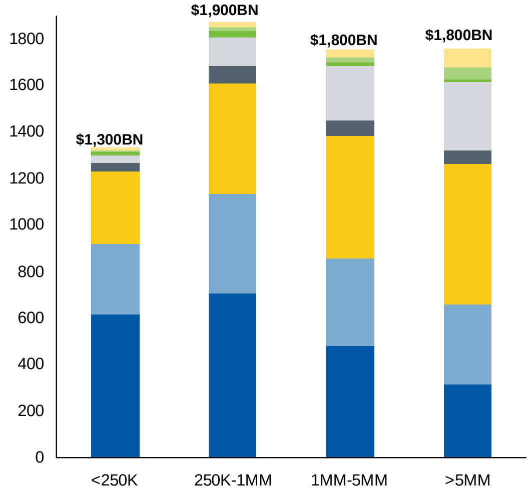
Sincerely yours,

Ira D. Hammerman
Senior Managing Director
and General Counsel

cc: Mary L. Schapiro, Chairman
Luis A. Aguilar, Commissioner
Kathleen L. Casey, Commissioner
Troy A. Paredes, Commissioner
Elisse B. Walter, Commissioner
Robert W. Cook, Director, Division of Trading and Markets
Andrew J. Donohue, Director, Division of Investment Management

Appendix 1: asset allocation across wealth segments and account types

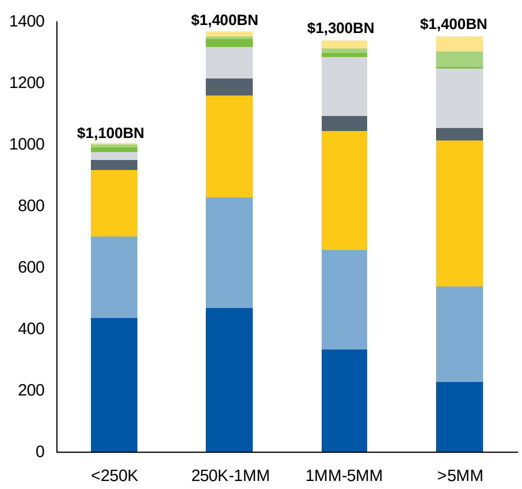
All account types
Asset allocation ($BN) by wealth segment, 2009[1,2]



	<250K	250K-1MM	1MM-5MM	>5MM
Government / Agency Bonds	9	23	35	80
Alternatives	7	14	21	57
Structured Products	18	28	12	7
Municipal Bonds	31	120	238	296
Corporate Bonds	37	76	66	58
Equities	311	478	528	604
Cash / other[3]	306	429	373	346
Mutual Funds / ETFs	614	705	484	313

1. Numbers may not sum to total due to rounding
2. 5 firms representing less than $400BN in assets did not provide asset allocation details by account type and are excluded from analyses on the following charts
3. Includes cash, currencies, money market funds, etc
Source: SIFMA member data, Oliver Wyman analysis

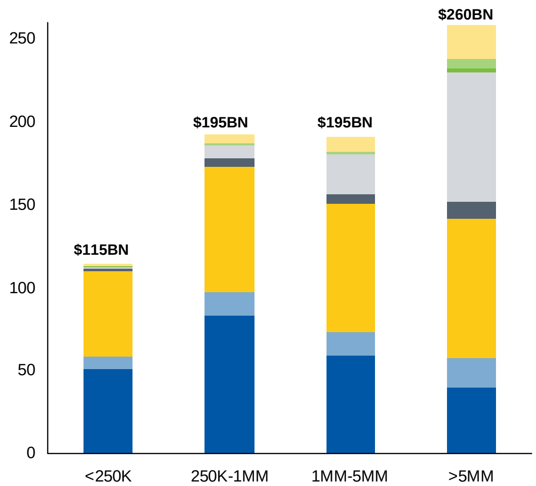
Commission-based, non-discretionary accounts
Asset allocation ($BN) by wealth segment, 2009[1]



	<250K	250K-1MM	1MM-5MM	>5MM
Government / Agency Bonds	7	15	23	51
Alternatives	6	10	17	45
Structured Products	17	25	11	5
Municipal Bonds	28	99	192	195
Corporate Bonds	32	59	51	41
Equities	230	332	386	477
Cash / other[2]	273	359	323	307
Mutual Funds / ETFs	457	468	336	230

1. Numbers may not sum to total due to rounding
2. Includes cash, currencies, money market funds, etc
Source: SIFMA member data, Oliver Wyman analysis

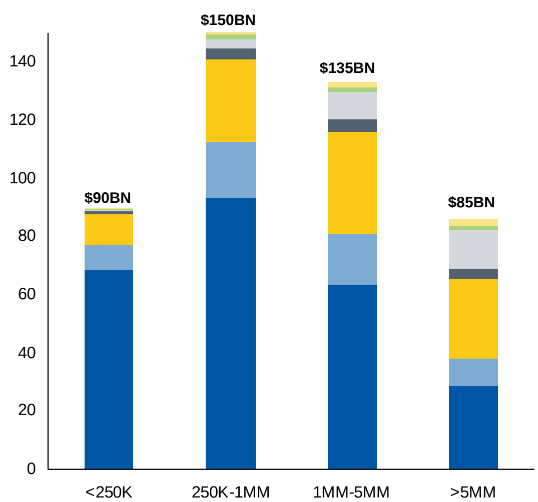
Fee-based, discretionary accounts
Asset allocation ($BN) by wealth segment, 2009[1]



	<250K	250K-1MM	1MM-5MM	>5MM
Government / Agency Bonds	2	6	9	21
Alternatives	<1	1	2	6
Structured Products	<1	<1	<1	2
Municipal Bonds	1	8	23	78
Corporate Bonds	2	5	7	11
Equities	52	75	77	84
Cash / other[2]	7	14	14	18
Mutual Funds / ETFs	51	83	59	40

1. Numbers may not sum to total due to rounding
2. Includes cash, currencies, money market funds, etc
Source: SIFMA member data, Oliver Wyman analysis

Fee-based, non-discretionary accounts
Asset allocation ($BN) by wealth segment, 2009[1]



	<250K	250K-1MM	1MM-5MM	>5MM
Government / Agency Bonds	<1	1	2	3
Alternatives	1	1	2	1
Structured Products	<1	<1	<1	<1
Municipal Bonds	<1	3	9	13
Corporate Bonds	1	4	4	3
Equities	11	28	35	27
Cash / other[2]	8	19	18	10
Mutual Funds / ETFs	69	94	63	29

1. Numbers may not sum to total due to rounding
2. Includes cash, currencies, money market funds, etc
Source: SIFMA member data, Oliver Wyman analysis

Appendix 2: data collection template

Variable inputs for member firms to complete

I. Assets, Revenues, and Costs for all accounts

	Wealth Segment (client assets)			
2009 data	**< 250,000**	**250,000-1MM**	**1MM-5MM**	**>5MM**
Number of households holding accounts (year-end)				
Total fees, commissions, other client-related revenues ($MM)				
Total client assets ($MM) (year-end)				
Asset composition ($MM)				
Equities				
Fixed Income | Corporate Bonds				
Fixed Income | Government and Agency Bonds				
Fixed Income | Municipal Bonds				
Mutual Funds and ETFs				
Structured Products				
Alternatives (Hedge funds, private equity, managed futures)				
Other Products (MM MF's, FCASH, CD's)				

