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# **NOTE: New Jersey's Rule Proposal for Applying a Uniform Fiduciary Standard to Broker-Dealers: Why State Fiduciary Action is Required to Protect Investors**

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## **Reporter**

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## **Text**

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### **[\*304] Part I. Introduction**

Retail investors often do not understand the differences between investment advisers and broker-dealers and frequently expect that both are obligated to act in their best interest.<sup>1</sup> Furthermore, many investors incorrectly believe that they can fully trust their financial professional's advice because they are acting in a fiduciary-type relationship of trust.<sup>2</sup> Therefore, investors are often unaware that the person giving them financial recommendations is receiving monetary benefits in exchange for directing them to certain products.

By regulation, investment advisers owe a fiduciary duty to their clients. However, broker-dealers are subject to a "suitability" standard, which means having reasonable grounds to believe that the broker-dealer's strategy, transaction, or recommendation is "suitable" for the customer based upon a reasonable inquiry concerning the retail investor's investment objectives, financial situation, needs, and any other relevant information known by the broker-dealer.<sup>3</sup> Currently, investors remain without adequate protection from broker-dealers who, under the suitability standard, are permitted to consider their interests ahead of their client's interests when making

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<sup>2</sup> See *infra* § III; See Paul Sullivan, *In Investing, Disclosure Only Gets You So Far*, N.Y. TIMES, Feb. 9, 2012 (stating "[A]verage investors do not understand the difference between a broker (legally bound only to recommend 'suitable' investments) and someone who is working as a fiduciary (more strictly required to recommend what's best for you, not merely suitable, and disclose any conflicts).").

<sup>3</sup> See U.S. SEC. & Exch. Comm'n, Study on Investment Advisers and Broker-Dealer as Required by Section 913 of The Dodd-Frank Wall Street Reform and Consumer Protection Act 93-101 (Jan. 2011) [hereinafter 913 STUDY] (citing studies indicating that investors generally do not understand the differences between advisers and broker-dealers regarding the services they provide and the standards of conduct to which they are subject).

<sup>4</sup> FINRA Rule 2111, available at [http://finra.complinet.com/en/display/display\\_viewall.html?rbid=2403&element\\_id=9859&print=1](http://finra.complinet.com/en/display/display_viewall.html?rbid=2403&element_id=9859&print=1); See *infra* § II.

[\*305] investment recommendations. <sup>5</sup>To better protect investors, New Jersey has proposed a new rule and amendment to its rules to require all financial professionals -- including broker-dealers, agents, investment advisers, and investment adviser representatives -- to be subject to a fiduciary duty. <sup>6</sup>

This paper will attempt to determine the potential efficacy of New Jersey's rule proposals [N.J.A.C. 13:47A-6.3](#) and N.J.A.C. 13:47A-6.4, which would subject broker-dealers to a fiduciary standard, and whether the Rule can withstand preemption challenges. This evaluation will require an overview of how the current standards of care and loyalty for financial services professionals came to be, the reasons for and against a uniform fiduciary standard, and potential ramifications of New Jersey's proposed rule. In summary, this paper will argue for the necessity of New Jersey to implement their proposed rule because imposing a fiduciary duty standard for broker-dealers protects investors against the abuses that can result when financial professionals place their own interests above those of their customers, will help to reduce investor confusion, and will work to foster public confidence in the financial profession.

This paper will begin with a background discussion in Part II that provides the legislative history of regulatory standards of care and loyalty for broker-dealers. Part III will cover the legal and factual bases for and against applying a fiduciary standard to all financial services professionals. Part IV will examine New Jersey's proposed rule, including the scope of the duty, types of recommendations that would trigger the duty, and to whom the duty is owed. Part IV will then review recent fiduciary actions taken by other states and predict the outcomes of the [\*306] inevitable challenges to states' fiduciary action. Finally, Part V will conclude with the future of and expected outcomes for New Jersey's proposed rule and the possible effects of states having different fiduciary standards for broker-dealers.

## **Part II. The Evolution of Broker-Dealer Standard of Care and Loyalty**

### **A. Overview of Broker-Dealers**

Brokers are individuals or a firm that charge a fee or commission for executing buy and sell orders submitted by an investor. <sup>7</sup>Section 3(4) of the Securities Exchange Act of 1934 ("Exchange Act") defines "broker" broadly as: "any person engaged in the business of effecting transactions in securities for the account of others." <sup>8</sup>The term "person" includes entities as well as individuals. <sup>9</sup>Thus, a "broker" also refers to the role of a firm when it acts as an agent for a customer and charges the customer a commission for its services.

Dealers are people or firms who buy and sell securities for their own account, whether through a broker or otherwise. <sup>10</sup>Unlike a broker, who acts as an agent, a dealer acts as a principal in trading for its own account. Section 3(a)(5) of the Exchange Act generally defines a "dealer" as "any person engaged in the business of buying and selling securities for his own account, through a broker or otherwise." <sup>11</sup>Although brokers and dealers

<sup>5</sup> See Michelle Singletary, *One Set of Standards for Financial Advisers, Brokers Makes Sense*, WASH. POST, Jan. 27, 2011, at A13 ("An investment adviser has a fiduciary duty to serve the best interest of clients... Brokers don't have to act in a client's best interest. Instead, the law says they have to make sure their recommendations are suitable for the client."); See *infra* § II.

