PACIFIC LIFE

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Submitted electronically to securitiesregs-comments@sec.state.ma.us

Office of the Secretary of the Commonwealth
Attn: Proposed Regulations – Fiduciary Conduct Standard
Massachusetts Securities Division
One Ashburton Place, Room 1701
Boston, MA 02108

Re: Proposed Massachusetts Fiduciary Standard of Conduct for Broker-dealers, Agents, and Investment Advisers.

Dear Secretary Galvin:

Thank you for providing us the opportunity to share our comments on the Massachusetts Securities Division's (the "Division") proposed fiduciary standard of conduct under the Massachusetts Securities Code ("Fiduciary Proposal") published on December 13, 2019[1].

Pacific Life has consistently supported regulatory harmony and collaboration as both federal and state regulators work on creating a uniform and reasonable standard of care for financial professionals. However, we have significant concerns about the Fiduciary Proposal and the approach the Division is taking by requiring *all* financial professionals making a recommendation or providing investment advice be subject to a fiduciary standard.

Pacific Life submitted our July 2019 Comment Letter[2] ("July 2019 letter") on the precursor to the Fiduciary Proposal that was published on June 14, 2019 ("Preliminary Proposal"). The July 2019 letter focused mainly on the steps Pacific Life believes are necessary to create a standard that can reasonably be understood by consumers, complied with by financial professionals, enforced by the applicable regulatory agencies, and requires *all* financial professionals to act in their clients' best interest. Namely, and for reasons expanded upon in our July 2019 letter, Pacific Life believes:

- **The Division Must Define and Distinguish What Makes a Financial Professional a Fiduciary:** It is important for the Division to clearly state within the Fiduciary Proposal that, while all financial professionals must act in their client's best interest, only the financial

[1] http://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/Notice-of-Comment-Period-and-Public-Hearing.pdf

[2] http://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/preliminarycomments/2019-07-25-Pacific-Life-Insurance-Company.pdf

professionals that agree to take dominion and control of the consumer's assets through a grant of discretionary authority, coupled with an obligation to manage, monitor, and review that client portfolio on an ongoing basis, rise to that "special fiduciary relationship" with the consumer.

- **The Division Must Coordinate with Federal and State Regulators Before Finalizing the Fiduciary Proposal:** The issue of applying a fiduciary duty or a heightened standard of care (e.g., "best interest") to financial professionals has been a part of a much larger debate involving Congress and numerous regulatory agencies with differing jurisdictions, including, at the federal level, the U.S. Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("FINRA"), and the U.S. Department of Labor ("DOL"). On the state level, the issue has been tackled by the North American Securities Administrators Association ("NASAA"), the National Association of Insurance Commissioners ("NAIC"), and the individual state securities and insurance departments. Ultimately, such coordination will avoid confusing, conflicting, or duplicative regulatory standards and help ensure that consumers are not asked to identify or be responsible for understanding what standard of care, from a multitude of standards, any particular financial product sale or investment/financial advice is under.

The purpose of this letter is to not only reiterate concerns addressed in the July 2019 letter, but to also point out the Division lacks authority to adopt such a proposal, as discussed further below.

The Fiduciary Proposal Exceeds the Authority Granted to the Division

The Fiduciary Proposal assumes authority that is not granted to the Division and contains imprecise and ambiguous terms that could potentially contradict and/or duplicate both Massachusetts Securities Law and Massachusetts Insurance Code.

The Securities Division Lacks Statutory Authority

The creation of a fiduciary duty by regulatory fiat violates core separation-of-powers principles by exercising a legislative function outside the scope of the Division's rulemaking authority. Codification of a judicially established fiduciary standard in Massachusetts securities regulations represents a significant change in the law. Establishing a fiduciary duty by *regulation*, therefore, inappropriately assumes the role and responsibilities reserved for the Massachusetts legislature.