II. Assets, Revenues, and Costs by account type

	Wealth Segment (client assets)			
2009 data	**< 250,000**	**250,000-1MM**	**1MM-5MM**	**>5MM**
Fee-based discretionary accounts				
Number of households holding accounts (year-end)				
Total fees, commissions, other client-related revenues ($MM)				
Total client assets ($MM) (year-end)				
Asset composition				
Equities				
Fixed Income | Corporate Bonds				
Fixed Income | Government and Agency Bonds				
Fixed Income | Municipal Bonds				
Mutual Funds and ETFs				
Structured Products				
Alternatives (Hedge funds, private equity, managed futures)				
Other Products (MM MF's, FCASH, CD's)				
Fee-based non-discretionary accounts				
Commission-based discretionary accounts				
Commission-based non-discretionary accounts				

III. Additional 'client profile' data

	Wealth Segment (client assets)		
2009 data	**< 250,000**	**250,000-1MM**	**1MM-5MM**
Number of clients holding IRA accounts (year-end)			
Fee-based			
Commission-based			
Number of clients holding both fee- and commission-based accounts (year-end)			
Number of clients with concentrated positions >25% of assets in one position (year-end)			
Number of clients executing less than 10 trades in 2009			
Number of clients purchasing shares in IPOs on principal basis in 2009			
Number of clients purchasing Municipal Bonds on principal basis in 2009			

Encl 3

July 14, 2011

Via E-mail

Mary L. Schapiro, Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Framework for Rulemaking under Section 913 (Fiduciary Duty) of the Dodd-Frank Act; **File No. 4-604**

Dear Chairman Schapiro:

The Securities Industry and Financial Markets Association[1] ("**SIFMA**") appreciates the opportunity to submit the following comments for consideration by the Securities and Exchange Commission (the "**SEC**" or the "**Commission**") as it establishes, pursuant to its plenary authority under Sections 913(f) and (g) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "**Dodd-Frank Act**"), a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers.

Throughout the legislative process and debate that preceded the enactment of the Dodd-Frank Act, SIFMA has supported the development of a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers.[2]

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

[2] *See, e.g., Hearing Before the H. Comm. on Financial Servs.*, 111th Cong. 2-3 (2009) (statement of John Taft, Head of U.S. Wealth Management, RBC Wealth Management on behalf of SIFMA), *available at* http://financialservices.house.gov/media/file/hearings/111/taft_testimony.pdf; *Hearing Before the H. Comm. on Financial Servs.*, 111th Cong. 21 (2009) (statement of Randolph C. Snook, Executive Vice President, SIFMA), *available at* http://financialservices.house.gov/media/file/hearings/111/snook.pdf.

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The purpose of this letter is to offer a framework and principles for rulemaking under Section 913 of the Dodd-Frank Act to help inform the Commission's rulemaking process. We also seek to encourage further deliberation and dialogue about the optimal approach for implementing a uniform fiduciary standard of conduct in accordance with the Dodd-Frank Act that is designed to protect investors, preserve investor choice and access to cost-effective financial products and services, and adapt to the substantially different operating models of broker-dealers and investment advisers.

Consistent with these objectives, we also believe that appropriately robust and rigorous cost-benefit analyses are essential to inform and shape any SEC rulemakings, particularly those that call for the type of "sea change" reform envisioned by Section 913 of the Dodd-Frank Act. Thus, we remain supportive of the current cost-benefit and other empirical analyses that we understand the SEC is currently undertaking on this issue, as well as any other analyses that may help inform the optimal approach for implementing a uniform fiduciary standard of conduct. We also will support, as an industry, such studies or analyses by providing appropriate data, feedback, or other information that would result in the most accurate and meaningful findings and conclusions. Accordingly, we are eager to further engage and communicate with the SEC and others on this important issue.

* * * *

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Executive Summary

SIFMA supports the establishment of a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers.[3] The guiding principle that underpins this uniform standard is to act in the best interest of the customer. The standard should be articulated through comprehensive SEC rulemaking as a uniform standard of conduct that is "no less stringent than" the general fiduciary duty implied under the Investment Advisers Act of 1940 (the "**Advisers Act**").

The SEC's Study on Investment Advisers and Broker-Dealers (the "**Study**")[4] contains a number of thoughtful findings. It does not, however, specify that the contemplated uniform fiduciary standard of conduct for broker-dealers and investment advisers should be separate and distinct from the general fiduciary duty implied under Section 206 of the Advisers Act. Instead, the Study raised the serious concern among our member firms that the SEC may be contemplating an "overlay" on broker-dealers of the existing Advisers Act standard.[5] SIFMA strongly opposes imposing on broker-dealers the existing Advisers Act standard together with its associated case law, guidance, and other legal precedent.

Our members are also concerned that the SEC could take the unnecessarily narrow view that, because Section 913 of the Dodd-Frank Act requires that the uniform fiduciary standard be "no less stringent than" the general fiduciary duty implied under Section 206 of the Advisers Act, the SEC's latitude and ability to establish a separate, unique uniform fiduciary standard is limited. We believe no such limitation exists or was intended under the Dodd-Frank Act. The plain language of Section 913, together with the legislative history of the Dodd-Frank Act, makes clear that the "no less stringent" language does *not* require that the SEC impose the Advisers Act standard on broker-dealers.[6] As Congressman Barney Frank has indicated,

[3] SIFMA's position is limited to retail customers, i.e., natural persons who use investment advice for personal, family or household purposes. SIFMA does not propose to modify the current Advisers Act standard applicable to the delivery of investment advice to the institutional clients of investment advisers, or the existing case law, guidance or other legal precedent developed under Section 206 of the Advisers Act.

[4] Commission Study on Investment Advisers and Broker-Dealers, as required by Section 913 (Jan. 2011), available at http://www.sec.gov/news/studies/2011/913studyfinal.pdf.

[5] *Id.* at pp. 109 and 111.

[6] Letter from Congressman Barney Frank to Chairman Mary Schapiro at p. 1 (May 31, 2011) (the **"Frank Letter"**) ("'no less stringent' … was not intended to encourage the SEC to impose the … Advisers Act… standard on broker-dealers…").

> "If Congress intended the SEC to simply copy the [Advisers] Act and apply it to broker-dealers, it would have simply repealed the broker-dealer exemption – an approach Congress considered but rejected. The new standard contemplated by Congress is intended to recognize and appropriately adapt to the differences between broker-dealers and registered investment advisers."[7]

Investment advisers are generally engaged in the business of providing advice about securities for a fee, or managing assets on a discretionary basis. Broker-dealers engage in the former activity on occasion (advice about securities), but also provide a broad range of additional products and services. Broker-dealers provide, for example, initial and follow-on public offerings and other underwritten offerings, and market fixed-income and affiliated products, all of which contribute to the capital raising, liquidity, best execution, and portfolio balancing functions of our securities markets. Yet, these services, which are beneficial to both the economy and individual investors, often carry inherent (though generally accepted and well-managed) conflicts of interest. The general fiduciary duty implied under Section 206 of the Advisers Act, as developed through case law, guidance and other legal precedent, however, provides incompatible and insufficient guidance for broker-dealers on how to manage, disclose, or obtain consents to these conflicts.

In Section II, we explain in detail why a wholesale extension to broker-dealers of the case law, guidance and other legal precedent under Section 206 of the Advisers Act would entail a host of adverse consequences. Most importantly, it would *not* be in the best interest of retail customers, because it would negatively impact choice, product access and affordability of customer services. It would also be problematic for broker-dealers from a commercial, legal, compliance, and supervisory perspective, thereby undercutting the SEC's stated intent to take a "business model neutral" approach. The Dodd-Frank Act authorizes, the SEC Study supports, and investor protection warrants, taking a fresh approach by establishing, through SEC rulemaking under Section 913 of the Dodd-Frank Act, a uniform fiduciary standard of conduct for broker-dealers and investment advisers.

