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## **“Trust Me!” Sales Talk, Advice, and Financial Planning**

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Historically securities brokers have been viewed as salespeople with special legal responsibilities: Treat customers fairly, follow special rules regarding the customers’ money and securities, and recommend to customers only suitable investments. Brokers offered liquidity by creating markets in certain securities, actions also subject to special rules designed to ensure customers were treated fairly.

Through the years, broker dealers also began to offer investment advice and financial planning. They not only collected commissions, as do pure-play brokers, but sometimes charged a percentage of the clients’ assets, as do advisers. Thus, small and large brokerage firms and banks, which have entered the fray, offer four types of services: Brokerage, dealership, advice, and financial planning.

While these four functions are differently regulated, the customers — and many of the broker-dealers-advisers-financial planners themselves — don’t know the difference. Legally, broker dealers are not subject to fiduciary duties; advisers and planners are. The difference between broker dealer regulation and fiduciary law is fundamental. Broker dealers can act for their own benefit, but must do so fairly. Advisers and financial planners must provide service solely for the benefit of their clients.

What does this difference mean in practice? A broker may offer a client securities that, while suitable for the client, may be more costly because the broker dealer received higher commissions or compensation for “pushing” the particular securities. Other securities would be better for the client, but the client never hears about them. If advisers recommend with incentive pay, they can be liable for breach of fiduciary duty, unless they make it clear to the client that they received financial or other incentives to make the

offers. Brokers are assumed to engage in “sales talk,” aimed at inducing a sale or another transaction. Advisers are assumed to give advice solely for the client’s benefit.

The two main duties of fiduciaries are to act for the sole benefit of the client (and to not act in conflict with the client’s interest) and to do their job well — the duty of care.

In light of the recent deteriorating reputation of broker dealers, it is not surprising that they would like to be called fiduciaries. They would not mind the required duty of care. After all, no adviser is a guarantor of the securities that he recommends, and the duty of care is very similar to the current duty of suitability that the broker dealers have borne for years.

The fiduciary duty of loyalty, however, is another matter. That duty would require broker dealers to disclose conflicts of interest to clients, something they would rather not have to do. For example, they would be forced to disclose that they did not complete a high school education, that they are charging clients above the maximum acceptable in the market place (more than 3% of the assets), that they are paid far more for selling one type of security and not another, that they are paid to put certain securities at the top of their list of 8,000 funds, or that they recommend certain notes as “cash” without mentioning that the notes carry some risk.

When brokers say that clients should know the risks, they are speaking as salespeople. But if they are advisers, their burden is heavier — they must have a better understanding of what they recommend and must explain it as if they were the client, or from the client’s point of view.

Even under current law, some courts will impose fiduciary duties on brokers, especially when clients have a harder time fending for themselves, such as the elderly.

Yet, the question is more fundamental: Should broker dealers who offer investment advisory services be required to give advice as fiduciaries? Should they be prohibited from having conflicts of interest when they give advice, and, if they do have a conflict, to tell their clients clearly what those conflicts are?

In the end it’s a matter of trust. If a client decides to buy the offered securities (with or without understanding what they are buying) at least the customer will know how much they can trust the offers of such broker dealers/adviser/financial planners