

SECURITIES LAW ALERT

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SEC Staff Study Recommends Adoption Of Uniform Fiduciary Standard For Broker-Dealers And Investment Advisers

The staff of the Securities and Exchange Commission (“SEC”) has just issued its study pursuant to Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act for the purpose of evaluating whether the SEC should adopt a uniform standard of care for the provision of personalized investment advice and recommendations about securities to retail customers (the “Study”). This Alert summarizes some of the key recommendations made by the Staff.

The Study, released on January 21, 2011, recommends that the SEC propose rules “that would apply expressly and uniformly to both broker-dealers and investment advisers, when providing personalized investment advice about securities to retail customers, a fiduciary standard no less stringent than currently applied to investment advisers under [Sections 206(1) and (2) of the Investment Advisers Act (the “Advisers Act”).]” Study at 108. Specifically, the Staff recommends that the SEC promulgate rules to provide that:

The standard of conduct for all brokers, dealers, and investment advisers, when providing personalized investment advice about securities to retail customers (and such other customers as the [SEC] may by rule provide), shall be to 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.

Id. at 109. The proposed standard would be known as the “uniform fiduciary standard.” *Id.*

The Staff interprets the uniform fiduciary standard “to include at a minimum, the duties of loyalty and care as interpreted and developed under Sections 206(1) and (2) of the Advisers Act.” *Id.* at 110-11. The duty of loyalty component of the uniform fiduciary standard “would require an investment adviser or broker-dealer to eliminate, or provide full and fair disclosure about its material conflicts of interest.” *Id.* at 112-13. In this regard, the Staff recommended that the SEC “consider developing a uniform approach to disclosure that would provide retail customers of both broker-dealers and investment advisers with relevant key pieces of information at the outset of the advisory or brokerage relationship and at appropriate times thereafter.” *Id.* at 116. The Staff also recommended that the SEC “explore the utility and feasibility of a summary disclosure document that would describe in clear, summary form, a firm’s services (including the extent to which its advice is limited in time or is continuous and ongoing), charges, and conflicts of interest.” *Id.* To address the concern raised by some commenters that investment advisers and broker-dealers “might seek to ‘disclose away’ conflicts of interest....,” the Staff observed that the SEC “could consider whether rulemaking would be appropriate to prohibit certain conflicts, or where it might be appropriate to impose specific disclosure and consent requirements (*e.g.*, in writing and in a specific format, and at a specific time) in order to better assure that retail customers were fully informed

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and can understand any material conflicts.” *Id.* at 117. With respect to principal trades by broker-dealers, the Study notes that such trades “raise the same potential conflicts of interest as such trades by investment advisers and thus implicate the duty of loyalty included in the uniform fiduciary standard.” *Id.* at 120. The Staff thus recommended that “a broker-dealer should be required, at a minimum, to disclose its conflicts of interest related to principal transactions, including its capacity as principal, but it would not necessarily be required to follow the specific notice and consent procedures of [Section 206(3) of the Advisers Act].” *Id.* The Study notes that “when engaging in principal transactions, broker-dealers would remain subject to obligations relating to suitability, best execution, and fair and reasonable pricing and compensation.” *Id.* The Staff recommended that the SEC “address through guidance or rulemaking how broker-dealers would fulfill the uniform fiduciary standard when engaging in principal trades.” *Id.* at 120. As to the details of how the uniform fiduciary standard would be implemented, the Staff commented that the standard “would require broker-dealers and investment advisers provide sufficiently specific facts so that investors are able to understand the conflicts of interest.” *Id.* Regarding the format of such disclosure, the Staff believes “requests for consents embedded in voluminous advisory agreements or other account opening agreements would impede the provision of such consent. *Id.*

Insofar as the duty of care component of the uniform fiduciary standard is concerned, the Staff recommends that the SEC “specify the minimum professional obligations of investment advisers and brokers-dealers under the duty of care.” *Id.* at 122. In this regard, the Study notes that “it could be useful to develop rules and guidance on the minimum requirements that are fundamental to a duty of care under the uniform fiduciary standard.” *Id.* at 123. The Study further notes that “[m]inimum baseline professionalism standards could include, for example, specifying what basis a broker-dealer or investment adviser should have in making a recommendation to a retail customer.” *Id.* The Staff further recommends that the SEC “engage in rule-making and/or issue interpretative guidance to define and/or interpret ‘personalized investment advice about securities’ to provide clarity to broker-dealers, investment advisers, and retail investors.” *Id.* at 127. The Study recommends that such definition “**at a minimum** should encompass the making of a ‘recommendation,’ as developed under applicable broker-dealer regulation, and should not include ‘impersonal investment advice’ as developed under the Advisers Act.” *Id.* (emphasis added).

The Study is available at: <http://www.sec.gov/news/studies/2011/913studyfinal.pdf>. ■

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