



PUBLIC INVESTORS ARBITRATION BAR ASSOCIATION

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via email to securitiesregs-comments@sec.state.ma.us

January 7, 2020

William F. Galvin

Secretary of the Commonwealth of Massachusetts

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 Amendments to 950 CMR Sections 12.204, 12.205 & 12.207

Dear Mr. Galvin:

I write on behalf of the Public Investors Advocate Bar Association (“PIABA”), an international bar association comprised of attorneys who represent investors in disputes with the securities and commodities industries. Since its formation in 1990, PIABA has promoted the interests of the public investor in all securities and commodities forums, while also advocating for public education regarding investment fraud and industry misconduct. Our members and their clients have a strong interest in rules which govern the conduct of those who provide advice to investors.

On June 14, 2019, the Office of the Secretary of the Commonwealth of Massachusetts (“the Secretary”) issued a Notice soliciting comments regarding amendments to its regulations to require that broker-dealers, agents, investment advisers, and investment adviser representatives be subject to a fiduciary duty when dealing with their customers and clients. The Secretary recognized in its Notice that a uniform fiduciary standard is in the public interest and is necessary to protect investors from the abuses that can result when financial professionals place their own financial interests ahead of their customers. The Secretary also recognized that the Securities and Exchange Commission’s (“SEC”) Regulation Best Interest (“Reg BI”) failed to establish a strong and uniform fiduciary standard. The Secretary has amended the proposal (“the Proposed Amendments”), and issued a subsequent request for comment (“Request for Comment”).¹⁰

PIABA has long advocated for a true fiduciary standard for all those who provide investment advice to their clients, and fully supports the Secretary’s Proposed Amendments and ultimately, the Rule 17c-1. The Commonwealth of Massachusetts Request for Comment (Dec. 13, 2019), available at <https://www.sec.state.ma.us/SEC/securitiesregscomments/Request-for-Public-Comment.pdf>. The Notice, PIABA believes a uniform fiduciary duty applicable to all financial intermediaries who provide investment advice would eliminate confusion.

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and best protect customers.²⁹ PIABA therefore believes fiduciary duty should apply to all forms of financial advice, and to all customers. PIABA also believes the fiduciary duty should arise whenever a financial or investment recommendation is made, and that it should last throughout the duration of the advisor-customer relationship. Finally, PIABA believes the Proposed Amendments should explicitly provide for a private right of action. PIABA's position is discussed in further detail below.

I. PIABA SUPPORTS THE PROPOSED AMENDMENTS' PROVISION OF A UNIFORM FIDUCIARY DUTY ON ALL BROKER-DEALERS, AGENTS AND ADVISERS WHO PROVIDE INVESTMENT ADVICE

A. Application of a Fiduciary Duty to Financial Professionals Who Provide Investment Advice

The Proposed Amendments protect Massachusetts investors by imposing a fiduciary duty on all financial professionals who render investment advice, and by broadly defining the types of investment recommendations and advice which trigger that obligation. The proposed statewide uniform fiduciary standard makes it clear that financial professionals owe a fiduciary duty whenever they provide financial recommendations and advice for financial remuneration, rather than putting the burden upon customers to prove that there was a relationship of trust and reliance.³⁰ PIABA supports the Secretary's approach of requiring all financial professionals, regardless of title or license, to adhere to a uniform fiduciary duty when providing investment advice.

The Proposed Amendments are consistent with what most retail customers believe about their financial advisor—that he or she is a fiduciary.⁴⁰ Indeed, brokerage firms—who have consistently lobbied against being considered fiduciaries—give their brokers titles that sound trustworthy, like “Financial Advisor,” “Wealth Consultant,” and “Wealth Manager.”⁵⁰ Brokers also pay millions of dollars every year in advertising to tell investors that they put the interests of customers ahead of their own. Brokers encourage investors to trust them, saying they will provide advice and guidance. As a result, when a customer meets with a broker, the customer reasonably expects that the broker is being given advice that is for his or her benefit, not for the benefit of the broker or brokerage firm. This is particularly true as to broker-dealers and financial professionals who are regularly registered as investment advisers. The Proposed Amendments will finally align the duty that financial professionals owe to customers in rendering investment advice with the representations made by such professionals and with the customers' reasonable expectations.

