Consumer Federation of America

January 6, 2020

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

Re: Solicitation of Comments on Proposed Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives

Dear Secretary Galvin:

We are writing on behalf of the Consumer Federation of America (CFA) to express our strong support for the Securities Division's proposal to hold all investment professionals to a uniform fiduciary standard of care when providing investment advice and recommendations.[1] CFA has long advocated adoption of a strong, uniform fiduciary standard for broker-dealers and investment advisers when providing personalized investment advice to individual investors.[2] Indeed, with tens of billions of dollars in investor losses each year on the line, we have identified this as the single most important policy change needed to enhance protections for average investors. These investors turn to investment professionals for advice on how to invest for retirement or fund their children's education, unaware that all too often their trusted "financial adviser" is really just a salesperson, incentivized to place their own financial interests ahead of the customer's interests. Unfortunately, after decades of delay and inaction, the SEC finally acted last June, only to adopt a vague, industry-friendly standard that offers the promise of improved protections for investors, but fails to deliver on that promise.[3]

In light of that failure in leadership at the SEC, it is left to the states to deliver the strong fiduciary protections their citizens need and deserve. If adopted without weakening amendments, your proposal would not only improve protections for the citizens of Massachusetts, it would

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[1] Consumer Federation of America (CFA) is a non-profit association of more than 250 national, state, and local pro-consumer organizations. It was formed in 1968 to advance the consumer interest through research, advocacy, and education.
[2] *See, e.g.*, Letter from Barbara Roper, Director of Investor Protection, CFA, to Arthur Levitt, Chairman, SEC, Oct. 26, 1999, http://bit.ly/2eXC5T4; Letter from Barbara Roper and Micah Hauptman, CFA, to Brent J. Fields, Secretary, SEC, Aug. 7, 2018, https://bit.ly/2T4eJgm.
[3] *See, e.g.*, SEC Commissioner Robert J. Jackson Jr., Statement on Final Rules Governing Investment Advice, June 5, 2019, https://bit.ly/2XJsaSp; Brief for Better Markets and Consumer Federation of America as Amici Curiae Supporting Petitioners, *XY Planning Network; Ford Financial Solutions v. SEC* (No. 19-2886).

provide a model that other states could follow to extend these protections to their own citizens. We greatly appreciate your willingness to lead that effort and strongly support the proposed rule.

Our more detailed comments on the proposal follow. CFA was among 16 pro-investor organizations that filed a comment letter with the Division in July voicing support in response to the preliminary request for comment.[4] In it, we explained why a fiduciary standard is appropriate for broker-dealers who routinely hold themselves out and function as advice providers in positions of trust and confidence with their customers, and why it would be inappropriate for Massachusetts to defer to Reg BI, which is not a true fiduciary standard and will not meaningfully change harmful industry practices or improve protections for investors. Rather than simply repeat the points we made in that letter, we incorporate it by reference here.

1) Key Industry Arguments Against State Action Are Unfounded

Before addressing the specifics of the proposal, however, one argument put forward by industry opponents of state action deserves some additional attention. That is the argument that state action undermines uniformity, which will result in increased investor confusion. In reality, however, the same industry groups that make this argument strongly support an SEC rule that maintains different standards of conduct for broker-dealers and investment advisers. And it does so while permitting brokers to continue to market themselves in ways that make any functional differences between their services and those of a fiduciary adviser indistinguishable to the average investor. That is a recipe not only for investor confusion, but for outright deception, made easier because the SEC actually requires brokers and advisers to describe their different standards of conduct using virtually identical language in the new Customer Relationship Summary.[5] If industry groups were genuinely concerned about investor confusion, they could not have supported such a rule.

In contrast, under the Massachusetts proposal, investors would not have to know whether their investment professional is a broker-dealer or an investment adviser in order to try to figure out what type of regulatory protections apply. They would be entitled to a strong fiduciary standard of care regardless of those distinctions. And, as discussed further below, that duty would follow the contours of the relationship, rather than being arbitrarily dictated by the regulatory status of the account. In an ideal world, of course, all U.S. investors would receive those same protections under a uniform federal standard. But, in the absence of effective federal action to provide those uniform protections, the kind of uniformity across industry categories provided by the Massachusetts proposal is far more important to combatting investor confusion than uniformity across state lines would be.

Similarly, we strongly concur with statements in the Request for Comment rebutting industry arguments that the proposal would limit investor "choice" or "access" to beneficial products and services. As discussed further below, the proposed fiduciary standard provides more than adequate flexibility to enable firms to adapt it to the broker-dealer business model.

