



July 26, 2019

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: Comments on Proposed Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisors, and Investment Advisor Representatives (the “Proposal”)¹

Dear Secretary Galvin:

Fidelity Investments (“Fidelity”)² believes that the MA Division of Securities has been an effective protector of consumer rights under your leadership and has battled fraud and other forms of misconduct by broker-dealers and investment advisors. We applaud those efforts. This Proposal, however, will add no material protection to consumers but will instead limit their investment choices and deprive them of benefits that they currently enjoy under the numerous laws, rules and regulations (including Regulation Best Interest) that govern the behavior of broker-dealers and investment advisors. We appreciate the opportunity to provide comments to the Massachusetts Division of Securities (the “Division”) on the Proposal.

Given our longstanding and ongoing commitment to the needs and interests of our customers, Fidelity has long supported a requirement that broker-dealers and investment advisers act in the best interest of retail investors when providing investment advice. This is evidenced by Fidelity’s active engagement in the regulatory discussions on the standard of conduct for investment advisors since 2013, which culminated in our support for the Securities and Exchange Commission’s (“SEC”) adoption of Regulation Best Interest (“Reg BI”)³. Reg BI provides a strong, clear, practical and workable fiduciary standard for the provision of investment advice to

¹ Available at: <https://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/fiduciaryconductstandardidx.htm>.

² Fidelity was founded in 1946 and is one of the world’s largest providers of financial services, including investment management, retirement planning, portfolio guidance, brokerage, benefits outsourcing, and many other financial products and services to more than 27 million individuals and institutions, as well as through 12,500 financial intermediary firms. Fidelity submits this letter on behalf of Fidelity Brokerage Services LLC, an SEC-registered introducing broker-dealer and FINRA member; National Financial Services LLC, an SEC-registered clearing broker-dealer and FINRA member; and SEC-registered investment advisers Fidelity Personal and Workplace Advisers LLC, Strategic Advisers LLC, and Fidelity Management & Research Company, the investment adviser to the Fidelity family of mutual funds.

³ Public Statement by SEC Chairman Jay Clayton: *Regulation Best Interest and the Investment Adviser Fiduciary Duty: Two Strong Standards that Protect and Provide Choice for Main Street Investors* (July 8, 2019), available at <https://www.sec.gov/news/speech/clayton-regulation-best-interest-investment-adviser-fiduciary-duty> (the “Public Statement”); and Securities and Exchange Division, *Duties of Brokers, Dealers and Investment Advisers* Release No. 34-69013 (March 1, 2013) (Fidelity comments available at <https://www.sec.gov/comments/4-606/4606-3117.pdf>).



retail customers. Our comments below reflect our concern that attempts to impose a Massachusetts-specific standard that is fundamentally at odds with Reg BI is unwise and unnecessary, and would harm Massachusetts residents by reducing their access to free investment advice incidental to brokerage transactions.

Fidelity's History of Serving Massachusetts Customers

Fidelity's core mission is to assist our customers in achieving their financial goals. To that end, Fidelity has been headquartered in Massachusetts since its inception in 1946, and has maintained a strong community and civic presence ever since. Fidelity operates a major home office base in multiple office locations in Boston, as well as nine Investor Centers throughout the state to service the needs of Massachusetts residents. Between the home office location and Investor Centers, Fidelity leases or owns over 1.6 million square feet of office space. Fidelity has 5,500 employees who are Massachusetts residents.

Fidelity serves more than 2.1 million individual Massachusetts residents, administering \$306 billion in assets. Fidelity also administers \$42.6 billion on behalf of Massachusetts-based institutions, with total administered assets of \$348.6 billion.⁴ Fidelity manages the Massachusetts 529 college savings and ABLE programs.

Importance of Investment Choices

Fidelity, like many other financial service providers, offers two relevant types of accounts for retail investors to choose from⁵: advisory accounts, and brokerage accounts. These accounts differ in material ways, including with respect to fee structures and trade decision-making. Advisory accounts may be more appropriate to investors who seek ongoing advice or discretionary portfolio monitoring. Brokerage accounts, on the other hand, are often most appropriate for self-directed investors who prefer to manage their own portfolios and require only incidental advice from time to time.