In Section III, we offer, for the first time, a proposed framework and principles to advance the development of a fiduciary standard of conduct through SEC rulemaking under Section 913 of the Dodd-Frank Act. Under our proposed framework, the general fiduciary duty implied under Section 206 of the Advisers Act, which derives from the traditional, generally understood and accepted common law,[8] would be newly articulated through SEC

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[7] *Id.*

[8] *See SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 195 (1963) ("…Congress codified the common law 'remedially' [in the Advisers Act] … to prevent[] fraudulent securities transactions by fiduciaries"). *See also* Restatement of Agency (Third) (agency is the fiduciary relationship that arises when one person (the principal) manifests assent to another person (the agent) that the agent shall act on the principal's behalf and subject to the principal's control, and

rulemaking under Section 211 of the Advisers Act and Section 15 of the Securities Exchange Act of 1934 (the "**Exchange Act**").[9] The standard of conduct would apply equally to broker-dealers (through Section 15(k) of the Exchange Act) and investment advisers (through Section 211(g) of the Advisers Act) when providing personalized investment advice about securities to retail customers. The SEC would also issue rules and guidance to provide the detail, structure and guidance necessary to enable broker-dealers and investment advisers to apply the uniform fiduciary standard of conduct to their distinct operational models.[10]"

The uniform fiduciary standard of conduct would begin with the core principle mandated by the Dodd-Frank Act that all brokers, dealers and investment advisers, when providing personalized investment advice about securities to retail customers, shall "act in the best interest of the customer …."[11] The complete phrase reads "act in the best interest of the customer *without regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice*" (emphasis added). The italicized language could be interpreted to require firms to operate a conflicts-free business (if read literally and not in conjunction with other Section 913 statutory language that permits disclosure of, and customer agreement to, material conflicts).[12] It also appears to conflict with other Section 913 statutory language that allows commission-based compensation, proprietary products, and a non-continuing fiduciary duty. Based upon our communications with the Commission and their staff, however, we agree with their view that such language should *not* represent an impediment to the SEC establishing a uniform fiduciary standard that is

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the agent manifests assent or otherwise consents so to act). *But see* Section II.B.2, explaining that existing case law regarding the fiduciary duty of investment advisers was developed in the context of a business model which is inapplicable to broker-dealers, and applying such case law in the broker-dealer context could have legal and regulatory consequences that would undermine the broker-dealer business model, with no corresponding benefit to retail customers.

[9] Thus, the uniform fiduciary standard of conduct would conclusively satisfy the Dodd-Frank Act's requirement that the standard be "no less stringent than" the standard implied under Section 206 of the Advisers Act.

[10] Our proposed approach is consistent with that historically followed in agency and trust contexts. The precise contours of the fiduciary obligation are molded to particular fiduciary fields or contexts. Thereafter, common sets of facts are addressed through implementing rules that apply the duties of loyalty and care to those circumstances. "The ... rules simplify application of the fiduciary obligation to cases that fall within their terms, reducing decision costs." *See* Robert H. Sitkoff, *The Economic Structure of Fiduciary Law*, 91 B.U. Law Rev. 1039, 1044-45 (2011).

[11] Section 913(g) of the Dodd-Frank Act.

[12] *Id.* ("In accordance with [the rules promulgated under the uniform fiduciary standard of conduct], any material conflicts of interest shall be disclosed and may be consented to by the customer.")

sufficiently flexible, fairly balanced, business model neutral and, most importantly, investor protection focused. Accordingly, the principle of "acting in the best interest of the customer" would serve as the bedrock cornerstone of the SEC rules promulgated under Section 211 of the Advisers Act and Section 15 of the Exchange Act.

Existing case law, guidance, and other legal precedent developed under Section 206 of the Advisers Act would continue to apply to investment advisers. While there would be many parallels, this Section 206 precedent would *not* apply to broker-dealers, because: (i) broker-dealers provide a different range of products and services, and operate under an operational model distinct from that of investment advisers;[13] and (ii) Section 206 precedent does not now apply to broker-dealers. Section 206 precedent would therefore not apply in the future to broker-dealers under the uniform fiduciary standard of conduct established under Section 211 of the Advisers Act and Section 15 of the Exchange Act.[14]

Attached as **<u>Appendix 1</u>** is a one-page graphical representation to help visualize the framework we are now proposing. Our framework is built around the following five key components:

1. Enunciate the core principles of the uniform fiduciary standard of conduct.

2. Articulate the scope of obligations under the uniform fiduciary standard of conduct.

3. Define "personalized investment advice".

4. Provide clear guidance regarding disclosure that would satisfy the uniform fiduciary standard of conduct.

5. Preserve principal transactions.

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[13] While broker-dealers and investment advisers may at times provide similar services, there are many substantive differences in the products, services, conflicts, and traditional compensation practices between the two well-established and highly regulated business models. *See, e.g.*, Letter to Elizabeth M. Murphy, SEC, from Ira D. Hammerman, SIFMA (Aug. 30, 2010), *available at* http://www.sec.gov/comments/4-606/4606-2553.pdf ("**SIFMA Section 913 Comment Letter**"); Frank Letter at p. 1.

[14] The express language of Dodd-Frank Act Section 913 appears to support this approach. Section 913 pegs the uniform fiduciary standard to Sections 206(1) and (2) of the Advisers Act, but not to Section 206(3), which restricts principal transactions, or to Section 206(4), which grants the SEC authority to issue rules under Section 206. Thus, it may fairly be said that Congress did not intend for Section 206 rules or other legal precedent to apply to broker-dealers under the uniform fiduciary standard of conduct.

Our proposal is intended to inform the Commission's rulemaking process and encourage further discussion about the optimal approach for implementing a uniform fiduciary standard of conduct. We believe the optimal approach is one that fully protects investors, preserves their choice of and access to financial products and services, and adapts to the substantially different business models of broker-dealers and investment advisers. We believe that our proposal, and call for a uniform fiduciary standard to be established through SEC rulemaking, fully satisfies these criteria and will benefit millions of retail investors for years to come. We are hopeful that the Commission will find this framework constructive and useful to the process going forward.

While not a focus of this letter, SIFMA also generally supports the Study's recommendation that the SEC consider harmonizing other areas of broker-dealer and investment adviser regulation, including advertising, the use of finders and solicitors, supervisory requirements, licensing and registration of firms and associated persons, and books and records, among others. We encourage further deliberation by the SEC regarding these discrete regulatory areas, and we hope to engage the staff in future dialogue on these topics.

I. Introduction

We welcome the Commission's efforts to develop a uniform fiduciary standard for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers. As we have previously stated, SIFMA's position is limited to retail customers, i.e., natural persons who use investment advice for personal, family or household purposes, and we do not propose to modify the current Advisers Act standard applicable to the delivery of investment advice to the institutional clients of investment advisers, or the existing case law, guidance or other legal precedent developed under Section 206 of the Advisers Act.

We believe the following key principles should guide the development of the standard:[15]

- The interests of retail customers should be put first. When providing personalized investment advice about securities to retail customers, broker-dealers and investment advisers should deal fairly with these customers, and, at a minimum, appropriately manage conflicts and provide retail customers with full disclosure that is simple and clear and allows retail customers to make an informed decision about a particular product or service.