[4] Letter from Alliance for Retired Americans, *et al*., to Secretary Galvin, Massachusetts Securities Division, July 26, 2019, https://bit.ly/37Kq49L.

[5] *See* Form CRS Relationship Summary; Amendments to Form ADV, 84 Fed. Reg. 33,532-33,533 n.507-08 (July 12, 2019).

The only firms that would struggle to comply with this standard are those whose profitability depends on taking advantage of vulnerable, financially unsophisticated investors in order to profit unfairly at their expense. We therefore strongly agree with the statement in the Request for Comment that, "When preserving 'choice' means preserving the option to choose opaque, poorly-understood products that are sold via heavily conflicted advice, the benefits of such 'choice' are illusory."

Under the Massachusetts proposal, brokers who compete for business as trusted advisers would be held to the fiduciary standard appropriate to that role. That would simultaneously help to ensure that investors have better choices available to them and make it easier for investors to make an appropriate choice. The good news is that there are more providers than ever offering investment advice at an affordable price under a fiduciary standard of care. As a result, investors no longer have to accept the false "choice" of trading away fiduciary protections in order to get "access" to a conflict-driven sales pitch masquerading as advice.

2) The Standard is Appropriately Broad in Scope

One of the key strengths of the Massachusetts proposal is that it would apply to all the services investors are likely to perceive and rely on as trusted advice. Specifically, the proposal applies to "all investment advice" and "recommendations" provided by a broker-dealer, agent, investment adviser, or investment adviser representative, acting in their professional capacity, regarding "any investment strategy, the opening of or transferring of assets to any type of account, or the purchase, sale, or exchange of any security, commodity, or insurance product." As such, it will help to insure that investors are fully covered in all their interactions with their financial professionals. For example, this broadly inclusive language should help to make clear that not only individual product recommendations, but also the development of investment strategies to meet the customer's goals, must be designed without regard to the broker or adviser's interests to serve the best interests of the investor. Similarly, key recommendations such as whether to roll over money from a 401(k) plan or what type of account to open, would also be covered.

In particular, we strongly support the decision to include recommendations regarding investments beyond securities, including commodities and insurance products, in the standard. As the proposal notes, these products are often included in the product menus of broker-dealers and investment advisers and offered in conjunction with advisory services. While regulators have taken the position that investment advisers' fiduciary duties apply to the entire advisory relationship, the same is not true of either Reg BI or the FINRA suitability standard. The reality is that most investors simply are not equipped to distinguish securities from these closely related non-securities investments in order to determine what regulatory standard applies, nor would most investors expect regulatory protections to differ based on the product type.

Without the broad coverage provided in the Massachusetts proposal, however, investors would bear the burden of determining when a product being recommended is subject to the fiduciary standard, and when it is not. For example, under Reg BI, investors will have to determine whether their account is an advisory account or whether it is a brokerage account and what type of product is being recommended to know what regulatory standards apply. Worse, without the broad coverage of the Massachusetts proposal, brokers seeking to profit unfairly at customers' expense will have a strong incentive to recommend high-cost, high-compensating non-securities products in order to evade the rule. For certain brokers that offer a limited menu of products dominated by annuities, for example, the incentive will be to shift from variable annuities, which are regulated as securities, to fixed indexed annuities, which are not.[6]

This broad coverage is an important way in which the Massachusetts proposal improves on the SEC's approach in Reg BI. As such, it offers important protections Massachusetts investors would not receive absent adoption of this proposal. We urge you to retain this broad coverage in the final rule.

3) The Standard Appropriately Follows the Contours of the Relationship

Another important strength of the Massachusetts proposal is that it recognizes that it is possible to apply a uniform fiduciary standard to a variety of business models by adopting a flexible, facts-and-circumstances based application of that standard. Under this approach, the fiduciary obligation extends throughout the provision of advice or recommendations, as well as the implementation of that advice, regardless of business models. But it does not impose duties that are not relevant or appropriate to that business model. So, for example, the Massachusetts proposal appropriately imposes an ongoing duty on brokers in instances where the broker "is *acting like* an investment adviser, or where the broker-dealer or agent leads the customer or client to reasonably believe that the broker-dealer or agent will act in such a manner," but imposes no such duty where there is no such implication that the investor will receive ongoing advice or account management.