Section 204(a)(2)(G) of the Act does authorize the Division to deny, revoke, suspend, cancel or withdraw the registration of any broker-dealer or investment adviser who, among other things, "(G) has engaged in any unethical or dishonest conduct or practices in the securities, commodities or insurance business." However, nothing in that statutory provision gives the Division authority to adopt regulations imposing a fiduciary duty on broker-dealers or investment advisers. The Division has authority to regulate conduct by broker-dealers and advisers that is actually *unethical* or *dishonest*, but the lack of stringent fiduciary obligations with respect to broker-dealers who are not fiduciaries at common law or by statute does not mean that broker-dealers are engaged in unethical or dishonest conduct.

Furthermore, the Massachusetts Department of Insurance ("MA DOI"), as the primary regulator of the Massachusetts insurance industry, is best suited to enforce standards of conduct with regard to recommendations of insurance products. Jurisdictional regulatory boundaries should be observed so that state laws are not inconsistent with respect to the standard of conduct applicable to these products. Absent

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such consistency, two insurance producers who are regulated by the MA DOI could be held to different standards simply because one of them is also subject to regulation by the Division.

The Fiduciary Proposal is Imprecise and Ambiguous

Section 12.207(1) of the Proposal provides a "non-exclusive list of practices by a broker-dealer, agent, investment adviser, or investment adviser representative which shall be deemed 'unethical or dishonest conduct or practices.'" This raises significant concerns about several aspects of this provision.

First, by characterizing this as a "non-exclusive list," the Proposal fails to clearly define the types of conduct it intends to prohibit. While this approach may provide the Division with greater latitude to pursue bad actors, we fear the ambiguous nature of this section will also drive trustworthy and reliable individuals to be more selective of the new investors they choose to service (i.e., those with higher amounts of assets to invest) and severely limit the services and investment advice offered to existing clients, thereby making it harder and more expensive for Massachusetts citizens to obtain individualized investment advice. Obviously, this would not be a positive outcome.

Second, subsection (a) refers to "Failing to act in accordance with a fiduciary duty to a customer or client when providing investment advice or recommending an investment strategy... or the purchase, sale, or exchange of any... *insurance product*." However, the Proposal fails to define any of these terms, most notably, what is meant by "insurance product." These undefined terms in the Fiduciary Proposal operate to contradict provisions under the Massachusetts Securities Law.

For example, Massachusetts Uniform Securities Law Section 110A § 401 (K) provides that:

> "Security" does not include any insurance or endowment policy or annuity contract under which an insurance company promises to pay a fixed or variable number of dollars either in a lump sum or periodically for life or some other specified period;

This definition brings all insurance, endowment policies, and annuity contracts outside the scope of Massachusetts Uniform Securities Law and the regulations thereunder. All insurance, endowment, and annuity contracts, therefore, are also excluded from the scope of regulations adopted under the Massachusetts Securities Code. Thus, the Fiduciary Proposal's imprecise and undefined terms and circumstances identified above could pull these excluded categories into the proposed regulation.

Third, subsection (b)4 would require broker-dealers, agents, investment advisers, and investment adviser representatives to meet a fiduciary duty whenever they receive "ongoing compensation or charge[] ongoing fees" for advice about the advisability of certain investment activities. Commission-based compensation arrangements frequently include both an upfront commission and a trailing (or "ongoing") commission. In practice, however, imposing a fiduciary duty on such arrangements would effectively impose a corresponding duty to provide ongoing monitoring.

Clearly, ongoing monitoring of a client's account and investments is a significant and valuable service. It is not, however, a service that is universally needed or wanted by all investors. Like nearly all other services, ongoing monitoring is not free; it requires additional time and effort, and exposes firms and financial professionals to risks and potential liabilities that would not otherwise exist. As such, ongoing monitoring comes with a cost, and that cost may outweigh the value for many investors. For example, a buy-and-hold investor could go multiple years without making any changes to his or her portfolio, and therefore, would derive little to no benefit from ongoing monitoring. Unfortunately, the Fiduciary

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Proposal would effectively prevent such investors from purchasing and paying for only those services they actually want or need.

Fourth, subsection (b)4 would also impose a fiduciary duty whenever broker-dealers, agents, investment advisers, and investment adviser representatives provide advice about the advisability of certain investment activities "as an integral component of other financially related services." Similar to the concerns initially expressed above, the Proposal provides no definition of this phrase, thereby preventing firms and financial professionals from knowing whether they have engaged in conduct that will trigger fiduciary obligations under this subsection.