- Investors should continue to have access to, and choice among, a wide range of products and services. The standard of conduct should allow broker-dealers to

[15] SIFMA Section 913 Comment Letter.

continue to offer products and services that are available today, such as providing retail customers liquidity as principal, proprietary products and advice regarding sophisticated investment strategies. The standard should allow retail customers to choose among various models for compensating their financial services provider.[16]

- The uniform fiduciary standard of conduct should be "business model neutral."

- The SEC should clearly define the standard of conduct and should provide guidance as to how it can be implemented by broker-dealers, tailored to their various business models.

- Where products and services involve material conflicts of interest, broker-dealers and investment advisers should be able to provide disclosures to customers in a pragmatic way to clearly and effectively communicate, and receive the customer's consent to, these conflicts of interest. Similarly, the SEC should provide guidance to clarify whether a customer's affirmative consent is required or not, and if so, at what point it should be obtained.[17]

The Dodd-Frank Act authorizes the Commission to adopt rules to provide that the standard of conduct for all broker-dealers and investment advisers, when providing personalized investment advice about securities to retail customers, is to act in the best interest of the customer. This standard of conduct shall be no less stringent than the fiduciary duty applicable to investment advisers under Sections 206(1) and (2) of the Advisers Act.

As explained in detail in Section II, while we embrace the adoption of a uniform fiduciary standard of conduct, we believe that a wholesale extension to broker-dealers of the general fiduciary duty implied under the Advisers Act is not in the best interests of investors and is problematic for the broker-dealer business model. Instead, we advocate for taking the sum and substance of the general fiduciary duty implied under the Advisers Act and articulating it through SEC rulemaking as the uniform fiduciary standard of conduct – a standard which would:

- apply only to, and be tailored for, those services and activities involving provision of personalized investment advice about securities to retail customers;

[16] We note that the Dodd-Frank Act provides that the sale of only proprietary or other limited range of products, or the receipt of commission-based compensation, shall not, in and of themselves, violate the uniform fiduciary standard of conduct.

[17] *See* Section III.C.4.b.v. and vi.

- provide for reasonable approaches to managing conflicts;

- provide adequate flexibility to preserve and enhance client choice, product and service innovation, and capital formation; and

- otherwise provide the detail and guidance necessary to enable broker-dealers and investment advisers to apply the standard of conduct to their distinct operational models.

In Section III below, we offer a framework for the uniform fiduciary standard of conduct to inform the Commission's rulemaking process. We believe that this proposed standard of conduct, adapted to the substantially different operating models for broker-dealers and investment advisers, offers the best approach for protecting investors and preserving investor choice and access to cost-effective financial products and services.

II. The Need for a New Articulation of a Uniform Fiduciary Standard of Conduct

A. Overview

In January 2011, the SEC published its Study, which contained a number of thoughtful findings. It did not, however, specify that the contemplated uniform fiduciary standard of conduct for broker-dealers and investment advisers would be separate and distinct from the general fiduciary duty implied under Section 206 of the Advisers Act. Instead, the Study raised serious concern among our member firms that the SEC may be contemplating an "overlay" on broker-dealers of the existing Advisers Act standard, with its associated case law, SEC guidance and other legal precedent.[18]

The wholesale imposition of the Advisers Act fiduciary duty on broker-dealers would be commercially impracticable. In light of the distinct differences between the operating models of investment advisers and broker-dealers,[19] and in order to maintain broker-dealer products and services for investors, SIFMA believes the obligations of broker-dealers when providing personalized investment advice about securities to retail customers under the uniform fiduciary standard of conduct should *not* be governed by the existing rules, case law, guidance or other legal precedent under Section 206 of the Advisers Act.[20]

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[18] Study at pp. 109 and 111.

[19] *See* SIFMA Section 913 Comment Letter.

[20] As explained in the Executive Summary, existing Section 206 legal precedent and guidance would continue to apply to investment advisers.

SIFMA therefore supports a new articulation, through SEC rulemaking, of the general fiduciary duty implied under Section 206 of the Advisers Act as the uniform fiduciary standard of conduct. SIFMA likewise opposes any approach that would extend the existing rules, case law, guidance and other legal precedent under Section 206 of the Advisers Act standard wholesale to broker-dealers.[21]

B. The Adverse Implications of Imposing the Advisers Act on Broker-Dealers

The viability of a uniform standard is predicated upon a new articulation of the standard of conduct for investment advisers and broker-dealers, because wholesale extension of the Advisers Act standard to broker-dealers is unworkable and inconsistent with the purposes of Section 913 of the Dodd-Frank Act, investor protection, and the broker-dealer business model.

1. The Advisers Act was not designed to regulate broker-dealer activity. The Advisers Act was not intended or designed to apply to the incidental advice offered by broker-dealers,[22] and the interpretations that have been given under that Act have not taken into account broker-dealer roles.

In passing the Dodd-Frank Act, Congress could have simply eliminated the broker-dealer exception to the Advisers Act definition of "investment adviser" and applied to both broker-dealers and investment advisers the general fiduciary duty implied under the Advisers Act. Congress affirmatively elected *not* to do so.[23] Thus, Congress recognized that the uniform fiduciary standard should "appropriately adapt to the differences between broker-dealers and registered investment advisers."[24]

2. The case law regarding the fiduciary duty of investment advisers was developed in the context of a business model which is inapplicable to broker-dealers. There are very

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[21] *See, e.g.*, SIFMA Section 913 Comment Letter; and SIFMA comment letter on FINRA Regulatory Notice 10-54 (Dec. 2010), available at http://www.sifma.org/Issues/item.aspx?id=22482 ("**SIFMA RN 10-54 Comment Letter**").

[22] The definition of "investment adviser" in the Advisers Act specifically excludes "any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor." Section 202(a)(11) of the Advisers Act.

[23] *See* Restoring American Financial Stability Act of 2009, S. ___, 111th Cong. § 913 (discussion draft as proposed by Senator Dodd, Chairman, Senate Comm. on Banking, Hous., & Urban Affairs, Nov. 10, 2009), *available at* http://banking.senate.gov/public/_files/AYO09D44_xml.pdf. *See also* Frank Letter at p. 1.

[24] Frank Letter at p. 1.

few federal fiduciary cases brought against investment advisers. A primary reason is that customers cannot sue their advisers for breach of their fiduciary duty under Section 206 of the Advisers Act.[25] The few existing case law precedents apply to a different business model, and speak only in very general, high-level and vague terms about the fiduciary standard and what is required to satisfy it. Yet, if the fiduciary duty applicable to investment advisers is simply overlaid onto broker-dealers, these same precedents could easily be misinterpreted and misapplied – by courts and regulators alike – in any number of ways that would disadvantage and undermine the broker-dealer business model, and without a corresponding benefit to retail customers.[26]

3. <u>SEC staff statements regarding the fiduciary duty of investment advisers under the Advisers Act are not readily translatable to broker-dealers.</u> Over the years, the SEC staff has issued guidance regarding the fiduciary duty of investment advisers under Section 206 of the Advisers Act. These statements speak far more in terms of entirely avoiding conflicts, rather than appropriately managing them.[27] Accordingly, these statements

[25] *Transamerica Mortg. Advisors v. Lewis*, 444 U.S. 11 (1979). In *Transamerica*, the Court found that private plaintiffs can only sue their advisers under Section 215 of the Advisers Act, which provides that contracts made or performed in violation of the Act are void.