<sup>6</sup> See *infra* § IV.

<sup>7</sup> Tim Smith, *Broker*, INVESTOPEDIA (Feb. 6, 2019), <https://www.investopedia.com/terms/b/broker.asp>.

<sup>8</sup> Securities Exchange Act of 1934 ([15 U.S.C. § 78c\(a\)\(4\)\(A\)](#)) (2018).

<sup>9</sup> Securities Exchange Act of 1934 ([15 U.S.C. § 78c\(a\)\(9\)](#)).

<sup>10</sup> Will Kenton, *Dealer*, INVESTOPEDIA (May 6, 2019), <https://www.investopedia.com/terms/d/dealer.asp>.

<sup>11</sup> Securities Exchange Act of 1934 ([48 Stat. 881](#), [15 U.S.C. § 78c\(a\)\(5\)\(A\)](#))

function in a similar capacity, they do provide distinct services. In contrast to dealers, a broker does not trade its own portfolio but instead facilitates transactions between buyers and sellers.<sup>12</sup> However, in practice, most dealers also act as brokers and are known as broker-dealers.

[\*307] In general, broker-dealers that operate in the United States are regulated by the selfregulatory organization Financial Industry Regulatory Authority ("FINRA"), the Securities and Exchange Commission ("SEC"), and the states.<sup>13</sup> Under the antifraud provisions of the Federal securities laws and FINRA rules, broker-dealers are required to deal fairly with their customers.<sup>14</sup> Furthermore, broker-dealers are subject to statutory, SEC, and FINRA requirements that are designed to promote business practices that protect customers from abusive practices, including practices that may be unethical but may not necessarily be fraudulent.<sup>15</sup>

Currently, broker-dealers, almost all of whom are members of FINRA, are governed by FINRA's suitability standards requiring brokers to have a reasonable basis to believe a recommended investment is suitable for the client.<sup>16</sup> The "reasonable basis" is based on information obtained by the reasonable diligence of the broker-dealer or agent to ascertain the customer's investment profile.<sup>17</sup> FINRA Rule 2111 provides that the customer's "investment profile" includes, but is not limited to, the customer's age, other investments, financial situation [\*308] and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, and risk tolerance.<sup>18</sup>

A person is an investment adviser if that person: (i) provides advice, or issues reports or analyses, regarding securities; (ii) is in the business of providing such services; and (iii) receives compensation for such services.

<sup>19</sup>The Investment Advisers Act of 1940 ("Advisers Act") is the primary vehicle for the federal regulation of investment advisers.<sup>20</sup> Under the Advisers Act, investment advisers are fiduciaries of their clients.<sup>21</sup> An

investment adviser is duty-bound to serve the best interests of its clients, including an obligation to act solely in the client's best interests and thus subordinate its own interests to those of its clients.<sup>22</sup> This duty of loyalty requires an investment adviser that has a material conflict of interest to either eliminate that conflict or fully disclose

<sup>12</sup> See Investment Advisers Act of 1940 § 202(a)(11)(C), [15 U.S.C. § 80b-3\(a\)\(11\)\(C\)](#) (2006).

<sup>13</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, **Pub. L. No. 111-203**, § 913 (2010).

<sup>14</sup> See Securities Exchange Act of 1934 § 10(b), [15 U.S.C. § 78j\(b\)](#) (2000); FINRA Rule 2111.

<sup>15</sup> See Investment Advisers Act § 206(4), [15 U.S.C. § 80b-6\(4\)](#) (2006) (stating that it shall be unlawful for any adviser "to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative").

<sup>16</sup> See NASD Rule 2310(a) (1996), [http://finra.complinet.com/en/display/display\\_main.html?rbid=2403&element\\_id=3638](http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=3638) ("In recommending to a customer the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs."); See Also FINRA Regulatory Notice 09-25 (May 2009), [http://finra.complinet.com/en/display/display.html?rbid=2403&record\\_id=11485&element\\_id=8374&highlight=09-25#r11485](http://finra.complinet.com/en/display/display.html?rbid=2403&record_id=11485&element_id=8374&highlight=09-25#r11485) (proposing to consolidate and replace NASD Rule 2310 with FINRA Consolidated Rule 2010).

<sup>17</sup> See e.g. NYSE Rule 405(1) (2008) (NYSE members must "[u]se due diligence to learn the essential facts relative to every customer, every order, every cash or margin account accepted or carried by such organization and every person holding power of attorney over any account accepted or carried by such organization.").

<sup>18</sup> FINRA, RULE 2111 (2012).

<sup>19</sup> See 913 STUDY, *supra* note 3, at 15.

