INVESTMENT ADVISER
ASSOCIATION

May 10, 2010

Via Electronic Mail

Elizabeth M. Murphy
Federal Advisory Committee Management Officer
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: SEC Investor Advisory Committee May 17, 2010 Meeting (File No. 265-25-04)

Dear Ms. Murphy:

The Investment Adviser Association (IAA)[1] appreciates the opportunity to submit a written statement to the SEC Investor Advisory Committee for its public meeting on May 17, 2010. One of the items on the agenda for the meeting is a discussion of fiduciary duty in the context of investment advisers and registered broker-dealers. The IAA strongly believes that broker-dealers who provide investment advice about securities to investors should be subject to a fiduciary duty under the Investment Advisers Act of 1940 (Advisers Act). Fiduciary duty is an important protection that will make a real difference to investors. This letter briefly describes the benefits that investors receive from investment advisers that are subject to a fiduciary duty and how customers of broker-dealers would benefit from the same protections.

Investment advisers are subject to a fiduciary duty, which means that they have an affirmative duty of utmost good faith and full and fair disclosure of all material facts to their clients, as well as an affirmative obligation to employ reasonable care to avoid misleading clients. Advisers must act in the best interests of their clients and place the interests of their clients before their own.

In practical terms, fiduciary duty means that, in the course of providing advice to clients, investment advisers must disclose all material information to their clients, including the fees that they charge, how they plan to invest client assets or recommend securities to

[1] IAA is a not-for-profit association that represents the interests of investment adviser firms that are registered with the US Securities and Exchange Commission (SEC). IAA's membership consists of investment advisory firms that manage assets for a wide variety of institutional and individual clients, including pension plans, trusts, investment companies, endowments, foundations, and corporations. For more information, please visit our web site: www.investmentadviser.org.

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clients, and any material disciplinary information involving the adviser or its investment personnel. Moreover, as fiduciaries, investment advisers must treat their clients fairly and not favor one client over another, especially if an adviser would somehow benefit from favoring one particular client or type of clients.

Most importantly, whenever an adviser's interests differ from those of the client, the adviser must explain the issue to the client and act to mitigate or eliminate the issue so that the adviser can act in the interest of the client and not for his or her own benefit. Broker-dealers do not have an obligation to explain to clients that they may be motivated by their own interest in recommending a particular security. In other words, even if a broker-dealer is motivated to recommend a particular security for its own interests, the broker-dealer does not have to disclose that information and can recommend the security to the client as long as it is "suitable" or not an unreasonable investment for the client.

As fiduciaries, investment advisers, from the onset of their relationship with their clients, must tell their clients about all the arrangements in which their interests may differ from those of their clients. For example, if an investment adviser receives payment from others for recommending certain types of products, the adviser must tell the client about the compensation and how the compensation may potentially affect or influence the investment advice that is given to clients. In addition to disclosing this information to the client, the investment adviser must act to recommend securities that are in the best interest of the client regardless of the additional compensation he or she may receive.

Broker-dealers, however, do not need to give this explanation of the potential incentive to favor certain products over others as long as the investment is at least suitable for that client. Broker-dealer representatives do not have to tell their clients if they individually receive higher commission or other monetary rewards for recommending certain products and their incentive to recommend certain securities that provide them the greatest amount of compensation.

Investment advisers must make disclosures regarding conflicts created by their compensation arrangements. For example, advisers that get paid by commissions have to disclose that commission-based compensation may motivate them to trade more frequently or to recommend trading more frequently because they would receive more compensation. Under these circumstances, investment advisers also would have to act to avoid trading or recommend trading just to earn more commissions. Broker-dealers currently do not need to disclose clearly to their clients the conflicts of interest that may arise in a commission-based relationship. Therefore, broker-dealers do not need to tell their clients their potential incentive to engage in more transactions than necessary to generate higher fees for themselves.