[26] In addition, the nationwide body of state case law on whether broker-dealers owe fiduciary duties and the scope of those duties also raises concerns, given that this body of law is so uneven and inconsistent – a point on which courts and commentators overwhelmingly agree. *See, e.g., Patsos v. First Albany Corp.*, 741 N.E.2d 841, 848-51 (Mass. 2001) ("Courts in other States have not been of single mind whether fiduciary duties inhere in every relationship between a stockbroker and his customer."); *Johnson v. John Hancock Funds*, 217 S.W.3d 414, 428 (Tenn. Ct. App. 2006) ("The courts have not been of a single mind whether fiduciary duties inhere in every relationship between a stock broker or investment advisor and his or her client"). *See also* discussion and cases cited in the following five scholarly works: (i) Arthur B. Laby, *Fiduciary Obligations of Broker-Dealers and Investment Advisers*, 55 Vill. L. Rev. 701 (2010) ("This sliver of securities law doctrine comprises a bewildering inconsistency of judicial decisions."); (ii) Steven A. Ramirez, *The Professional Obligations of Securities Brokers Under Federal Law: An Antidote for Bubbles?*, 70 U. Cin. L. Rev. 527 (2002) (describing division in state courts regarding fiduciary obligations of broker-dealers); (iii) Cheryl Goss Weiss, *A Review of the Historic Foundations of Broker-Dealer Liability for Breach of Fiduciary Duty*, 23 Iowa J. Corp. L. 65 (1997) ("Courts have often failed to do a careful analysis of the duty, resulting in erroneous, confusing or poorly explained opinions."); (iv) Gregory A. Hicks, *Defining the Scope of Broker and Dealer Duties – Some Problems in Adjudicating the Responsibilities of Securities and Commodities Professionals*, 39 DePaul L. Rev. 709 (1990) (noting the "uncertain significance of the fiduciary label often attached to these [brokers and dealers], and an accompanying uncertainty about the legal duties which the fiduciary label implies"); and (v) Carol R. Goforth, *Stockbrokers Duties to their Customers*, 33 St. Louis U. L.J. 407 (1989) (discussing inconsistent judicial approaches to whether and when fiduciary relationship arises between broker and customer).

[27] *See, e.g.,* Release No. IA-3060, File No. S7-10-00 ("An adviser must … seek to avoid conflicts with its client…."); Information for newly-registered investment advisers, available at

could be interpreted and applied in a manner more proscriptive than the "eliminate or disclose conflicts" approach recommended in the Study.[28] If such guidance were applied to broker-dealers under the uniform fiduciary standard of conduct, it would create legal and compliance uncertainty (described in greater detail below) that would in the worst case prevent, and in the best case disincentivize, broker-dealers from offering many of the beneficial products and services that they currently provide and that retail customers have come to value and rely upon.

4. <u>The inability to gauge compliance with, or legal exposure under, the Advisers Act standard would undermine the broker-dealer business model.</u> The Advisers Act standard does not provide necessary guidance regarding, for example, what disclosures will be adjudged complete and how and when consents must be obtained, when a broker-dealer provides advice involving principal trades, structured products, receipt of commissions and differential loads for different products. Nor does it provide necessary guidance regarding when the fiduciary duty begins and ends, or how it applies in the context of, for example, hybrid accounts or complex investment strategies, such as concentrated positions which may in many instances be at the customer's request.

Absent new rules and guidance – issued under Section 211 of the Advisers Act and Section 15 of the Exchange Act, as authorized by the Dodd-Frank Act – to enable broker-dealers to apply the fiduciary standard to their distinct operational models, broker-dealers cannot adequately supervise or gauge their compliance with the standard, nor can they manage litigation risks. Moreover, as noted above, customers cannot sue their advisers for breach of their fiduciary duty under Section 206 of the Advisers Act.[29] Thus, application of the Advisers Act standard to broker-dealers would subject broker-dealers to the unfair and unharmonized (and likely Congressionally unintended) consequence that retail customers could sue their broker-dealers, but not their investment advisers, for breach of the "uniform" fiduciary standard. Under circumstances where the business and legal risks are unmanageable, broker-dealers will withdraw from offering the affected products and services, which would disserve the interests of retail customers.

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http://sec.gov/divisions/investment/advoverview.htm ("You should not engage in any activity in conflict with the interest of any client…"); *In re Terence Michael Coxon*, Release ID-140 (Apr. 1, 1999) ("A fiduciary must therefore refrain from putting himself in a position of conflict of interest…"); *In re Monetta Financial Services, Inc.*, Release No. ID-162 (Mar. 27, 2000) (same); SEC No-Action Letter, National Deferred Compensation, Inc. (Aug. 31, 1987) ("An adviser may not fulfill its fiduciary obligations if it … imposes an additional fee on a client for choosing to change his investment").

[28] Study at p. vii.

[29] *Transamerica Mortg. Advisors v. Lewis*, 444 U.S. 11 (1979).

5. Empirical study shows that wholesale application of the Advisers Act duty to broker-dealers would negatively impact choice, product access, and affordability of customer services.[30]

a. **Choice**. Notwithstanding the Dodd-Frank Act provision stating that commission-based compensation alone would not violate the uniform fiduciary standard, undifferentiated application of existing Advisers Act case law, guidance and other precedents to broker-dealers could result in reduced access to brokerage accounts, given the potential conflicts that could arise from charging commissions. Commission-based brokerage accounts are overwhelmingly the preferred model for retail customers, with only 5% of households preferring the fee-based advisory platform. This is true across all wealth segments, but particularly for smaller investors with less than $250,000 in assets. For smaller investors, or those with more limited trading activity, a commission-based brokerage account is likely to be the more economical choice.

b. **Product access**. Undifferentiated application of existing Advisers Act case law, guidance and other precedents to broker-dealers could result in reduced access to products distributed primarily through broker-dealers. Given their inherent (though generally accepted and well-managed) conflicts, broker-dealers may not be able to continue to act as principal and sell proprietary products, including: sales of underwritten offerings (*e.g.*, IPOs); providing retail customers liquidity through market making and principal trading, including access to fixed-income products (*e.g.*, municipal and corporate bonds, which represent approximately 15% of assets held by retail customers); and sales of proprietary and affiliated products (notwithstanding the Dodd-Frank Act provision stating that such sales alone would not violate the uniform fiduciary standard).

c. **Affordability of advisory services**. Undifferentiated application of existing Advisers Act case law, guidance and other precedents to broker-dealers could result in reduced access of broker-dealer customers to investment options with fee structures adaptable to their needs, as well as the imposition of increased compliance, disclosure and surveillance costs, which would disproportionately impact small investors.

For these reasons, the Advisers Act standard is unworkable for broker-dealers. It would result in unfair treatment of broker-dealers vis-a-vis investment advisers, is inconsistent with the principles of investor protection (and likely Congressional intent), and would result in decreased access to products and services for retail customers. For a uniform

[30] *See* SIFMA/Oliver Wyman study (Oct. 2010), available at http://www.sifma.org/Issues/item.aspx?id=21999. The SEC has also acknowledged the negative consequences of imposing the requirements of the Advisers Act, which include an adverse impact on retail investor choice of products and services, and how investors pay for those products and services. *See* Study at pp. 139-143.

standard of conduct to work without fundamentally disrupting the broker-dealer business model, it must employ a new articulation of the standard of conduct.