An investor's investment portfolio, need for brokerage and advice services, and preferred fee structure for those services can vary over time. For example, an investor may seek advice when starting a college savings fund or changing jobs and may be interested in receiving advice at that point in time only. In a brokerage account model, customers can receive that sort of advice without charge; if the customer then decides to act on the advice and execute securities trades, she would incur only costs associated with the securities trade(s). On the other hand, customers could prefer to have their portfolio managed by a team of professionals, who monitor the market, their investments, and their investing needs, and make and implement trading decisions on their behalf. Investors often have both types of accounts: a brokerage account for some of their assets, and a discretionary advisory account with ongoing asset-based fees for

⁴ As of June 30, 2019.

⁵ Fidelity offers several account types to choose from, including non-retirement, retirement, Health Savings Accounts, 529 college savings, etc. However, the most relevant impacts of the Proposal are to the general classifications of brokerage and advisory accounts.

others. Fidelity believes that there are benefits to both types of accounts, and that it is imperative to preserve that choice for investors.

The SEC's formulation of Reg BI was guided, in significant part, by the recognition that preserving customer access to both models is critical. As the SEC noted in its release of Reg BI, "we believe that our approach in adopting Regulation Best Interest will best achieve the Commission's important goals of enhancing retail investor protection and decision making, while preserving, to the extent possible, retail investor access (in terms of choice and cost) to differing types of investment services and securities."⁶ This was further emphasized by SEC Chairman Jay Clayton, who recently stated: "Under our approach, Main Street investors will be able to choose the type and level of services they want—from occasional recommendations about particular investments to comprehensive account management—and how they want to pay for those services. I do not believe that a 'one size fits all' approach would best serve the diverse interests of our Main Street investors. Further, I believe in this area, a one-size fits all approach could reduce the availability and increase the cost of advice and services, particularly for those with relatively smaller accounts."⁷ Preserving investor choice for Massachusetts residents should be similarly paramount in considering state regulation in this area.

Regulation BI Provides a Strong and Workable Standard of Conduct

As noted, it has long been Fidelity's view that broker-dealers and investment advisers should act in retail investors' best interest, and that a standard embracing this obligation would benefit both retail investors and the financial services industry. We have therefore commended the SEC for its efforts to develop thoughtful, comprehensive proposals through an inclusive process, which resulted in the release of Reg BI. Reg BI has allowed the SEC to develop consistent standards across account types and services, including brokerage accounts and advisory accounts, as well as retirement and non-retirement accounts. In fact, we believe there is no meaningful difference between Reg BI's standard of conduct for broker-dealers and the fiduciary standard for investment advisers – in both, the customer's interests must always come first.

Fidelity has actively engaged for many years in regulatory discussions on the standards of conduct for broker-dealers and investment advisers. We responded to the SEC's 2013 Request for Data and Other Information,⁸ the SEC's June 2017 Request for Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers,⁹ and we provided extensive comments to the Department of Labor ("DOL") on

⁶ See "Regulation Best Interest: The Broker-Dealer Standard of Conduct," Final rule, Release No. 34-86031; File No. S7-07-18, found at <https://www.sec.gov/rules/final/2019/34-86031.pdf>, page 636.

⁷ Public Statement by SEC Chairman Jay Clayton: *Regulation Best Interest and the Investment Adviser Fiduciary Duty: Two Strong Standards that Protect and Provide Choice for Main Street Investors* (July 8, 2019), available at <https://www.sec.gov/news/speech/clayton-regulation-best-interest-investment-adviser-fiduciary-duty> (the "Public Statement")

⁸ Securities and Exchange Division, *Duties of Brokers, Dealers and Investment Advisers* Release No. 34-69013 (March 1, 2013) (Fidelity comments available at <https://www.sec.gov/comments/4-606/4606-3117.pdf>).

