

## Best Interest or Disinterest—How Should We Label the Duties of an Investment Adviser?

At lunch with my broker the other day (my tab naturally), I asked the waiter for a hamburger and soda, but my broker interjected and told him to bring me a kale salad, no dressing, and a carrot and beet smoothie. "I'm supposed to look after your best interest," my broker said, "and you're clearly a bit overweight. By the way, I have scheduled an hour with your personal trainer after lunch." I couldn't deny it; this was all in my "best interest." I understand that this is not what the Securities and Exchange Commission (SEC) means when it repeatedly asserts ["An investment adviser is a fiduciary, and as such ... must act in the best interest of its client."](#) But the term is vague and can easily be misunderstood by the lay public. [It can lead an actor to claim that his financial advisers should have kept him from buying an entire village in France.](#) I do not think we need to be so imprecise—we can distinguish between "best interest" and "disinterest." It is *disinterested* advice the SEC should expect of advisers.

### "Fiduciary" Isn't an All-Purpose Label

In my view, since at least the adoption of Section 36(b) of the Investment Company Act, we have become lazy in drawing important distinctions among fiduciaries. We often quote, but seldom truly abide by, the injunction from [SEC v. Chenery Corp.](#):

But to say that a man is a fiduciary only begins analysis; it gives direction to further inquiry. To whom is he a fiduciary? What obligations does he owe as a fiduciary? In what respect has he failed to discharge these obligations? And what are the consequences of his deviation from duty?

The reply to the second question ("What obligations does he owe as a fiduciary?") is too often a superficial recitation of "duties of care and loyalty." We freely generalize from any precedent that mentions "fiduciary," ignoring critical differences between a fully discretionary trust and a transient agency for a limited purpose. A general partnership may require ["the punctilio of an honor the most sensitive;"](#) an agent running an errand for his principal, not so much.

### Fiduciaries Who Need to Act in their Charge's "Best Interest"

A fiduciary who cannot effectively communicate with her charge must use her judgment as to what course should best serve her charge's interest. A trustee or guardian for a minor child or incompetent adult faces this necessity, as does the director for a widely-held corporation. Thus, we might properly impose on these fiduciaries a duty to ascertain and act in the best interest of their beneficiaries or corporations. In contrast, the director of a wholly-owned company can ask the sole shareholder for direction on a proposed course of action. The director might or might not try to advise the shareholder as to the wisest course, but it should be considered officious for the director to refuse to follow any lawful course directed by the shareholder based on a different view of the shareholder's "best interest."

### Investment Advisers Should Give Disinterested Advice

Investment advisers are agents of their clients—not trustees, partners or directors. Like other agents, their

fiduciary duties should reflect the limits of their authority. The SEC seems to acknowledge this by citing §2.02(1) of the Restatement (Third) of Agency, which provides that:

An agent has actual authority to take action designated or implied in the principal's manifestations to the agent and acts necessary or incidental to achieving the principal's objectives ....

More simply, the agent has a duty to do what the principal has asked and the agent agreed to do and nothing more. The duties of an adviser with fully discretion over a client's entire portfolio may differ meaningfully from those of an adviser helping a client pick the best 529 plan. An agent is also constrained by a duty of loyalty. In the context of investment advice, the SEC properly explains that the duty of loyalty requires "[\[a\]n investment adviser ... not \[to\] favor its own interests over those of a client or unfairly favor one client over another.](#)" In other words, investment advice should be "disinterested," meaning responsive to the client's expressed objectives (regardless of the adviser's views of those objectives) rather than the interests of the investment adviser or her other clients. Although it is surely too late to expunge "best interest" from this conversation, the SEC would be better served by avoiding the term wherever possible in adopting its formal interpretation of an investment adviser's fiduciary duties.

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