RAND Material for FPA of Minnesota Board Meeting

> On January 3, 2008, the Securities and Exchange Commission released the much-anticipated "RAND Corporation Study on Investor and Industry Perspectives on Investment Advisers and Broker-Dealers."
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> On January 22, 2008, a teleconference concerning the RAND report was held. Attendees were Joan Rossi, Mike Shovein, Buzz Moen, Steve Carlson, and Keith Loveland. This Special Interest Group [**SIG**] reviewed the RAND report, and believes the following is true:

THE RAND MANDATE
Rand addressed two questions: What business practices exist now, and what is the consumer understanding of these business practices? In other words, RAND examined the current business practices of broker-dealers and investment advisers and explored individual investors' perceptions as to the differences between, and relationships among, the two.

RAND FINDING #1 - CONFUSION
RAND found that most investors don't understand the distinction that regulators make between advisers and broker-dealers. RAND concluded that investors fail to discern and appreciate the distinctions between investment advisers and broker-dealers — even when those distinctions are explained to them. While investors have a general sense about the differences in services provided, they were not clear about the varying legal duties of and standards imposed on each. . According to the RAND study, consumers discern absolutely no difference between the two, believing that both types of financial professionals are acting in their best interest.

RAND FINDING #2 – GENERAL SATISFACTION
According to RAND, investors indicated that they are largely satisfied with the service they've received. Among investors who rely on financial advisers, 70 percent said they were happy with the service they received, compared with 79 percent of brokerage customers. One difference: 80 percent of advisory clients said they receive a useful service, compared with only 69 percent of brokerage clients.

RAND FINDING #3 – DIFFERENT REGULATIONS
RAND found that investment advisers and brokers are regulated by two different sets of rules and may owe different legal duties to their clients; however, RAND failed to note that state common law may apply fiduciary duties to brokers if they enter into relationships based upon trust and confidence.

1. Registered investment advisers, on the one hand, are regulated under the Investment Advisers Act of 1940 and are defined as statutory fiduciaries. A fiduciary is someone who must act in the best interest of his or her client and avoid self-dealing. Financial advice given by an investment adviser must be

conflict-free or, if a conflict of interest exists, it must be fully disclosed to the client.

2. Brokers, on the other hand, are governed by the Securities Exchange Act of 1934 and are not statutory fiduciaries like investment advisers. In the context of customers and brokers, the scope of the legal duty is defined by the nature of the customer-broker relationship. A fiduciary duty often arises if the broker exercises control over the decisions of the client and for many other reasons.

NO POLICY RECOMMENDATIONS
The RAND report did not make policy recommendations to the SEC, which is considering what other regulation might be needed for broker-dealers and investment advisers; however, the report confirms that fiduciary protections for consumers are essential. Although, many believe the report de-emphasizes the duty of loyalty, which lies at the heart of fiduciary principles.

NATIONAL FPA COMMENTARY
Duane Thompson, managing director for the Financial Planning Association, said the findings suggest that SEC regulation of brokers should be more similar to those covering advisers, now that the brokerage business is geared toward offering financial advice.

Dan Moisand said, "Instead of hoping that the public can tell the difference, government should require all persons holding out as offering personal financial advice to deliver the same uniform disclosures and adhere to the same uniform fiduciary standards of care."

SIG CONCERNS
Widespread confusion exists among investors as to the core issue of fiduciary obligations.

Professionals 'holding out' as "advisors" should be held to fiduciary standards of care.

Specific conflicts of interest are permitted for brokers [e.g., proprietary products favored over non-proprietary products, advice intended to generate commissions for favored products, and principal trading, to name a few], but are forbidden for registered investment advisers.

SIG SUGGESTED ACTION STEPS
FPA of Minnesota Board should adopt a resolution expressing concern about limitations of RAND report. <u>Specifically, the de-emphasis of the **DUTY of LOYALTY**.</u>

FPA of Minnesota Board should communicate their concern and resolution to other chapters and the Financial Planning Association.

Members should be notified of the above concern and resolution at the March chapter meeting, and in Newsletter articles.

SUGGESTED RESOLUTION LANGUAGE
Whereas, the RAND Report found that investment advisers and brokers are regulated by two different set of rules and may owe different legal duties to their clients; and

Whereas, the RAND Report concluded that investors fail to discern and appreciate the distinction that regulators make between advisers and broker-dealers; and

Whereas, the RAND Report found that most investors don't understand the distinction that regulators make between advisers and broker-dealers.

Now, Therefore Be It Resolved, by the Board of Directors of the FPA of Minnesota, that the FPA of Minnesota urge the SEC, FINRA, and State Investment Adviser regulators to require all persons holding out as offering personal financial advice to deliver the same uniform disclosures and adhere to the same uniform fiduciary standards of care.

Adopted: Approved by FPAMN chapter board of directors at March 11, 2008 board meeting.