PIABA also strongly supports the Proposed Amendments' broad definition of the types of investment advice that trigger a fiduciary duty. The Secretary correctly recognizes that brokers do not merely pick investments or devise investment strategies. Specifically, brokers sometimes recommend other financial courses of action preceding the

²⁹SEC, *Study on Investment Advisers and Broker-Dealers* (“SEC Study”) (Jan. 2011), available at <http://www.sec.gov/news/studies/2011/913studyfinal.pdf>. The SEC reviewed two studies which it sponsored (the “Seigel & Gale Study” and the “RAND Report”), and a study conducted by Consumer Federation of America. The SEC Study found that, based on the comments, studies and surveys it had reviewed, investors did not understand the differences between investment advisers and broker-dealers. The SEC determined that this misunderstanding is compounded by the fact that many retail investors may not have the sophistication, information, or access needed to represent themselves effectively in today's market and to pursue their financial goals.” *Id.* at 101.

³⁰See, e.g., *Hays v. Ellrich*, 471 Mass. 592 (Mass. 2015); *Genovesi v. Nelson*, 85 Mass. App. Ct. 243 (Mass. App. 2014); *Patsos v. First Albany Corp.*, 433 Mass. 23 (Mass. 2000).

⁴⁰See Spectrum Group, *Fiduciary – Do Investors Know What it Means* (2015), available at <http://spectrum.com/Content/Whitepaper/fiduciary.aspx>.

⁵⁰Peiffer, Joseph C. and Christine Lazaro, *Major Investor Losses Due to Conflicted Advice: Brokerage Industry Advertising Creates the Illusion of a Fiduciary Duty, Misleading Ads Fuel Confusion, Underscore Need for Fiduciary Standard* (March 25, 2015), available at <https://piaba.org/sites/default/files/newsroom/2015-03/PIABA%20Conflicted%20Advice%20Report.pdf>.

recommendation of a particular security or investment strategy, in order to earn the client's trust and cause the client to entrust their assets to the broker for management. Prime examples of such scenarios include a recommendation to a prospective client to rollover an employer-based retirement account into a new IRA, or a recommendation to a prospective client that they retire early and/or elect a lump sum payment in lieu of a defined benefit pension and turn the lump sum over to the broker for investment. Obviously, the broker has a financial incentive to recommend these courses of action. The Proposed Amendments appropriately hold financial professionals to a fiduciary duty for all types of investment advice, including, but not limited to, the situations described above.

B. Incorporating the Duty of Care and Duty of Loyalty

PIABA supports the Proposed Amendments' incorporation and definition of the two primary duties of a fiduciary: the duty of care and the duty of loyalty, which are set forth in the Proposed Amendments.⁶⁹ PIABA agrees that the Secretary's approach to fiduciary duties and the definitions utilized in the Proposed Amendments strike an appropriate balance between accommodating the traditional, compensation-based model of many broker-dealers and other sales agents, with the interests of protecting investors from the financial harm of conflicted advice causes. Moreover, PIABA strongly believes that any lesser standard will undermine the meaning of the term "fiduciary", a legal standard that has been developed through centuries of law and precedent and, as a result, has a certain understanding among public investors and those in the investment advice community.

II. THE PROPOSED AMENDMENTS ARE NECESSARY AND APPROPRIATE BECAUSE THEY PROVIDE GREATER PROTECTION FOR MASSACHUSETTS'S INVESTORS THAN THE SECURITIES AND EXCHANGE COMMISSION'S "REGULATION BEST INTEREST"

As the Request for Comment explicitly recognizes, Reg BI does not provide sufficient protections for Massachusetts investors.⁷⁰ PIABA strongly agrees and has so stated repeatedly in public comments since the SEC first introduced the proposals behind Reg BI.

A. Reg BI Does Not Sufficiently Protect Investors

Despite its title, Reg BI does not impose a true fiduciary standard upon broker-dealers and affiliated persons who provide investment advice. Reg BI essentially builds upon and codifies FINRA's interpretation of its suitability rule.⁸⁰ Reg BI does not define best interest, but rather, creates a checklist of four obligations a firm must discharge to meet the standard—disclosure, care, conflict of interest, and compliance obligations. Incredibly, none of the elements of this checklist actually obligates the firm to place the customer's interests ahead of the firm's. Effectively, this results in the SEC's Reg BI being misleading in its name as "best interests" is there in name only, not in the actual standard of care.