Lastly, subsection (b)5 provides that a fiduciary duty can arise as a result of the "reasonable expectation" of the customer or client. Again, the Proposal offers no clarity or certainty as to the types of situations or conduct that would be sufficient to create a "reasonable expectation" that ongoing monitoring will be provided (except for the use of certain titles identified in subsection (c)).

Based on the foregoing, we respectfully urge the Division to revise Section 12.207(1)(a) and (b) to more clearly define the circumstances under which broker-dealers, agents, investment advisers, and investment adviser representatives will be required to satisfy a fiduciary duty. Clarity and certainty are critical for any regulation to effectively achieve its intended objectives, and we sincerely hope the Division recognizes this as well.

The Fiduciary Proposal Conflicts with Insurance Commissioner's Exclusive Authority to Regulate Insurance Products

The Massachusetts Insurance Code states that the negotiation, solicitation, sales, or transaction in fixed or variable insurance or annuity contracts by any person shall not be subject to the provisions of the Massachusetts Securities Code.[3] This statutory provision in the Insurance Code gives exclusive, unequivocal jurisdiction to the Insurance Commissioner.

Notwithstanding the Insurance Commissioner's exclusive jurisdiction over all insurance and annuity contracts, the request for comment states that "given the overlap of securities-related and non-securities-related advice, the Division has a strong interest in regulating the conduct of its registrants *regardless of the presence or absence of securities*" and expresses that insurance product sales are within scope of the regulation. But the exclusive jurisdiction of the Insurance Commissioner precludes the Division's assertion of jurisdiction and the application of a fiduciary standard to insurance product sales and distributors. The attempt to impose a fiduciary duty regarding insurance and annuity contracts blatantly ignores the legislature's unequivocal reservation of exclusive jurisdiction to the Insurance Commissioner and Insurance Code. The Division has no authority over the sale of insurance or annuity contracts.

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[3] M.G.L. c. 175, § 3; Section 3: Unauthorized insurance, annuity or variable annuity contracts; prohibition
Section 3. No company shall make a contract of insurance or annuity, including any such insurance or annuity contract which is a contract on a variable basis, upon or relative to any property or interests or lives in the commonwealth, or with any resident thereof, and no person shall negotiate, solicit, sell or in any manner aid in the transaction of such contracts, or of their continuance or renewal, except as authorized by this chapter or chapter one hundred and seventy-six, or except as otherwise expressly authorized by law; and any such contract and the negotiation, solicitation, sale or transaction thereof by any person shall not be subject to the provisions of chapter one hundred and ten A [the MA Securities Code].. (emphasis added).
https://malegislature.gov/Laws/GeneralLaws/PartI/TitleXXII/Chapter175/Section3

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Conclusion

Ultimately, Pacific Life is requesting that the Division revisit the Fiduciary Proposal and consider whether the Division even has the authority to adopt the Fiduciary Proposal as currently drafted. If it is somehow determined the authority exists, then the Division should seriously consider coordinating with the federal and state regulators before finalizing the Fiduciary Proposal, so as to avoid conflicting or duplicative regulatory standards. Pacific Life fears that without these coordination efforts and changes to clarify certain circumstances and/or terms within the Fiduciary Proposal, the Fiduciary Proposal will directly harm the very consumers it is intended to help by interfering with their access to valuable retirement products and information about them.

Pacific Life joins the American Council of Life Insurers, the Committee of Annuity Insurers, and the Insured Retirement Institute in supporting a full and comprehensive review of the Fiduciary Proposal and coordination with federal and state regulators before finalizing. In order for us to achieve our shared goal for Massachusetts citizens to save for a secure retirement, and receive advice that is in their best interest, it is necessary that the Fiduciary Proposal and its implementation is done properly and thoughtfully to minimize market disruption and avoid ongoing consumer confusion.

Thank you again for the opportunity to share our views on this important regulatory effort. Pacific Life supports a uniform best interest standard of care applicable to all financial professionals and we stand ready to help you find the right path forward.

Sincerely,

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