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Fiduciary standard could choke sales of mutual funds

Sellers may switch to fee-based model and wealthier clients, leaving average investors in the dust

By Jessica Toonkel

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With regulators inching closer to setting a universal fiduciary standard for all financial advisers, mutual fund companies may want to brace for the shift. Indeed, a number of attendees of the Investment Company Institute's Mutual Funds and Investment Management Conference in Palm Desert, Calif., this week said that a single standard of care will drastically alter the way fund firms sell their offerings.

Until now, the issue of the fiduciary standard has been a topic of hot debate in adviser circles. That will change, however, as soon as the Securities and Exchange Commission releases details of what the standard will look like, said Barry Barbash, former director of the Division of Investment Management and now a partner at Willkie Farr & Gallagher LLP.

“The SEC hasn't articulated what the fiduciary standard is with specificity other than through enforcement activity,” Mr. Barbash said in an interview with InvestmentNews at the ICI conference. “When they do, it will be a lightening show in terms of how mutual fund companies will react to it.”

Many funds are “sold, not bought,” said one attendee at the conference, who asked not to be identified. “At the end of the day, without effective distribution of mutual fund products, no one eats,” the attendee said.

Specifically, if the fiduciary standard pushes more advisers to adopt fee-based businesses, it could shift advisers' focus to wealthier clients and away from the “average-Joe investor who invests in funds through his 401(k),” said Robert Kurucza, a partner at Goodwin Procter LLP and a former associate director of the Division of Investment Management at the SEC.

“The intent of the standard is good, but the unforeseen consequences could be that some customers aren't treated fairly,” he said.

Fund companies already are wrestling with what the practical implications of a fiduciary standard on their businesses.

In a panel discussion Monday, Craig S. Tyle, general counsel at Franklin Resources Inc., asked Jennifer McHugh, senior adviser to SEC Chairman Mary Schapiro, about what implications the standard may have on fund companies. Ms. McHugh responded that the impact would be “secondary” to the mutual fund industry but that there could be disclosure requirements that fund companies would need to make to investors through brokers.

The form that disclosure takes could be meaningful, she said.

The fund industry is trying to figure out if the fiduciary standard is going to “be fundamental to how fund shares are sold,” Mr. Tyle told InvestmentNews after the panel discussion.

The Dodd-Frank financial reform law mandated that the SEC conduct a study on the need for a fiduciary standard for retail advice. In January, the commission released its findings and called for an extension of the fiduciary standard to broker-dealers. The SEC said such a move would protect investors, who it said are confused by differing standards that investment advisers and brokers must meet. And despite opposition on Capitol Hill and within the advice industry, agency officials expect to establish the standard this year.

But given everything on the SEC's plate, some fund company executives aren't worried that a fiduciary standard won't disrupt their businesses anytime soon.

“I think it's a long while away,” Natalie Bej, a principal at The Vanguard Group Inc., told InvestmentNews.