Reg BI substantially relies on disclosure rather than meaningful investor protection. While theoretically an enhancement of FINRA rules, the Customer Relationship Summary form ("Form CRS") that Reg BI requires and relies upon will not provide investors with timely, useable information, nor result in resolving the acknowledged confusions investors face when dealing with different kinds of financial advisors. This is not merely PIABA's opinion. In fact, the SEC's own commissioned study by the RAND Corporation confirmed that Form CRS was largely ineffective

⁶⁹ Proposed Amendment to 950 CMR 12.207(2).

⁷⁰ See Request for Comment at 24, *supra* note 1.

⁸⁰ Securities and Exchange Commission, Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34-86031, 17 C.F.R. pt. 240 (June 5, 2019) ("Final Rule").

in helping investors understand the different duties of financial professionals, and that many individuals still remained confused about when firms and their agents owed them fiduciary duties and when they did not, even after reading Form CRS.⁹⁹ Further, in an attempt to provide greater flexibility for firms to tailor the wording of Form CRS disclosures,¹⁰⁰ Reg BI does not require firms to disclose every material conflict, but instead, gives firms wide discretion on what to disclose.¹¹⁰

Additionally, Reg BI still allows brokers to satisfy their purported disclosure obligations regarding costs by providing percentages or ranges, rather than the dollar amounts likely to be understood by investors. In short, under Reg BI, firms will be able to satisfy their duties regarding costs through disclosure and those disclosure obligations can largely be met through boilerplate disclosures. As provided above, that means brokers can withhold actual cost and conflict of interest information until after the sale of the product at issue has been made under Reg BI, completely undercutting investor protections.

Moreover, in contrast to the Proposed Amendments, Reg BI will not require brokers to weigh the relative risks, costs and benefits of different strategies or types of investments available to achieve the customer's goals. Shockingly to most investors and certainly all investor advocates, this means that under Reg BI a broker will not be required to recommend the best of the reasonably available options. Reg BI also limits the purported "best interest" obligation to the beginning and end of a transaction, rather than for the duration of the customer-broker relationship.

Furthermore, Reg BI's conflict obligation does not prohibit firms from creating conflicts that would reasonably be expected to encourage and reward advice that is not in the customer's best interests. Reg BI simply requires firms to develop and enforce policies and procedures to "mitigate" most conflicts and, to the extent not mitigated or eliminated, the firm may satisfy this obligation through disclosure. However, providing greater disclosure does not appropriately mitigate the conflicts of interest inherent in the relationship between financial advisors and customers. Instead, it places the burden on the customers to fully understand the impact of those conflicts on the future of their retirement savings.

Last and most problematic, as the Secretary and the Proposed Amendments recognize, Reg BI continues differing standards of conduct for dually registered investment advisers and brokers. This will require public investors to be able to differentiate whether the advice being given from the same investment professional is being given as a broker or an investment adviser, effectively shifting the burden to public investors to protect themselves against conflicted advice. Harmonizing the standard of care will correctly put that obligation back on the investment professional.

The weak and ineffective provisions of Reg BI stand in sharp contrast to the Proposed Amendments. As discussed in Section 2 above, the Proposed Amendments hold all financial professionals who render investment advice to a fiduciary standard. The Proposed Amendments require that financial professionals adhere to a duty of care and a duty of loyalty, which cannot be discharged solely through purported disclosures. The Proposed Amendments define what the fiduciary duty requires, and what is meant by the duty of care and the duty of loyalty. The Proposed Amendments provide that conflicts of interest are presumed to be a breach of the duty of loyalty. Lastly, the

⁹⁹ Investor Testing of Form CRS Relationship Summary, SEC 46 (Nov. 2018), available at

<https://www.sec.gov/about/offices/investorad/investor-testing-form-crs-relationshipssummary.pdf>. In fact, the written responses to specific questions about the disclosures reveal that a significant number of participants did not understand important sections of the form, and still had a general misunderstanding of the different standards governing investment accounts and financial professionals. The RAND report also reflects that many of the participants were unable to synthesize and apply the information. *Id.* at 47-48.

