CFA and AFR Warn: SEC's "Regulation Best Interest" Will Harm Vulnerable Investors

The Securities and Exchange Commission will vote **Wednesday, June 5** on rules governing broker-dealers and investment advisers that were supposed to improve investor protections, but don't.

Investor advocates, state securities regulators, legal experts, and fiduciary advisers all agree that the regulations the agency is set to approve are a betrayal of the "Mr. and Ms. 401(k)" investors SEC Chairman Jay Clayton pledged to protect when he undertook this rulemaking. Ordinary investors lose tens of billions of dollars each year as a result of self-interested advice from investment advisers and brokers. With this rule, the SEC is effectively sanctioning the conflicts of interest that create incentives for brokers to give self-interested advice to their clients. The drain on people's hard-earned savings will continue.

Do not be deceived by the label. The so-called "best interest" standard doesn't require brokers to do what's best for their customers. It will not require them to recommend the investments they reasonably believe are the best match for the customer, and it will not require them to consider costs except when comparing otherwise identical securities. That's why state securities regulators have warned that the proposal "subverts," rather than protects, investors' best interests.

The standard will not prevent brokers from placing their own interests ahead of their customers' interest. That requirement doesn't make it into the care, conflict, and disclosure obligations that form a compliance safe harbor. As a result, if brokers have incentives – such as the extra fees they get from steering an investor into an in-house product – that create a conflict of interest, firms do *not* have to have procedures that would resolve that conflict or prevent it from tainting their advice. That's why investor advocates have warned that the standard will mislead investors into expecting protections the rule does not deliver.

The rule will weaken protections that investors currently receive under state common law fiduciary standards. By applying the broker-dealer standard exclusively on a transaction-by-transaction basis, the rule will deprive investors of protections they currently receive under state common law fiduciary standards when they enter long-term relationships of trust and confidence with their broker. That's why one of the nation's leading experts on broker-dealer law and regulation has warned that "Reg BI offers *less protection* than is available under the current law governing a broker-dealer's duties to its customers."

Instead of strengthening the standard for brokers, the Commission has proposed a weak, disclosure-based interpretation of the Investment Advisers Act fiduciary

standard. In a dramatic weakening of the Commission's traditional interpretation of the Investment Advisers Act fiduciary duty, the Commission has suggested that investment advisers can satisfy their fiduciary obligations to clients through disclosure alone. This will formally enshrine as Commission policy its traditionally weak enforcement of that standard, making it more difficult for a future Commission to adopt a more pro-investor approach. That's why fiduciary advisers have rejected the Commission's proposed approach as too weak and ineffective to protect investors.

SEC Chairman Jay Clayton needs to hear that investors deserve, and Congress expects, much better. That's what Congress intended when it authorized the SEC to adopt a standard requiring brokers and advisers alike to act in their customers' best interests, without regard to their own conflicting interests. This package fails to live up to that fundamental standard.