⁹ Public Statement by SEC Chairman Jay Clayton: *Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers* (June 1, 2017), available at

its Fiduciary Rule¹⁰ (“DOL Fiduciary Advice Rule”). Fidelity has long advocated for the SEC to develop standards of conduct for broker-dealers and investment advisers when providing investment advice to retail investors.¹¹

In our view, Reg BI establishes an effective framework for broker-dealers to address potential conflicts of interest and significantly advances the goal of ensuring that retail investors understand their broker-dealers’ and investment advisers’ fees, services and obligations. Reg BI imposes a practical standard of conduct tailored to the brokerage model, with an enhanced standard of conduct for broker-dealers. We believe this standard significantly enhances the obligations already applicable to broker-dealers under the Securities Exchange Act of 1934, as amended (“Exchange Act”), and FINRA’s rules, as well as the common law of agency and trust forming the foundation of the federal securities laws.¹²

As a result, we urge the Division to reconsider the need for a state-specific regulation that differs from Reg BI. Advice providers cannot reasonably be expected to alter the fundamental characteristics and methodology of their advice to Massachusetts residents, and we believe a patchwork of inconsistent state-specific regulation in this area would have the unintended consequence of reducing services and increasing costs for Massachusetts investors. That is directly contrary to what we believe is the Division’s goal.

Problems with the Proposal

Unlike Reg BI, the Proposal in its current form suffers from several problems that would make it difficult, and in key respects impossible, for broker-dealers to continue to provide incidental brokerage advice. Many of these problems are described in detail in the comment letter submitted by the Securities Industry Financial Markets Association (“SIFMA”) on July 26, 2019. We agree with the views of SIFMA in its letter, and also wish to highlight the following issues, which we believe are critical.

<https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31> (the “Public Statement”) (Fidelity comments available at <https://www.sec.gov/comments/ia-bd-conduct-standards/cll4-2216673-160638.pdf>).

¹⁰ *Fidelity Investments* comment letter submitted July 21, 2015 at: <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00658.pdf>; *Fidelity Investments* comment letter submitted September 24, 2015 at <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/03089.pdf>; *Fidelity Investments* comment letter submitted April 17, 2017 at: <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB79/01385.pdf>; and *Fidelity Investments* comment letter submitted August 7, 2017 at <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00545.pdf>.

¹¹ See Letter to Ms. Elizabeth M. Murphy Re: Duties of Brokers, Dealers and Investment Advisers, Release No. 34-69013; IA-3558; File No. 4-606 (July 5, 2013); Letter to The Honorable Jay Clayton Re: Standards of Conduct for Investment Advisers and Broker-Dealers (August 11, 2017).

¹² Reg BI Proposal at 21640-1.

1. It is impossible to comply with a “Best of all available options” standard.

The Proposal would require that any advice given, and any remuneration received, be “the best of the reasonably available options.” This requirement is unprecedented in financial regulation and is not only higher than long-standing common law fiduciary requirements, but objectively impossible for advice providers to meet. Recommendations depend on subjective judgments and opinions, unique to each investor and their particular financial needs and preferences. In very few cases is it possible to identify a single, objectively “best” security or investment strategy for a customer. Different advice providers inevitably have different, but nonetheless equally reasonable, views and opinions on how to invest specific funds or manage a portfolio over time, and of the relative importance of different factors involved in reaching a recommendation.¹³ That is, of course, impossible, and requiring advice providers to identify the “best” security or investment strategy, at risk of breaching a fiduciary duty, is simply unworkable.

2. The Proposal does not define “best”.

Although it would impose an entirely new and unprecedented standard of identifying the “best” security, account type, or investment strategy in every circumstance, the Proposal itself does not provide any definition of “best”. Ambiguity on this point, which is at the core of the Proposal, would leave advice providers with no reasonable means to comply. As both the SEC and the DOL explicitly recognized, it is not enough to identify the cheapest available option because many other factors besides cost are relevant to an investment decision.¹⁴ Indeed, advice providers who always recommended the cheapest available option would be derelict in their responsibility to the investor, and for that reason no federal or state financial regulation we are aware of has ever contained such a requirement.

We urge the Division to reconsider this requirement and to remove it from the Proposal. At a minimum, if the Proposal contains a requirement to identify the “best”, the Proposal must also provide an objective, workable definition of “best” that takes into account the variety of factors involved in formulating advice and the inherently forward-looking nature of investment advice. Advice providers should not be subject to potential liability, in hindsight, for failing to predict how any security or investment strategy would ultimately perform over time, or for failing to predict what the Division or others would retrospectively consider to have been the “best” in any particular case.

