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The Battle Over Brokers' Duty to Their Clients Reaches a Standstill

By SARAH MORGAN

It may not be a household word, but the battle over your broker's "fiduciary" role has moved in a new direction—away, some say, from a lot of clients' best interests.

A major push by consumer advocates to hold stockbrokers to the same client-comes-first standard of care required of investment advisers—the so-called fiduciary standard—seemed close to success only a year ago. That was after a study by the Securities and Exchange Commission had called for the new rules, despite brokers arguing that dispensing advice was only a part of their business model and they shouldn't be held to the same standard as advisers in all situations.

Two Standards

Advisers and brokers offer different levels of care.

BROKERS

Must recommend "suitable" products, not necessarily best or cheapest.

Earn commissions or other transaction-based fees.

ADVISERS

Must put clients' interests before their own.

Most charge a percentage of assets or a fixed fee.

The five SEC commissioners, however, never voted to change the rules. Now, the SEC is saying it won't write any new rules until it studies how much they might cost the industry.

The shift largely is due to an unrelated case from last year, in which the U.S. Court of Appeals for the District of Columbia struck down an SEC rule on "proxy access" that would have allowed shareholder groups to put up their own proposals and board-of-directors candidates on company-distributed proxy ballots. The court said that the agency hadn't done a thorough review of the rule's potential costs.

That changed the climate for all future SEC rule making, says David Tittsworth, the executive director of the Investment Advisor Association. "The SEC doesn't want to be proposing rules that will just be struck down," he says.

Indeed, this month SEC Chairman Mary Schapiro wrote to Congress to confirm that three staff economists were studying the issue and drafting another request for data on the market for retail financial advice.

The SEC declined to comment further.

Though the fiduciary issue is hotly contested among some groups, surveys conducted on behalf of the SEC showed a majority of investors don't understand what fiduciary means, nor do they realize brokers and investment advisers offer different levels of care.

Investment advisers and financial planners typically offer year-round planning services and portfolio management. Most charge a percentage of assets, usually 1% or so for up to $1 million, but some also charge a straight hourly rate or a fixed fee for whatever help they provide.

Brokers, meanwhile, provide not only advice, but act as agents for clients in securities transactions. They are generally paid commissions or other transaction-based fees.

Under current rules, brokers only need to ensure the products they sell their clients are "suitable," and not necessarily the best possible or least expensive option. For example, a broker can sell a client a variable annuity that comes with a generous commission over a cheaper product, says Andrew Stoltmann, a Chicago-based securities lawyer who represents investors in arbitration and litigation. Advisers, on the other hand, are held to a fiduciary standard that requires them to recommend the less-pricey option, he says.

Investor advocates say new rules would be an important step forward. "It's simply good policy, wise and fair. It will give retail customers greater protection," says Harvey Goldschmid, a professor at Columbia University Law School and a former SEC commissioner.

For their part, brokers say they support the uniform fiduciary standard, but only if it is applied solely to personalized investment advice—and not when they are selling products or executing trades. "The SEC should not take a statute that applies to a different business model and apply that to the broker-dealer business," says Ira Hammerman, the general counsel for the Securities Industry and Financial Markets Association, an industry trade group.