III. The Framework for Rulemaking

A. Overview

We offer below a framework for a newly articulated fiduciary standard of conduct to inform the Commission's rulemaking process. We believe that a standard guided by these principles, adapted to the substantially different operating models for broker-dealers and investment advisers, is the best approach for protecting investors and preserving investor choice and access to cost-effective financial products and services.

B. The Standard

The Commission's rulemaking under Section 913 shall "provide that the standard of conduct for all brokers, dealers, and investment advisers, when providing personalized investment advice about securities to retail customers… shall be to act in the best interest of the customer…." Material conflicts of interest should be disclosed and may be consented to by the customer. Section 913 also provides that the newly articulated standard must be no less stringent than Sections 206(1) and (2) of the Advisers Act, and is not constrained by the principal transactions restrictions of Section 206(3) of the Advisers Act.

As explained in the Executive Summary, under our proposed framework, the general fiduciary duty implied under Section 206, which derives from the traditional, generally understood and accepted common law, would be newly articulated as the uniform standard.[31] Under Section 211 of the Advisers Act and Section 15 of the Exchange Act (as authorized by the Dodd-Frank Act), the SEC would issue rules and guidance to provide the detail, structure and guidance necessary to enable broker-dealers to apply the fiduciary standard to their distinct operational model. In addition, while many parallels would occur, existing Section 206 investment adviser case law, guidance, and other legal precedent would continue to apply to investment advisers, but would *not* likewise apply wholesale to broker-dealers, in recognition that broker-

[31] In the Executive Summary, we noted that our proposed approach is consistent with that historically followed in agency and trust contexts. We also note that it is not unprecedented for a federal regulator to borrow and restate standards applicable to one group of financial services professionals in order to promote clarity and transparency in regulations applicable to a different set of financial services professionals. For example, the Department of Labor ("**DOL**"), rather than requiring bank collective funds to complete SEC Form N-1A, extracted the elements of certain calculations set forth in the Form and incorporated them into a DOL regulation. *See* 29 CFR Part 2550, Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans, 75 Fed. Reg. 64910 at 64940 (October 20, 2010), available at http://webapps.dol.gov/FederalRegister/PdfDisplay.aspx?DocId=24323.

dealers provide a different range of products and services, and operate under a distinct operational model.

C. Rulemaking Principles to Implement Dodd-Frank Act Section 913

Commission rulemaking to articulate the uniform standard of conduct must provide retail customers with tangible protections and affordable choices, while maintaining sufficient flexibility to accommodate distinct operational models for financial service providers. To facilitate the Commission's rulemaking under Section 913 of the Dodd-Frank Act, we recommend that the following key principles be addressed:[32]

1. Enunciate the core principles of the uniform fiduciary standard of conduct. SEC rulemaking should clearly enunciate the core principles that underpin the uniform standard applicable to all brokers, dealers, and investment advisers. First, the standard for all brokers, dealers, and investment advisers, when providing personalized investment advice about securities to retail customers, should be to act in the best interest of the customer.[33] Second, the standard should be no less stringent than the standard applicable to investment advisers under Sections 206(1) and (2) of the Advisers Act.[34] Third, material conflicts of interest should be disclosed and may be consented to by the customer.[35] Finally, consistent with Section 913, unless otherwise agreed with the customer, a broker or dealer or registered representative should not have a continuing duty of care to the customer after providing personalized investment advice about securities.[36]

2. Articulate the scope of obligations under the uniform fiduciary standard of conduct. SEC rulemaking should articulate the scope of a broker-dealer's obligations under the uniform standard of conduct. For example:

a. **Commencement of the standard of conduct**. The standard of conduct should commence when the customer agreement is signed by the customer (or, if earlier, upon the making of trades based on personalized investment advice about securities) and should apply only when providing personalized investment advice about securities to retail customers. Introductory discussions regarding the *nature of the relationship* would not be subject to the standard of conduct. Broker-dealers and investment advisers may discuss

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[32] It is critical that the Commission provide for a reasonable phase-in period for the new rules, to facilitate the transition for broker-dealers and thus for their retail customers.

[33] Derived from the explicit language of Section 913 of the Dodd-Frank Act.

[34] *Id.*

[35] *Id.*

[36] *Id.*

the different types of relationships available with a potential client without the standard of conduct applying to these discussions.

b. **Shape of the standard of conduct**. A broker-dealer's obligations to a retail customer under the standard of conduct should be specified in the customer agreement. The obligations may be crafted to reflect the specific agreement and objectives of the parties. For example, the customer agreement might specify that the broker-dealer's obligations do not extend beyond the particular sale, or might address the broker-dealer's obligations in the case of "hybrid" accounts; or the obligations may appropriately be limited to assets over which the broker-dealer has been given discretionary authority, specific recommendations about securities that are available through the broker-dealer, or such other limitations and disclosures to which the customer agrees.[37]

c. **Application of the standard of conduct to an account**. The uniform fiduciary standard of conduct should apply on an account-by-account basis, when providing personalized investment advice about securities, pursuant to the written customer agreement. Application on an account basis is consistent with they way firms currently enter into agreements with customers, and document customer relationships. Application on an account basis is also consistent with broker-dealers' records requirements to document investment objectives on an account basis.

d. **Inclusion of traditional product sales or compensation**. Traditional types of broker-dealer product sales or compensation arrangements should not be viewed to violate the standard of conduct. For example, the sale of proprietary-only, or other limited range of products, should not violate the standard, as applied to a broker or dealer, provided there is appropriate disclosure to and possibly consent by the customer, and the fiduciary ('best interest of the customer') standard is otherwise satisfied.[38] In addition, receipt of compensation based on commissions or other fees or standard forms of compensation including, without limitation, annual marketing or distribution fees on mutual funds, revenue sharing or shareholder accounting, should not violate the standard of conduct with appropriate customer disclosure.[39]

The SEC might consider "scenario planning" as part of the rulemaking process so that it can comprehensively examine, taking a bottom-up approach, the areas of particular concern to broker-dealers (e.g., advice involving principal trades, structured products,

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[37] There is, of course, a mandatory core to the fiduciary duty that cannot be overridden by agreement. For example, the principal cannot authorize the fiduciary to act in bad faith. The fiduciary must always act in good faith and deal fairly with and for the principal. *See* Sitkoff, 91 B.U. Law Rev. at 1046.

[38] *Id.*

[39] *Id.*

hybrid accounts, complex investment strategies, concentrated positions, and receipt of commissions and differential loads for different products). The SEC should provide the necessary rule-based guidance regarding when the fiduciary duty begins and ends and what disclosures and consents, if any, are necessary to satisfy the duty, and otherwise address how broker-dealers can satisfy the uniform fiduciary standard of conduct under these various scenarios.

3. Define "personalized investment advice." The standard of conduct applies only "when providing personalized investment advice about securities to retail customers." Thus, SEC rules should define with specificity which business activities fall within, and which remain outside, the scope of "personalized investment advice."[40]

A general definition might provide that "personalized investment advice" about securities means investment recommendations about securities that are provided to address the objectives or needs of a specific retail customer after taking into account the retail customer's specific circumstances.[41]

SEC rules should also provide specific guidance on personalized investment advice. For example, personalized investment advice about securities should include:[42]

- communications to a specific customer recommending that the customer purchase or sell one or more securities;
- communications about securities to one or more targeted customers encouraging the particular customers to purchase or sell a security;
- technology that analyzes a customer's financial or online activity and sends specific investment suggestions that the customer buy or sell a security;[43] and

[40] SEC rules should likewise adequately define the term "retail customer" to appropriately limit the scope of the new standard to, for example, natural persons that do not meet the "Qualified Institutional Buyer," or QIB, threshold.

