MARKETCOUNSEL®

August 6, 2019

VIA ELECTRONIC MAIL SUBMISSION

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: Preliminary Solicitation of Public Comments: Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives

Dear Secretary Galvin,

We commend and support the Massachusetts Securities Division (the "Division") efforts to raise standards of conduct for financial professionals. These efforts can make the financial marketplace stronger for all Massachusettsans. MarketCounsel is adding our support to placing a fiduciary duty on broker-dealers while providing comments on other areas that we believe require additional guidance.

For perspective, MarketCounsel is a business and regulatory compliance consulting firm to some of the country's preeminent independent investment advisers. In addition, our affiliated law firm, the Hamburger Law Firm, renders legal counsel to entrepreneurial investment advisers, broker-dealers, hedge funds, family offices, and registered securities personnel. From its roots in 2000, MarketCounsel has been steadfast in its mission to deliver elegant solutions to the most substantial challenges faced by entrepreneurs in this fast-growing and highly-regulated industry.

We write today to share our opinions with the Division's proposed Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives (the "Proposal") in light of recent federal action in this area.

UNDERSTANDING THE CHALLENGE

Broker-dealers who provide advice to retail investors have posed regulatory challenges for at least the past twenty-five years. Their entry into fee-based services, along with a new emphasis on the advice they provided that was supposedly incidental to those transactions, started to blur the lines between securities sales and investment advice. During this time, the SEC sat on the sidelines as broker-dealers started using titles for their agents such as "advisors," "financial consultants," and "financial planners," to name a few. Clearly, those titles implied to consumers that they could reasonably expect advisory (rather than sales) services from their registered representative.

When SEC Commission Jay Clayton unveiled the SEC's proposed Regulation Best Interest rule ("Reg BI") in April 2018, it marked a step towards meeting these challenges. Understandably, market participants greeted the proposal with mixed reactions. Consumers continued, however, to be confused by differing standards of care and state agencies across the country, like the Division, began to take action to impose more regulations on financial professionals.

When the Division circulated the proposal for preliminary comment, it became the latest state, to announce a proposal for a state level fiduciary rule.[1] The Division's notice emphasized that it was acting because the SEC's rulemaking, "fails to establish a strong and uniform fiduciary standard."[2] The Division made clear that it was undertaking its proposal to address the long-standing danger and harms retail investors, "[t]he need for a conduct rule mandating that investment advice must be provided under a fiduciary standard has been recognized for many years."[3]

IMPACT OF REGULATION BEST INTEREST ("REG BI")

On June 5, 2019, the SEC approved its rulemaking release for standards of conduct for broker-dealers and investment advisers. Reg BI uses the undefined "best interest" term, a term synonymous with an investment adviser's fiduciary duty, but also makes it clear that this "best interest" is not a true fiduciary duty. Consumer confusion is a big part of what Reg BI was supposed to cure, yet using the same words for two different standards will undoubtedly continue to confuse investors and further blur the regulatory lines between broker-dealers and investment advisers.

On one hand, we are reticent to recommend additional requirements on broker-dealers that will create a difficult to follow patchwork of federal and state laws. MarketCounsel has been one of the voices that expressed concern over states adopting a fiduciary duty on broker-dealers while the SEC was contemplating action. We know that increased compliance costs would be passed to investors in either the form of higher fees or a reduction of access to investing opportunities. On the other hand, we remain concerned that the SEC's Reg BI will result in further erosion of the distinction between investment advisers and broker-dealers. Clients will get less protection for their broker-dealer relationships than investment adviser relationships ("best interest," but not "fiduciary best interest") without any ability to understand the difference.

Our concerns over Reg BI's flaws eclipse our concerns about the additional burdens that broker-dealers will face. Broker-dealers have had decades to stop adding to consumer confusion, but they went full speed towards offering adviser-like services and even calling themselves "advisors." Broker-dealers were involved in supporting and shaping Reg BI and the SEC came up with a framework that results in broker-dealer and investment adviser standards that are indistinguishable to consumers, but provide less protection.

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[1] Thrasher, Michael. "Massachusetts Seeks Comments for Its Own 'Fiduciary Rule'." Wealth Management, 17 June 2019, www.wealthmanagement.com/industry/massachusetts-seeks-comments-its-own-fiduciary-rule.

[2] "Preliminary Solicitation of Public Comments: Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives." Securities: Preliminary Solicitation of Public Comments: Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives. 15 June 2019. 25 July 2019 <https://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/fiduciaryconductstandardidx.htm>.