As we discussed in our earlier investor group comment letter, brokers routinely hold themselves out as providing ongoing advisory services, and encourage relationships of trust and confidence, through the titles they use and the way they describe and market those services. This creates a reasonable expectation among investors that the broker will provide at least periodic monitoring of the account. Under Reg BI, however, brokers would continue to be able to hold themselves out in this way without incurring any ongoing duty to the customer. As a result, Reg BI actually weakens common law fiduciary protections investors currently receive from courts and arbitration panels, particularly in situations where a vulnerable investor relies on the broker as a trusted adviser.[7]

[6] As we explained in a recent comment letter sent jointly with Center for Economic Justice (, the NAIC's proposed revisions to its model suitability standard for annuities are completely inadequate to protect investors from abusive sales practices too often associated with these products. For example, the revised model would allow insurance agents to meet their "best interest" obligation by recommending any annuity that meets the consumer's need, in other words, by making a suitable recommendation. And, while the proposal includes new provisions to address conflicts of interest, cash and non-cash compensation are exempt from the definition of material conflicts. In short, the insurance standard is even weaker than Reg BI and even more likely than the SEC standard to mislead investors into expecting protections it does not deliver. Letter from Birny Birnbaum, Executive Director, Center for Economic Justice, and Barbara Roper, Director of Investor Protection, CFA, to Doug Ommen, Chairman, Life Insurance and Annuities (A) Committee, NAIC, Dec. 4, 2019, https://bit.ly/39GkGGm.

[7] Letter from Jill I. Gross, to the SEC, March 11, 2019, https://bit.ly/31v15os.

In contrast, the Massachusetts proposal would make clear that brokers that use titles and portray their services in ways that create a reasonable expectation of ongoing, advisory services would have an ongoing duty to the customer. At the same time, it clarifies that brokers that truly limit themselves to episodic recommendations and do not create a reasonable expectation of ongoing monitoring or account management would have no such duty. Brokers would then have a choice: do the marketing benefits of portraying themselves as trusted advisers in ongoing relationships outweigh any additional costs or burdens that doing so entails? They could then tailor their actions, including the titles they adopt and the marketing they engage in, accordingly.

This provision of the proposal is essential to ensuring that investors receive regulatory protections that match their reasonable expectations. We therefore strongly urge you to retain this provision in the final rule without weakening amendments.

4) The Proposal Adopts an Appropriately Flexible Approach to Application of the Duty of Care

As noted above, the fiduciary duty is a facts-and-circumstances-based standard, where the specific application of the standard will vary depending on the nature of the relationship, the services provided, and the products recommended. The proposal reflects that by adopting a flexible, principles-based approach to application of the duty of care. It will then be up to firms and their representatives to determine what level of analysis of the client's situation and of the available options to meet those needs is appropriate in light of the services being provided. This will vary greatly depending, for example, on whether the broker or adviser has been engaged to provide ongoing, comprehensive financial planning, a one-time recommendation to establish a college savings plan, or something in between. So, while there is certainly overlap between the obligations a fiduciary will have under the duty of care to engage in a prudent process and the obligation a broker has under FINRA know-your-customer and suitability rules, it does not follow that compliance with FINRA rules will fully satisfy the fiduciary duty of care in all circumstances.

The Division is therefore right to resist pressure to provide safe harbors based on compliance with FINRA rules that may fully satisfy the standard in some instances, but not in others. We urge you to retain this principles-based approach to the duty of care in the final rule.

5) The Proposal Adopts an Appropriate Interpretation of the Duty of Loyalty

One of the key strengths of the Massachusetts proposal is that it makes crystal clear, in a way that Reg BI does not, that brokers and advisers are required to seek to minimize conflicts of interest and to act "without regard to" their financial or other interests when developing and implementing their advice and recommendations. As such, the Massachusetts reflects congressional intent, and expressed in Section 913(g) of the Dodd-Frank Act, in a way that Reg BI does not. Furthermore, as the Request for Comment notes, requiring brokers and advisers to act "without regard to" their own interests does not mean that they can't have conflicts of interest, which would be an unattainable goal. Indeed, the Division makes this clear in its discussion regarding the application of the rule to transaction-based compensation, such as commissions, and to principal transactions. On the other hand, adopting the "without regard to" language should help to restrict firms' ability to artificially create incentives that undermine compliance with the fiduciary standard, something Reg BI fails to do.

