Consumer Federation of America

October 3, 2017

The Honorable Jay Clayton
Chairman
Securities and Exchange Commission
100 F Street, N.E.
Washington D.C. 20549-1090

Dear Chairman Clayton:

As you are doubtless aware, a number of industry groups opposed to the Department of Labor's fiduciary rule have suggested that the rule is causing brokerage firms to shift investors into fee accounts where they face higher costs than they would have in a commission account. Indeed, this argument has featured prominently in letters responding to your request for input on the appropriate standard of conduct for broker-dealers and investment advisers from industry groups, such as SIFMA and ICI, that are urging the Commission to adopt a less rigorous standard than that adopted by DOL for retirement accounts. If true, however, these arguments provide evidence, not of problems with the DOL rule itself, but of a failure of enforcement by DOL, the SEC, and FINRA.

There are good reasons to dismiss these arguments as nothing more than the misleading rhetoric of industry groups intent on watering down the DOL rule's strong investor protections. After all, those making the claim exaggerate the role of the Department's fiduciary rule in prompting a migration to fee accounts that is several decades old, ignore evidence that most firms have chosen to continue offering commission accounts as an option under the rule, and provide no evidence that retirement investors who are moved to fee accounts are worse off as a result. On the contrary, they both exaggerate the supposed cost advantage of commission accounts and fail to consider the significant benefits of fee accounts for many investors.[1] Despite our skepticism, however, we cannot dismiss out of hand the possibility that *some* firms are using the rule as an excuse to shift customers into fee accounts, even when that is not the best option for the investor, or charging them unreasonable fees as a result. If this is occurring, then the Commission has an important role to play in preventing this misconduct.

It has long been Commission policy that securities firms that offer both fee and commission accounts must recommend the type of account that is best for the customer. Given that most brokerage firms have chosen to continue to offer commission retirement accounts as an

[1] Letter from Barbara Roper and Micah Hauptman, CFA, to the DOL, April 17, 2017, at 71-75, http://bit.ly/2oXIZfq.

option under the DOL rule, the allegation that firms are nonetheless pushing retirement savers toward fee accounts when they would be better off in commission accounts is a serious one. For example, Fidelity stated in its recent comment letter that investors are being forced by the DOL rule to "pay an asset-based fee to receive exactly the same services that were previously provided to them for no additional fee under a transaction-based fee structure."[2] If true, and it is important to acknowledge that Fidelity has offered no evidence to support the allegation, that would suggest that investors are being forced to pay on-going fees when they would be better off paying commissions and are not receiving the on-going advice and account monitoring that would justify those fees – a clear violation of SEC standards.

As long as the fees charged are reasonable and investors receive the ongoing advice to which they are entitled in a fee account, fee accounts can offer significant benefits for many investors. That presumably explains why the Commission has, in the past, gone to considerable lengths to encourage their adoption[3] and why some of the same groups making this argument today once identified fee accounts as a "best practice" that offered broad benefits even for buy-and-hold investors.[4] It is certainly true, however, that firms may have an incentive to recommend fee accounts even for investors who would be better off in a commission account. Moreover, when it comes to determining what type of account is best for the customer, the Department of Labor's fiduciary rule has changed the equation. By imposing a best interest standard and restrictions on conflicts of interest, the rule makes commission accounts a far more attractive option than they were previously or are outside the retirement market. Firms must take that into account when weighing what option is best for the customer.

In light of brokerage firms' incentive to maximize their fee income, industry groups' claims that investors are being inappropriately shifted to fee accounts should be investigated. If verified, the Commission must act to end the practice. It should start by sending a clear message that it takes the requirement that firms recommend the type of account that is best for the investor seriously and that it is prepared to hold firms accountable for complying with this requirement. We are issuing a similar request to FINRA, and we have written to Secretary Acosta urging him to enforce both the requirement in the DOL rule that the type of account recommended be based on the best interests of the investor and the requirement that any compensation received be reasonable in light of services offered.

If there is validity to this claim, the lesson here is *not* the one industry lobbyists would have you learn – that a watered down, disclosure-based rule will be better for investors than strong protections against conflicts of interest. Rather, the clear lesson is that it will take strong restrictions on conflicts of interest, and a willingness to enforce those restrictions rigorously, to prevent firms from profiting inappropriately at their customers' expense. This is true whether the

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[2] Letter from Marc R. Bryant, Fidelity, to the SEC, August 11, 2017, at 3, http://bit.ly/2wLJSKh.

[3] *See, e.g.*, Letter from Barbara Roper, CFA, to the SEC, Certain Broker-Dealers Deemed Not To Be Investment Advisers, January 13, 2000, http://bit.ly/2eMqEhg (discussing an SEC proposal to exempt fee accounts offered by broker-dealers from regulation under the Investment Advisers Act in order to encourage adoption of fee-based compensation it viewed as better aligning the interests of brokers and their customers). *See, also,* Tully Commission, Report of the Committee on Compensation Practices, April 10, 1995, http://bit.ly/2nwNb0E.

[4] *See, e.g.*, Letter from Ira D. Hammerman, General Counsel, Securities Industry Association, to the SEC regarding Release No. IA-2273, Certain Broker-Dealers Deemed Not To Be Investment Advisers, September 22, 2004, http://bit.ly/2oxtk2w.

conflict involves the potential to maximize asset-based fees when customers would be better off in a commission account or the incentive in commission accounts to recommend investment products that pay the broker-dealer the most.

Investors who turn to financial professionals for advice should be able to trust that the advice they receive will be designed to serve their best interests. The Commission has a long way to go before it can claim to provide that assurance. In the meantime, the Commission can at least help to ensure that firms comply with their existing obligation to recommend the type of investment account that is best for the customer and not just the type of account that is most profitable for the firm.

Respectfully submitted,

Barbara Roper
Director of Investor Protection

Micah Hauptman
Financial Services Counsel

cc: The Honorable Michael Piwowar, Commissioner
The Honorable Kara Stein, Commissioner