¹³ Indeed, if it were possible to identify a single “best” security or strategy, there would be little need for investment advice at all; investors could simply be provided with a list of the “best” securities and strategies. That is, of course, impossible.

¹⁴ “Nevertheless, we emphasize that while cost must be considered, it should never be the only consideration. Cost is only one of many important factors to be considered regarding the recommendation.” See “Regulation Best Interest: The Broker-Dealer Standard of Conduct,” Final rule, Release No. 34-86031; File No. S7-07-18, found at <https://www.sec.gov/rules/final/2019/34-86031.pdf>, page 38. “Consistent with the Department’s prior interpretations of this standard, the Department confirms that an Adviser and Financial Institution do not have to recommend the transaction that is the lowest cost or that generates the lowest fees without regard to other relevant factors.” See “Best Interest Contract Exemption,” 81 FR 21001, found at <https://www.federalregister.gov/documents/2016/04/08/2016-07925/best-interest-contract-exemption>, page 21030.

3. The requirement for ongoing monitoring of advice given in brokerage accounts would prevent broker-dealers from providing advice to Massachusetts investors.

While the Proposal suggests on the one hand that a fiduciary duty for “a standalone recommendation” is limited to the time it is made, it further states that “If a broker-dealer, agent, or adviser makes ongoing recommendations *or provides investment advice, in any capacity, to a customer or client*, or receives ongoing compensation in connection with the recommendation or advice, *the fiduciary duty shall be deemed an ongoing.*” (emphasis added). To fulfill this ongoing fiduciary duty, a broker-dealer would be required to perform ongoing monitoring of a customer’s account.

This provision is in direct conflict with federal securities laws and would prevent broker-dealers from providing free advice to Massachusetts customers at all. While broker-dealers can provide certain limited account monitoring, they are prohibited under Section 202(a)(11)(C) of the Investment Advisers Act of 1940 from providing the continuous monitoring that the Proposal would require. The Advisers Act provides a limited exemption from investment adviser registration for broker-dealers giving advice only if, among other things, the “performance of such services is solely incidental to the conduct of his business as a broker or dealer.”¹⁵ The SEC has made clear that broker-dealers cannot routinely provide ongoing account monitoring advice services in light of this statutory requirement because such services are a significant advisory function that cannot be considered “solely incidental” to a brokerage business.¹⁶

The SEC recently reaffirmed this requirement in releasing the “Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser,”¹⁷ which states that Section 202(a)(11)(C)’s exemption would “*not permit a broker-dealer to agree to monitor a customer account in a manner that in effect results in the provision of advisory services that are not in connection with or reasonably related to the broker-dealer’s primary business of effecting securities transactions, such as providing continuous monitoring*” (emphasis added). As Chairman Clayton explicitly noted in the Public Statement, “let me be clear about what such a requirement would mean: *imposing an ongoing monitoring obligation would effectively prohibit brokers from providing retail customers with advice without registering as investment advisers*. Again, that would mean less access and choice, and higher costs, for retail customers.”¹⁸ (emphasis added).

In short, the Proposal would effectively limit Massachusetts customers to using investment advisers, and consequently to pay advisory fees, for all investment advice. Free

¹⁵Section 202(a)(11)(C) of the Investment Advisers Act of 1940.

¹⁶ See Section 202(a)(11)(C) of the Investment Advisers Act of 1940.

¹⁷ Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser, SEC Release No. IA-5249, found at: <https://www.sec.gov/rules/interp/2019/ia-5249.pdf>.

¹⁸ Public Statement by SEC Chairman Jay Clayton: *Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers* (June 1, 2017), available at <https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31>

brokerage advice incidental to transactions would effectively be eliminated. We do not believe this was the Division's intent.

4. The requirement to “avoid conflicts of interest”, and not just mitigate such conflicts as is required in Reg BI, will prevent recommendations of fixed income securities, including Massachusetts municipal bonds.