Importantly, the proposal makes clear that, even after conflicts have been disclosed and appropriately managed, the broker or adviser still has an obligation to do what is best for the customer. As the Request for Comment explains, "all advice and recommendations must be provided with complete focus on what is best for the customer or client." This distinguishes it not only from Reg BI, but from the SEC's interpretation and enforcement of the Investment Advisers Act fiduciary standard, which too often relies on disclosure alone. This is critically important, if the goal is to adopt a standard that minimizes the harmful impact of conflicts of interest on vulnerable investors.

The proposal backs up these more general provisions to ensure that conflicts don't taint the recommendations investors receive with a specific prohibition on the most harmful practices – contests, sales quotas, and special incentives programs. While Reg BI and the NAIC model rule both take a step in that direction, their prohibitions are too narrowly drawn. The likely result is that firms subject only to these rules will adjust, rather than eliminate, harmful incentives. In contrast, the Massachusetts proposal's prohibition on contests, sales quotas, and special incentives programs should be much more effective in eliminating practices that clearly encourage recommendations based on the firm's and the representatives financial interests, rather than the customer's best interests. As such, it should greatly increase compliance with the best interest standard.

We are disappointed, however, that the Division has chosen to eliminate language from the standard clarifying what it means to act in the client's best interests. A refusal to imbue the phrase "best interest" with any meaning is a key failure of Reg BI and the NAIC's proposed revisions to its model suitability rule for annuity sales. In both cases, it is difficult to identify any difference between the new "best interest" standard and the existing suitability obligation. Indeed, under the NAIC proposal, insurers would meet their "best interest" obligation by recommending a product that meets the customer's needs, which is clearly just a different way of describing a suitability standard. Meanwhile, in Reg BI, the Commission has chosen to frame the standard in language that is virtually indistinguishable from FINRA's characterization of its suitability standard.[8]

Massachusetts has an opportunity to clarify that acting in the customer's best interest means something more than suitability. Specifically, it could and should clarify that brokers and advisers satisfy their fiduciary obligation to act in the customer's best interests by recommending the investments, investment strategies, accounts, etc. that the broker or adviser reasonably believes are the best option for the customer from among the reasonably available alternatives. As we have explained at greater length elsewhere, this does not mean that the broker or adviser

[8] Reg BI prohibits a broker from "placing the financial or other interest of the broker-dealer ahead of the interests of the retail customer." Similarly, according to the FINRA suitability rule and its related guidance and case law, "In interpreting FINRA's suitability rule, numerous cases explicitly state that 'a broker's recommendations must be consistent with his customers' best interests.' The suitability requirement that a broker make only those recommendations that are consistent with the customer's best interests *prohibits a broker from placing his or her interests ahead of the customer's interests."* FINRA Regulatory Notice 11-02; FINRA Rule 2111 (Suitability) FAQ (emphasis added).

must consider options that would not provide reasonable compensation. Nor does it mean they must consider every product available in the marketplace or always recommend the lowest cost option. Finally, a careful review would not always identify a single "best" option that would uniquely satisfy the standard. Instead, in many if not most circumstances, there might be several options that would be equally good for the customer and thus equally compliant with the fiduciary standard. The key point is that a best interest standard should require the broker or adviser to narrow the acceptable options beyond those that would satisfy a suitability standard and to have a reasonable basis for believing their recommended approach is among the best available options for the customer.

Although we are disappointed that this clarification is not included in the proposal, we do take some comfort from the discussion included in the Request for Comment on how the Division anticipates enforcing the standard. Specifically, we strongly support statements that the Division intends to pursue enforcement actions where transaction-based compensation is unreasonable, where another available compensation structure would result in a greater benefit to the customer or client, or where an option is recommended despite the fact that "other options were available which would have been less remunerative" and which would have been "reasonably expected at the time of the recommendation to result in a better outcome for the customer or client." This should help to discourage brokers from recommending the investments, accounts, or investment strategies that would pay them the most when options that are better for the customer are available.

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Investors have been waiting for decades for the SEC to act to protect their interests by holding all investment professionals to a strong fiduciary standard when they provide personalized investment advice to retail investors. Unfortunately, the SEC has failed to do so, adopting instead a vague and weak standard that does more to perpetuate harmful industry practices than to protect investors from the harmful impact of conflicted advice. We greatly appreciate the willingness of states, such as Massachusetts, to step forward and fill that void. The proposal you have put forward is a strong, pro-investor rule that provides a model for other states to follow. We urge you to adopt it without weakening amendments.

Respectfully submitted,

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