

## Ep. 209 - Fiduciary Rule Nearing the End? - Transcript

**Tom Mullooly:** Welcome to the Mullooly Asset Management podcast. I'm your host, Tom Mullooly, and this is episode number 209. In this podcast, we'll discuss whether the fiduciary rule is going away.

And when we talk about the fiduciary rule or fiduciary responsibility, a lot of times our clients' eyes glaze over because we are talking in somewhat legal terms, so we'll try and break this down and keep things as simple as possible.

But there are some events taking place that we think investors need to know about in 2018. This is a topic, this fiduciary rule, that we've covered before in other podcasts and in posts on our website, mullooly.net. But first a quick break and a quick word from our legal team.

**Speaker 2:** Tom Mullooly is an investment advisor representative with Mullooly Asset Management. All opinions expressed by Tom and his podcast guests are solely their own opinions and do not necessarily reflect the opinions of Mullooly Asset Management. This podcast is for informational purposes only and should not be relied upon as a basis for investment decisions. Clients of Mullooly Asset Management may maintain positions and securities discussed in this podcast.

**Tom Mullooly:** In an effort to keep things brief, I just want to quickly mention the definition of a fiduciary in the terms of investing and managing assets. A fiduciary's expected to manage the assets for the benefit of the client rather than for his or her own profit.

The fiduciary is held to what's called the prudent standard of care. That requires that a fiduciary needs to act first and foremost with the needs of the beneficiary, the client, in mind.

We know that investment advisors need to live under that umbrella of this fiduciary standard of care. Brokers, on the other hand, employees of brokerage firms, don't have the same fiduciary responsibility.

Brokers need to make sure that their investment recommendations to their clients are suitable. There's, in my opinion, a gigantic difference between something that is prudent and something that is merely suitable. And we can get into a much longer discussion.

We can probably fill three or four podcasts talking about the differences between what's suitable and what's prudent.

The reason why we're recording this podcast now in March of 2018 is because there's been a recent development, just a few weeks ago, where the Fifth Circuit Court of Appeals ruled against this fiduciary rule.

Without getting into a long history, understand that the Department of Labor, not the SEC, the Department of Labor, several years ago, started working on creating this fiduciary rule, basically as a way to protect investors with their retirement accounts.

This fiduciary rule basically said if you're going to have retirement accounts, it should be managed by a fiduciary. The problem is we have 401k accounts and IRAs that are being managed by brokers who work on commission, and that creates, for many people, an inherent conflict of interest.

The Obama administration pointed out when this law was about to be signed in April of 2016, that each year retirement investors lose up to \$17 billion a year in fees that are charged against their retirement account. A lot of them may be unnecessary.

They may be extra fees or higher fees than normal or commissions paid for products sold to clients.

Just a few weeks ago, the Fifth Circuit Court of Appeals ruled against the Department of Labor and their fiduciary rule.

In this case, understand that the brokerage community successfully argued that their representatives, the brokers, are sales people, and that they should not be burdened with these Department of Labor regulations.

Now, investment advisors already have this mantle of fiduciary responsibility. They have to comply with that. The brokerage community has not had to and they're reticent to begin making changes to act that way. Think about that for a moment.

There are many different terms for brokers in the investment community. One of the most obvious ones now is brokers are often called financial advisors. That sounds very close to the term investment advisor, doesn't it?

But a financial advisor and an investment advisor are two very different things. But the brokerage community likes to blur the distinction between the two. When I was growing up, the brokers were called stock brokers or sometimes they were called account executives.

When I worked for a brokerage firm, in their morning product calls, they would always start their calls by saying, "Good morning sales force." Think about that.

This distinction between brokers and investment advisors continues to this day, and this recent development is not going to help. We recently made a blog post on [mullooly.net](http://mullooly.net), and we'll link to this in the show notes for the podcast with tweets from a couple of industry leaders.

Michael Kitces, who's an industry thought leader and also Barbara Roper who's the Director of Investor Protection at CFA. That's the Consumer Federation of America.

Is this fiduciary rule dead? In its current state, it might be, but it might be not. It might not be dead. There is an upcoming court case in Washington, DC that will help shed more light on this. There were two previous court cases where there was the opposite outcome. The Department of Labor prevailed in upholding the fiduciary rule.

We think, as investment advisors, it makes sense. We're already complying with it, so of course we're going to think that it makes sense. But this could very well wind up going to the Supreme Court at some point in the future, and we think that ultimately, it's our opinion that it should be the law of the land that someone who is going to be managing assets for clients, they should act first and foremost with the needs of the client in mind.

Also, you should know that the SEC is still talking about coming on with their own version of a fiduciary rule, separate and apart from what the Department of Labor has already done. Now investment advisor firms and investment advisor representatives are overseen by the SEC. Brokers and their employees are overseen by FINRA. FINRA was created by the SEC.

It was actually created in 2007 when they merged the enforcement divisions of the New York Stock Exchange and the NASD together. A lot of people think the NASD just copped a new name and called it FINRA. FINRA actually stands for Financial Industry Regulatory Authority, but they found that the enforcement divisions of the New York Stock Exchange and the NASD were pretty much overlapping and doing the same things. They put them together.

Understand that FINRA is not a government agency. It's called an SRO, self-regulatory organization. It is put together and run by the members of the group. Investment advisors and their firms overseen by the SEC, brokers overseen by FINRA.

The SEC's responsible for ensuring fairness for the individual investor. FINRA is responsible for overseeing virtually all US stockbrokers and brokerage firms.

So a lot going on with this fiduciary rule. Clients, like I said earlier, sometimes their eyes glaze off when we start talking about this thing, but it's an important distinction to understand how your advisor is being compensated.

Is your advisor getting a commission, maybe a bigger commission for selling you a product, or is your advisor taking a fiduciary standard of care? Yes, they work for a fee, but are they gaining some kind of extra compensation?

That's really the guts of this, is understanding how your advisor is compensated, and that should be whenever you're talking to a potential investment advisor, someone who's going to be managing your assets.

It's an important topic to bring up. How are you compensated for managing my account? That is a very, very big deal, and that's why Mullooly Asset Management is set up as a fee only registered investment advisory firm.

We appreciate you listening to episode number 209, and we look forward to speaking with you again in our next episode. If you do have questions, feel free to get in touch with us, and we'll have links in the show notes in how you can reach us.