Fixed income securities are almost exclusively offered on a “principal” basis, where a broker-dealer will take the security into its inventory and then sell the bond from its inventory to a customer. Many fixed income trades are done as “riskless principal” trades, in which a broker-dealer buys a bond into its inventory, and then immediately sells that bond to a customer, pursuant to a customer's order (i.e. the broker-dealer is not purchasing and holding the bond, speculating that they will be able to sell it to a customer at a higher price). Principal trading, by its nature, presents a conflict of interest, as the broker-dealer is selling its inventory to the customer. Reg BI acknowledges this market structure, and requires that such conflicts be mitigated; the Proposal, in requiring that all such conflicts be avoided, does not.

Since the Proposal will effectively prohibit advice to be provided in principal fixed income trades, this will no longer allow firms to assist customers in, for example, structuring a bond ladder, which is a common request for investors looking to hedge risk over time. Additionally, firms will not be able to recommend new issue municipal securities issued by Massachusetts municipalities, which are also offered on a principal basis. This will likely have a severe negative impact on not only investors but on issuers of municipal bonds, as principal trades are the most common form of trading in the municipal market. With brokers being unable to provide assistance, it is very likely demand for municipal bonds will decrease, making it increasingly expensive for municipal bond issuers.

The Proposal Would Harm Massachusetts Investors

As described above, we believe the Proposal would likely result in less choice, less access, and greater costs to Massachusetts investors. Indeed, the DOL Fiduciary Advice Rule illustrates the negative impact that imposing unworkable restrictions can have on customer choice. As SIFMA reported in its letter to the DOL on August 9, 2017, pursuant to a study conducted by Deloitte and Touche, preparation for the DOL Fiduciary Advice rule resulted in:

1. “[A]s of the Rule's first applicability date on June 9th, 53% of study participants reported limiting or eliminating access to brokerage advice for retirement accounts, which the firms estimate impact 10.2 million accounts and \$900 billion AUM.”
2. “Roughly 95% of study participants indicated that they have reduced access to or choices within the products offered to retirement savers because of efforts to comply with the Rule¹⁹.”

¹⁹ Products affected include mutual funds, annuities, structured products, fixed income, private offerings, and more, impacting an estimated 28.1 million accounts. Examples of the reduction in mutual fund availability include: 1) the elimination of no-load funds from brokerage platforms; 2) the elimination of mutual funds held directly at the mutual fund company; 3) reduced product offerings; and 4) elimination of other share classes.

Fidelity strongly supports the preservation of investment access and choice for our customers, which we believe the SEC's Reg BI accomplishes through its stringent, clear, and balanced approach. Reg BI clearly recognizes that broker-dealers serve a critical role for customers, and it is thoughtfully crafted to further the SEC's express goal of preserving broker-dealers' ability to provide investment advice without an additional fee. This is especially important for customers who cannot afford additional advisory fees or who need only occasional guidance, who might otherwise forego seeking valuable advice entirely.

In contrast, the Proposal in its current form would result in the elimination of investment products, an increase in fees and costs, and the elimination of investment advice in brokerage accounts, all of which would be harmful to Massachusetts investors. This would be particularly harmful to investors who need investment advice the most, as an estimated 98% of low- and middle-income individuals receiving personalized investment assistance obtain that assistance from broker-dealers without any advisory fee.²⁰

Given the harm that the Proposal would have to Massachusetts investors, we urge the Division to retract the Proposal and await full implementation of Reg BI. As firms are in the process of preparing for full compliance with Reg BI, we suggest that the Division study the additional protections afforded Massachusetts investors by Reg BI before making any future proposals that might impose a higher standard on investment advice.

Fidelity is happy to provide further information, participate in any direct outreach efforts the Division undertakes, or respond to questions the Division may have about our comments.

Sincerely,



David Forman
Chief Legal Officer
Fidelity Brokerage Services LLC

²⁰ Oliver Wyman report: Assessment of the impact of the Department of Labor's proposed "fiduciary" definition rule on IRA consumers (April 12, 2011).

cc: The Honorable Jay Clayton, Chair
The Honorable Robert J. Jackson Jr., Commissioner
The Honorable Allison H. Lee, Commissioner
The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner

Dalia Blass, Director, Division of Investment Management
Brett Redfearn, Director, Division of Trading and Markets