[41] Derived from p. 125 of the Study.

[42] Derived from p. 124 of the Study.

[43] NASD Notice to Members 01-23, "Online Suitability" ("**NTM 01-23**"). NTM 01-23, however, also cites several examples of electronic applications that would fall outside the definition of "recommendation" and thus, in our view, should also fall outside the definition of personalized investment advice.

- discretionary decisions regarding securities bought, sold, or exchanged by the person or firm exercising investment discretion.

Personalized investment advice about securities should *not* include: [44]

- providing general research and strategy literature;
- discussing general investment and allocation strategies;
- seminar content that is not specific to a customer;
- general marketing and education materials that are not specific to a customer;
- financial planning tools and calculators that use customer information but do not recommend specific securities;
- broker-dealer investing web sites where retail customers use tools to analyze securities to make self-directed investment decisions;
- holding securities, including concentrated positions, or other complex or risky investment strategies, at the customers' request in a nondiscretionary account;
- taking and executing unsolicited customer orders;
- account and customer relationship maintenance (*e.g.*, periodic contact to remind customers to rebalance assets to match allocations previously established, absent efforts to recommend changes to the allocation percentages);
- needs analysis (*e.g.*, meetings to determine customers' current and any new investment objectives and financial needs);
- providing ancillary account features and services (*e.g.*, debit card, cash sweep, and margin lending);
- market making, absent efforts to recommend the traded securities;
- underwriting, absent efforts to recommend the underwritten security;

[44] Derived generally from p. 126 of the Study, and Section 913 of the Dodd-Frank Act.

- referring customers to affiliated or third-party providers of financial or financial related services; or

- use of social media to convey investment strategies to a broad audience.

4. Provide clear guidance regarding disclosure that would satisfy the uniform fiduciary standard of conduct. Adequate disclosure guidance should be in place on or before the date the Section 913 standard of conduct becomes operative. Otherwise, broker-dealers cannot reasonably be expected to comply with or manage liability risks under the uniform fiduciary standard.

Establishment of clear guidelines regarding what disclosure is adequate and reasonable is particularly pressing for broker-dealers, whose activities involve conflicts that have not previously been subject to a "customer best interest" standard of conduct. Without clear guidelines, broker-dealers face the unquantifiable risk of courts and arbitrators second-guessing the adequacy of their disclosure of these conflicts on a post-hoc basis, and ultimately holding them liable as guarantors of their products or services based on inadequate disclosure or consent. This, in turn, creates the very real risk that broker-dealers would withdraw from offering many products and services, many of which are helpful to investors who wish to develop portfolios tailored to their needs and tolerance for risk.

a. ***Prospective guidance on disclosure should incorporate the following principles***:[45]

i. ***Clear disclosure***. Section 913 of the Dodd-Frank Act requires "simple and clear disclosures to investors…."[46] Retail customers will benefit from disclosure that is concise, direct, and in plain English.

ii. ***A layered approach***. Detail can overwhelm key facts. A layered approach to disclosure should be used to provide retail customers with the clearest, most relevant information at the time it is most important to their decision making, and therefore most likely to be read, with greater detail simultaneously made available to the customer if desired. For example, broker-dealers and investment advisers could provide printed materials applicable to all retail customers at the time of account opening, with more detailed disclosures that are relevant to particular transactions available on the internet.

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[45] These principles were also set forth in the SIFMA RN 10-54 Comment Letter.

[46] Section 913(g) of the Dodd-Frank Act.

iii. ***Web-based disclosure***.[47] Web-based disclosure is an effective manner to make immediate information available to many customers at a time that is most relevant to their investment decisions. It is also well adapted to providing layered disclosure that provides supplemental information to customers at the level of detail they desire.[48] Web-based information is also always available, while paper disclosures are easily discarded and easily forgotten. Of course, paper disclosures should be provided to customers that lack effective Internet access or that otherwise so request.

b. ***Specific disclosure guidance would address the following areas***:

i. ***Prospective customers***. Web-based disclosures should accompany web-based marketing materials for prospective customers that have had direct contact with a broker-dealer.

ii. ***Account opening***. Disclosures should include:

- the type of relationships available from the broker-dealer or investment adviser, and the scope of the standard of conduct that would apply to those relationships;

- the services that would be provided as part of the relationships, and information about applicable fees;

- material potential conflicts of interest that apply to these relationships, including conflicts arising from compensation

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[47] SIFMA has been a consistent advocate of the benefits of web-based disclosure for over five years. *See*, *e.g.*, Letter from George R. Kramer, Vice President and Acting General Counsel, Securities Industry Association, to, Jonathan G. Katz, Secretary, SEC (April 12, 2004) (comments on proposed point of sale disclosure requirements for transactions in certain mutual funds), *available at* http://www.sec.gov/rules/proposed/s70604/sia041204.pdf; Letter from Elizabeth Varley, SIFMA, to Department of Labor (July 24, 2007) (comments on request for information regarding fee and expense disclosures to participants in individual account plans), *available at* http://www.sifma.org/issues/item.aspx?id=232; Letter from Ira D. Hammerman, Senior Managing Director and General Counsel, SIFMA, to, Kim Allen, International Organization of Securities Commissions (Oct 2, 2008), *available at* http://www.sifma.org/issues/item.aspx?id=355 (comments on IOSCO's point of sale disclosure issues paper).

[48] For example, where the customer has the ability to effectively access documents furnished in electronic form, a "notice and access" delivery option should be available, whereby the firm posts material on its internet website and sends a notice to the customer that the materials are available online. The SEC successfully followed this approach in the E-proxy rules. See http://www.sec.gov/rules/final/2010/33-9108.pdf.

arrangements, proprietary products, underwritten new issues, types of principal transactions,[49] and customer consents thereto;

- the availability of many products under other fee structures and from other providers;

- disclosure and consents regarding any aggressive or sophisticated investment strategy, including concentrated positions; and

- disclosures of the background of the firm and of its associated persons, building upon existing systems, such as FINRA's BrokerCheck database.

iii. ***Point-of-sale***. If applicable, in appropriate circumstances, disclosures might include: the nature of the product; the nature of the fees involved; and the specific conflicts of interest applicable to that product. The regime should be sufficiently flexible to allow for verbal disclosures with further details made available via confirmation or online information.

iv. ***Disclosure updates***. Updates, if necessary or appropriate, should be permitted through an annual notification that provides a website address where specific changes to a firm's disclosure are highlighted.

v. ***Consents, generally***. Guidance should be provided to clarify when a customer's affirmative consent is required and when it is not.[50] When it is required, the rules should facilitate obtaining customer consent, including, in appropriate circumstances, through global consents granted at account opening. In general, the consent regime should focus particular attention on ensuring that it can be practically implemented and readily integrated into the current broker-dealer operational model.[51]

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[49] In omitting any reference to Section 206(3) of the Advisers Act in the legislative language of Section 913 of the Dodd-Frank Act, the Congressional intent was to preserve for broker-dealers the ability to engage in principal transactions under the uniform standard of conduct. Accordingly, SEC rules should affirmatively provide this relief for broker-dealers. See further discussion on principal transactions in Section III.C.5. *infra*.

[50] Section 913 of the Dodd-Frank Act does not appear to contemplate consent in every instance. *See* Section 913(g)(1) ("…conflicts of interest shall be disclosed and may be consented to by the customer.").