[3] *Ibid.*

To be blunt, Reg BI is a consumer trap. It is time to put an end to the confusion. While MarketCounsel has always supported darkening the line between broker-dealers and investment advisers, that is no longer an option. Therefore, MarketCounsel supports the Division's attempt to protect investors and end confusion and applauds the imposing of a true fiduciary duty on broker-dealers.

CONCERNS THAT NEED CLARITY OR REVISIONS

Before moving forward with a formal rule, however, MarketCounsel respectfully submits that the Division should address the following concerns with the proposal:

Explicitly exempt SEC advisers and their representatives

The Division's rule release states that for the term "adviser" there, "is a rebuttable presumption that such term includes all investment advisers and investment adviser representatives, as well as other persons who charge fees based on assets under management or portfolio performance for rendering investment advice."[4] However, Massachusetts regulation excludes SEC registered investment advisers from its definition.[5] The definition of "investment adviser representatives" includes associates of SEC-registered investment advisers, but subject to the limitations of the Investment Advisers Act of 1940, as amended (the Advisers Act).[6] The Advisers Act standards require that investment advisers follow a duty of care and duty loyalty and act in the customer's best interest at all times.[7] Adding a similar state rule governing investment adviser conduct creates the possibility that the contours and nuances of the rules develop differently and subsequently SEC advisers would be unintentionally subject to two fiduciary standards. Therefore, MarketCounsel requests that Massachusetts' final rule explicitly exempt SEC registered investment advisers and their representatives from the Massachusetts fiduciary requirements.

Safe Harbor for state registered investment advisers that follow a fiduciary duty in their home state

We remain concerned with a patchwork of state regulations. It will be difficult for state registered investment advisers that are registered in multiple states to comply with different fiduciary rules depending upon where their clients are located. Even just a few states drafting their own rules creates confusion. For example, Nevada's fiduciary proposal does not define the terms "fiduciary duty" or "best interest" despite giving several examples of what is a fiduciary violation and what is not a *per se* violation.[8] Addressing fiduciary duty in this way is complicated. Meanwhile the Division's rule uses "the prudent person" standard of care and a duty of loyalty that requires advice, "without regard to the financial or any other interest of the broker-dealer, agent, adviser, any affiliated or related entity and its officers, directors, agents, employees, or contractors, or any other third-party."[9] While both Nevada and Massachusetts may have the same intent, since they articulate the standard differently, it is possible that the contours of fiduciary law will develop differently in each state.

The burden of inconsistent regulations is a challenge. Our main concern is for small, state registered investment advisers that may have to register in multiple states. These firms often have less resources than bigger investment advisers. They act in their clients' best interests, but conflicting or inconsistent laws will make compliance difficult. MarketCounsel believes it will be very difficult for Massachusetts state registered investment advisers to understand and prepare for standard of care nuances amongst the jurisdictions in which they are registered. Therefore, we are still in favor of Massachusetts and other states working with each other through NASAA to develop model fiduciary rules. In addition, MarketCounsel

[4] Proposed 950 CMR 12.207(a)
[5] M.G.L. c. 110A, §401(m)(2)
[6] M.G.L. c. 110A, §401(n)(B)
[7] SEC Interpretation Regarding Standard of Conduct for Investment Advisers, Release No. IA-5248, p.7.
[8] *Notice of Draft Regulations and Request for Comment*. 18 Jan 2019 https://www.nvsos.gov/sos/home/showdocument?id=6156.
[9] Proposed 950 CMR 12.207(c)(1)

suggests that Massachusetts provide a safe harbor for state registered investment advisers and their financial professionals who follow a principles-based advice standard drawn from the concepts of a fiduciary duty that are established by the regulator where the firm's principal office and place of business (as defined in Form ADV) is located.

Duty of care confusion

The proposal states that, "the duty of care requires a broker-dealer, agent, or adviser to use the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use."[10] Under the federal fiduciary standards, investment advisers are subject to a "reasonableness" standard.[11] The term "prudent" presents the possibility for confusion and legal uncertainty because it is term that is predominantly interpreted in other legal regimes.[12] To avoid confusion, the final rule should model the SEC language and use the reasonable person standard.