So what would these benefits of fiduciary duty mean for customers of broker-dealers? A few examples follow:

- Brokers recommending and selling investment products to customers would have to disclose all fees, compensation, and other incentives they earn from the advice;

- Brokers would have to disclose not only information about investment products they recommend, but also information about themselves – including their conflicts of interest – that is important to customers;

- Brokers would have to recommend products that are in the best interest of their customers, and would not be able to steer customers to certain products that, while technically not inappropriate for the customer, are not in the customer's best interest;

- If a firm has an economic interest in steering clients to certain products or a broker-dealer representative can receive an extra reward for being the highest seller of a particular type of product, they must tell customers about these potential incentives for a product recommendation and refrain from making the recommendation if it is not in the best interest of the customer;

- Customers would know at the outset if a broker-dealer or its representative has a material disciplinary history (rather than having to take the initiative to look at FINRA's BrokerCheck for disciplinary information); and

- Brokers would have to offer a limited investment opportunity (as well as any other appropriate investment opportunity) to the client first and not to take the opportunity for themselves.

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Because of the overarching nature of the fiduciary duty, which requires investment advisers to place the interests of their clients before their own in every circumstance, Congress and regulators do not need to develop a comprehensive list of rules and conflicts that may exist now or in the future. Instead, advisers must be constantly on the alert for new conflicts of interest they face and disclose and mitigate those conflicts. This prevents advisers – and would prevent brokers – from being able to exploit regulatory loopholes presented by rules addressing only specific activities and conflicts. In fact, the principles-based obligations that flow from an adviser's fiduciary duty to its clients have permitted the framework to address potential issues that would have been difficult to foresee when the Advisers Act was adopted 70 years ago. The breadth and flexibility of the fiduciary duty of investment advisers have allowed the regulation of investment advisers to remain dynamic and relevant in changing business and market conditions.

Many commenters also have recognized the strength of the fiduciary principles and written in support of extending fiduciary duty to all financial professionals giving investment advice.[2]

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[2] *See, e.g.*, Jane Bryant Quinn, *Will Brokers Have to Put Your Interest First?*, janebryantquinn.com, May 6, 2010; Tara Siegel Bernard, *Trusted Adviser or Stock Pusher? Finance Bill May Not Settle It*, N.Y. Times, Mar. 3, 2010; Paul Sullivan, *Broker? Adviser? And What's the Difference*, N.Y. Times, Feb. 18, 2010; Tara Siegel Bernard, *Struggling Over a Rule for Brokers*, N.Y. Times, Feb. 16, 2010; Jason Zweig, *The Fight Over Who Will Guard Your Nest Egg,* WALL ST. J., Mar. 28, 2009.

We appreciate the opportunity to present our views to the SEC Investor Advisory Committee in anticipation of the fiduciary duty discussion at the May meeting. Please contact the undersigned, Karen L. Barr, General Counsel, or Jennifer S. Choi, Associate General Counsel, at (202) 293-4222 with any questions regarding these matters.

Respectfully submitted,

David G. Tittsworth
Executive Director

cc: Mark Anson, Chief Investment Officer, Oak Hill Investments
Jeff Brown, Senior Vice President, Legislative and Regulatory Affairs, Charles Schwab & Co., Inc.
Mercer Bullard, Founder and President of Fund Democracy, Inc. and Associate Professor of Law, University of Mississippi Law School
Hye-Won Choi, Vice President and Head of Corporate Governance for TIAA-CREF
Stephen Davis, Senior Fellow and Project Director, Yale University School for Management's Millstein Center for Corporate Governance, and nonexecutive chair of Hermes Equity Ownership Service
Abe Friedman, Managing Director, Global Head of Corporate Governance & Responsible Investment, BlackRock
Richard Hisey, President of AARP Financial Incorporated and AARP Funds
Mellody Hobson, President of Ariel Capital Management
Fred Joseph, President of the North American Securities Administrators Association and Securities Administrator for the State of Colorado
Adam Kanzer, Managing Director and General Counsel, Domini Social Investments LLC
Mark Latham, Director of Proxy Democracy, a nonprofit organization helping individual investors
Barbara Roper, Director of Investor Protection, Consumer Federation of America
Dallas Salisbury, President and CEO, Employee Benefit Research Institute
Kurt Schacht, Managing Director, CFA Institute
Damon Silvers, Associate General Counsel, AFL-CIO
Kurt Stocker, Chairman of the Individual Investors Advisory Board of the NYSE
Ann Yerger, Executive Director, Council of Institutional Investors