¹⁰⁰ Final Rule, *supra* note 12, at 81.

¹¹⁰ Firms are not expected to disclose every material conflict of interest, and should instead consider what would be most relevant for retail investors to know in deciding whether to select or retain the particular firm. *Id.* at 61.

Proposed Amendments eliminate the false distinction between investment advisers and brokers by treating both as the financial professionals which they hold themselves out to be, and by requiring both to adhere to the same standard of conduct.

Simply put, the differences between Reg BI and the fiduciary standard proposed in the Proposed Amendments are significant and will actually work to increase the standard of care for investors. Consequently, as the Request for Comment states, the Proposed Amendments are necessary and appropriate in order to sufficiently protect Massachusetts investors.

B. Reg BI Does Not Preempt the Secretary from Enacting the Proposed Amendments

Based on public statements that have been made, PIABA believes that some in the financial services industry may argue that Reg BI preempts States from enacting a fiduciary standard. Such an argument is not supported by Reg BI, nor by the Dodd-Frank Act under which Reg BI has been promulgated. In fact, the exact opposite is true.

Specifically, there is no express language in Reg BI which alters or supersedes any existing obligations applicable to brokers and broker-dealers with respect to the circumstances under which brokers may owe customers a fiduciary duty under state law. To the contrary, the SEC explained in its Release that “the preemptive effect of [Reg BI] on any state law governing the relationship between regulated entities and their customers [will] be determined in future judicial proceedings.”¹²

Further, Reg BI was promulgated pursuant to Section 913 of Title IX of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”). This provision required the SEC to conduct a study to evaluate the effectiveness of existing legal or regulatory standards of care (imposed by the Commission, a national securities association, and other federal or state authorities) for providing personalized investment advice and recommendations about securities to retail customers; and whether there are legal or regulatory gaps, shortcomings, or overlaps in legal or regulatory standards in the protection of retail customers relating to the standards of care for providing personalized investment advice about securities to retail customers that should be addressed by rule or statute.¹³ It is clear from the foregoing that the SEC’s task was to determine whether a rule establishing a baseline standard for investment advice was warranted based on gaps in the existing regulatory scheme. Indeed, the Dodd-Frank Act does not provide that rulemaking by the SEC in this area would preempt state law. Likewise, Reg BI does not indicate that it is intended to preempt state law. Simply put, Massachusetts retains the right to enact more stringent rules than the SEC if its legislators or judiciary conclude that an enhanced level of investor protection is warranted based on the needs of the State.

Finally, the only potential challenge to the Draft Regulations would be under the National Securities Markets Improvement Act of 1996 (“NSMIA”). Section 103 of NSMIA limits states from enacting any rule or regulation that imposes upon broker-dealers any “[c]apital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements” that are greater than those imposed under federal law, rules or regulations.¹⁴ The Proposed Amendments expressly address this concern.¹⁵ As such, the Secretary is well.

¹² Final Rule, *supra* note 12 at 43.

¹³ See “Study on Investment Advisers and Broker-Dealers,” Executive Summary, p. i, January 2011, available at <http://www.sec.gov/news/studies/2011/913studyfinal.pdf>.

¹⁴ 15 U.S.C. §780(i).

¹⁵ 950 CMR 12.207(f)

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within his authority to enact this provision and has appropriately addressed any preemption issues that could be raised.

III. Conclusion

PIABA supports the Secretary's efforts to heighten the duty of brokers who provide investment advice to their customers. PIABA urges the Secretary to adopt its Proposed Amendments. PIABA applauds the Secretary on taking on this incredibly responsibility to make sure that the standard of care for those who provide investment services meet with the reasonable expectation of the investing public. Last, PIABA thanks the Secretary for the opportunity to comment on this important issue.

Very truly yours,

A handwritten signature in black ink, appearing to read "Samuel B. Edwards". The signature is fluid and cursive, with a long horizontal stroke at the end.

Samuel B. Edwards
President, PIABA