Unclear ongoing duty requirements

The proposal seeks to impose an ongoing obligation for broker-dealers and advisers, "[i]f 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."[13] However, it is not clear what "investment advice" is. We also need clarity concerning the meaning of "ongoing obligation." For example, is a financial plan "investment advice" and if so does that mean that the broker-dealer (or investment adviser) now has to update previous advice in perpetuity? Since federal regulation requires broker-dealers to disclose the ongoing nature of their services to customers, there could be situations where a broker-dealer discloses that the relationship has no ongoing component under federal law, but the Division interprets that the broker-dealer is giving investment advice and therefore holds the broker to an ongoing duty under state law.[14] MarketCousnel believes that such an ongoing responsibility would be overreaching. MarketCounsel respectfully suggests that the Division should hold broker-dealers (and investment advisers as well) only to the duties that they disclose, or agree to, with their clients.

Missing duty for "non-customers"

Proposed new subsection (c) excludes certain entities and individuals from the definition of "customer."[15] These types of institutional customers may not need the same protections as retail customers, but this rule is intended to protect clients and eliminate confusion. If these types of customers are excluded from broker-dealer fiduciary responsibility, they should also be excluded from that duty for registered investment advisers.

No additional disclosure requirement for broker-dealers

The proposal intends to require investment advisers and broker-dealers to act as fiduciaries. However, it does not include any disclosure requirements for broker-dealers. If the final rule intends to hold broker-

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[10] Proposed 950 CMR 12.207(c)(1)

[11] SEC Interpretation Regarding Standard of Conduct for Investment Advisers. Release No IA-5248. p.13. *The duty to provide advice that is in the best interest of the client based on a reasonable understanding of the client's objectives is a critical component of the duty of care.*

[12] Regulation Best Interest. Release: The Broker-Dealer Standard of Conduct, Release No, 34-86037 p. 256-257. *Prudence is an ERISA term based on trust law that is not generally used under the federal securities laws.*

[13] Proposed 950 CMR 12.207(b)(1)(ii)

[14] SEC Form CRS. Release. Release Nos. 34-86032; IA-5247 p. 94 "*The final instructions require all firms to address the following topics in the description of their services: (i) monitoring."*

[15] Proposed 950 CMR 12.207 (d)

dealers to a standard beyond the federal level, then it should specify how broker-dealers are to make additional disclosures since disclosing conflicts of interest is an integral part of a fiduciary duty.

MAINTAINING CONSUMER CHOICE

While MarketCounsel's clientele is comprised of registered investment advisers, we believe there is a meaningful role within the financial services ecosystem for broker-dealers that benefits financial markets and consumers. The number of broker-dealer firms has declined 20% over the last decade.[16] Specifically, the number of independent broker-dealers has declined 28%, from 1,255 in 2005 to only 904 in 2015.[17]

Many broker-dealer groups claim that smaller investors will no longer be serviced should broker-dealers be held to a fiduciary duty. Some firms have even threatened to pull out of states that impose a fiduciary duty upon them. But Reg BI has been embraced by the broker-dealer industry. Many broker-dealers and their lobbying groups have said, or implied, that Reg BI is as strong as the Advisers Act's fiduciary duty. If Reg BI is so close to the Advisers Act's fiduciary duty, the slight uptick to a true fiduciary duty would pose no meaningful harm to those firms. Therefore, it is hard to recognize their threats as credible. In fact, they seem completely illogical.

CLOSING REMARKS

At MarketCounsel we admittedly champion the entrepreneurial independent investment adviser as the true bastion of objective investment advice. But we appreciate the utility of the broker-dealer model, too. We support a true fiduciary standard for any investment professional who offers or appears to offer investment advice to retail investors. Reg BI does not provide this protection and results in further confusion to consumers. That is why we support Massachusetts' fiduciary proposal.

We hope that our comments made on behalf of us and our independent investment adviser clients, who serve investors across the country, are beneficial to this process. Should you have any questions or require any additional information regarding any of the foregoing, we remain available at your convenience using any of the methods below.

Best regards,
MARKETCOUNSEL, LLC

Brian Hamburger, JD, CRCP
President and CEO

Daniel Bernstein
Chief Regulatory Counsel

[16] "Statistics." *Types of Investments.* FINRA.org, www.finra.org/newsroom/statistics#reps.

[17] Fidelity Clearing & Custody Solutions. "How Independent Broker-Dealers Use M&A to Build Their Businesses." *About Fidelity Clearing & Custody Solutions*, Fidelity Clearing & Custody Solutions®, 26 Nov. 2018, clearingcustody.fidelity.com/app/literature/view?itemCode=9882259&renditionType=pdf.