[51] For example, as our industry has long argued, the Advisers Act framework for consent to principal transactions would be unworkable for broker-dealers. See further discussion on principal transactions in Section III.C.5. *infra*.

vi. ***Consents from existing customers***.[52] Guidance should be given that would allow customers with accounts established prior to the effective date of the uniform fiduciary standard to consent to disclosures of conflicts by continuing to accept or use account services after receiving written disclosures.

Because customers often do not provide affirmative responses even to repeated requests from broker-dealers, requiring written consent to conflicts from existing retail customers would risk an interruption of services for these customers until the new account arrangements were in place.

For existing retail customers, consent by continuing to accept or use account services after disclosure should be permitted due to the impracticability of obtaining signatures from all existing retail customers.

5. Preserve principal transactions. In omitting any reference to Section 206(3) of the Advisers Act in the legislative language of Section 913 of the Dodd-Frank Act, Congress intended to preserve for broker-dealers the ability to engage in principal transactions under the uniform fiduciary standard of conduct. Accordingly, new SEC rules should affirmatively provide this relief for broker-dealers. One possible formulation is as follows:

A broker-dealer may, acting as principal for his own account, sell any security to or purchase any security from a customer, or acting as broker for a person other than such customer, effect any sale or purchase of any security for the account of such customer, if (A) such broker or dealer is not acting as an investment adviser in relation to such transactions; or (B) the customer has consented in writing prospectively authorizing the broker or dealer to act in any such capacity after receiving disclosure of material conflicts of interest that the broker or dealer may have and the compensation or ranges of compensation the broker or dealer may receive in such transactions.[53]

IV. Conclusion

SIFMA supports the Commission as it undertakes to address various, interrelated investor protection concerns. We urge the Commission to newly articulate a uniform fiduciary standard of conduct, rather than attempting to apply Section 206 legal precedent to the broker-dealer business model with significant negative effects for investor protection and choice. By adhering to the principles outlined above, and the additional principles noted in our prior comment letters, the Commission can develop a regulatory structure for the uniform fiduciary standard of conduct that ensures that investors are protected and are able to access the financial services they want and need to achieve their investment goals.

[52] This point was also made in the SIFMA Section 913 Comment Letter.

[53] Modeled after the language of Section 206(3) of the Advisers Act.

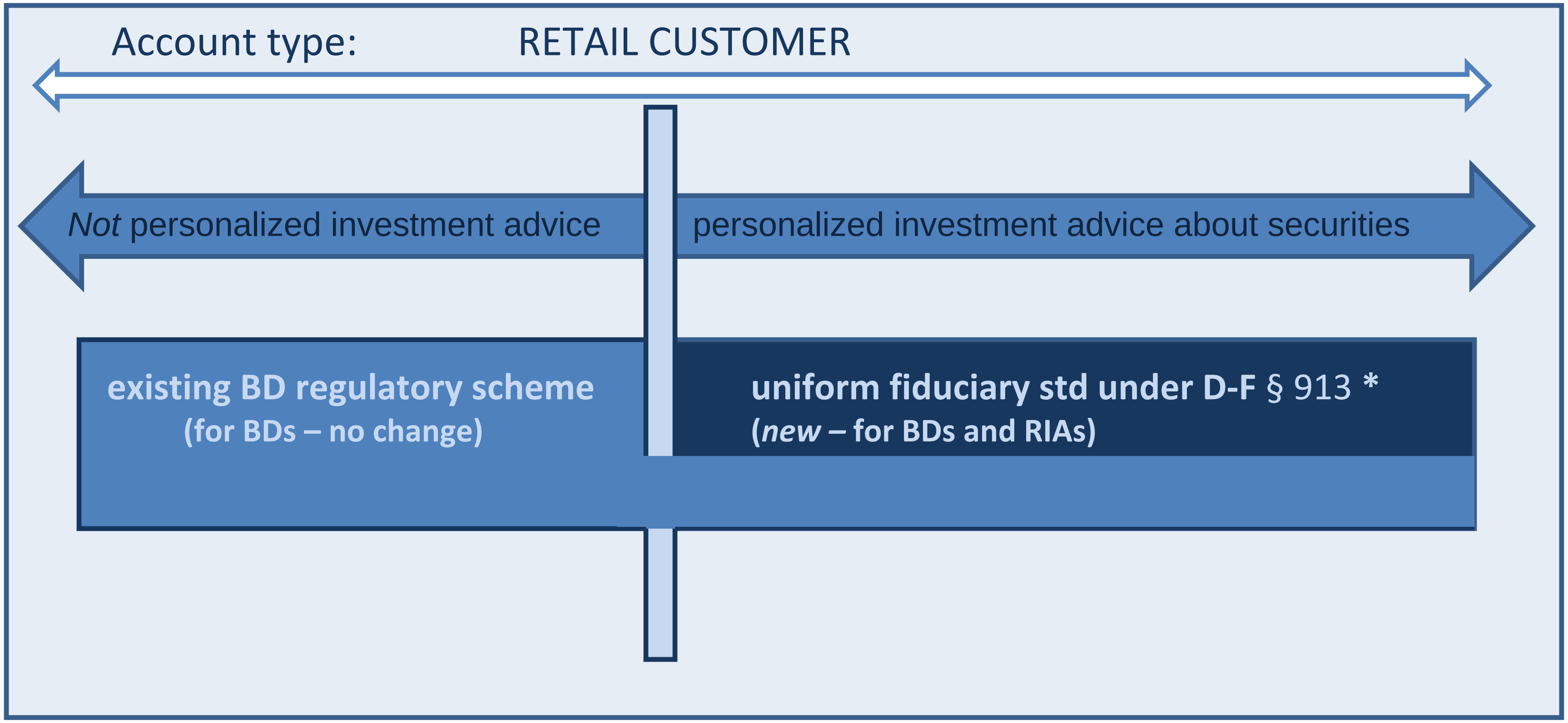
We hope we can continue to serve as a constructive and insightful voice of the securities industry during the course of what we expect will be a significant undertaking and multi-step process.

Sincerely yours,

Ira D. Hammerman
Senior Managing Director
and General Counsel

cc: Luis A. Aguilar, Commissioner
Kathleen L. Casey, Commissioner
Troy A. Paredes, Commissioner
Elisse B. Walter, Commissioner
Robert W. Cook, Director, Division of Trading and Markets
Eileen P. Rominger, Director, Division of Investment Management
Jennifer B. McHugh, Senior Advisor to the Chairman
Rule-comments@sec.gov

Appendix 1: Framework for Implementing D-F § 913



* The SEC would issue rules & guidance under § 211 of the Advisers Act and § 15 of the Exchange Act to provide the detail & guidance necessary to enable BDs and RIAs to apply the uniform fiduciary standard to their distinct operational models.

The rules would also articulate the general fiduciary duty implied under § 206 of the Advisers Act as the uniform fiduciary standard of conduct to apply equally to BDs and RIAs when providing personalized investment advice about securities to retail customers.

Existing case law & guidance under § 206 would continue to apply to RIAs, but not to BDs, because § 206 does not now, and would not under the uniform fiduciary standard, apply to BDs.

United States House of Representatives
Committee on Financial Services

"TRUTH IN TESTIMONY" DISCLOSURE FORM

Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name:	2. Organization or organizations you are representing:
JOHN G. TAFT	RBC WEALTH MANAGEMT
3. Business Address and telephone number:	
[redacted]	
4. Have you received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?	5. Have any of the organizations you are representing received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?
☐ Yes ☒ No	☐ Yes ☒ No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.	
7. Signature:	

Please attach a copy of this form to your written testimony.