<sup>20</sup> *Id.*

<sup>21</sup> See Investment Advisers Act of 1940 § 202(a)(11)(C), [15 U.S.C. § 80b-6](#) (2006).

to the investor all material facts relating to the conflict and obtain his or her written consent. <sup>23</sup>The duty of care ascribed to an investment adviser requires it to "make a reasonable investigation to determine that it is not basing its recommendations on materially inaccurate or incomplete information." <sup>24</sup>Thus, in practice, the Advisers Act establishes a statutory fiduciary duty for investment advisers to act for the benefit of their clients, requiring advisers to exercise the utmost good faith in dealing with clients, to disclose all material facts, and to employ reasonable care to avoid misleading clients.

[\*309] Although broker-dealers also give advice, like investment advisors, they are shielded from adviser regulation by virtue of an exclusion in the Advisers Act: <sup>25</sup>As long as a broker's advice is "solely incidental" to brokerage services and they do not receive any "special compensation" for rendering such advice, the broker is excluded from the Advisers Act regulation. <sup>26</sup>Thus, while investment advisers have continuing obligations pertaining to being a fiduciary, broker-dealers are able to insulate themselves from liability by pointing to the suitability of the singular trade at that given point in time. <sup>27</sup>

"Special compensation" refers to investment advisers' business practice of charging a general fee, rather than broker-dealers' practice of charging transaction-specific fees. <sup>28</sup>The proscription on special compensation has traditionally meant that broker-dealers receive compensation from their brokerage clients in the form of commissions on specific trades. In essence, then, investment advisers' business practice of charging a general fee, rather than broker-dealers' practice of charging transaction-specific fees, has evolved into their primary distinction. Thus, the mechanism by which broker-dealers and investment advisers charge clients for services has become a significant issue from a regulatory perspective. However, broker-dealers can charge a management fee and avoid being deemed an investment adviser by giving solely incidental investment advice. <sup>29</sup>Consequently, broker-dealers have begun to drift subtly into a domain of activities that have historically been the province of investment advisers. <sup>30</sup>Even [\*310] the SEC has recognized that the two groups are erasing the outward differences between them, <sup>31</sup>while investors today see little difference between a broker-dealer and an adviser. <sup>32</sup>

<sup>22</sup> 913 STUDY, *supra* note 3, at 22.

<sup>23</sup> For example, an investment adviser is restricted from selling its own inventory to an investor, to prevent conflicts of interest. In contrast, when a broker-dealer recommends a security, the firm, acting as a dealer, is permitted to sell the security to an investor from the firm's own account. *Id.* at 22, 26; See Investment Advisers Act of 1940 at § 80b-6(3).

<sup>24</sup> *Id.* at 22.

<sup>25</sup> See Investment Advisers Act of 1940 at § 80b-3(a)(11)(C).

<sup>26</sup> See *Id.*

<sup>27</sup> See *Id.*

<sup>28</sup> See FINRA, RULE 2111 (2012).

<sup>29</sup> See generally Angela A. Hung ET AL., LRN-RAND Center For Corporate Ethics, Law, and Governance, Investor and Industry Perspectives on Investment Advisers and Broker-Dealers (2008).

<sup>30</sup> See James Hamilton, SEC Reg. Of Investment Advisors And Brokers In The Brave New World 7 (2008), <http://business.cch.com/securitieslaw/news/03-26-08a.pdf> ("Some investment advisers, for example, may offer services that employ computerized trading programs and may take an active, discretionary management role over customer accounts. From the retail investor's prospective [sic], these activities may not be obviously distinct from those in which brokers typically engage.").

<sup>31</sup> See *Enhancing Investor Protection and Regulation of Securities Markets, Hearings Before the Senate Comm. on Banking, Housing, and Urban Affairs*, 111th Cong. 1 (2009), <http://www.sec.gov/news/testimony/2009-ts032609mls.htm> (statement of Mary L. Schapiro, Chairman, U.S. Sec. & Exch. Comm'n) (stating that services provided by broker-dealers and advisers are "virtually identical from the investor's perspective").

The differences between broker-dealers and advisers functions are negligible, however the difference between being regulated as an investment adviser or as a broker-dealer is important because the two are held to different legal standards in connection with the investment advice given.<sup>32</sup> A fiduciary standard is a much higher level of accountability than the suitability standard required of broker-dealers.<sup>33</sup> The suitability standard is met as long as an investment recommendation meets an investor's defined needs and objectives.<sup>34</sup> Importantly, this standard does not require the advice to be in the client's best interest.<sup>35</sup> In contrast, to satisfy fiduciary standards, an investment adviser must satisfy "an affirmative duty of utmost good faith, and full and fair disclosure of all material facts, as well as an affirmative obligation to employ reasonable care to avoid misleading his clients," or it will be subject to civil liability.<sup>36</sup>

## B. The Fiduciary Rule

[\*311] The United States witnessed one of its largest declines in investor wealth during the 2008 Financial Crisis when 401(k)s and IRAs lost close to \$ 2.4 trillion in value.<sup>37</sup> Recognizing a need to address flaws within the financial markets,<sup>38</sup> Congress directed the SEC to perform a study ("913 Study"), in accordance with Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"),<sup>39</sup> on the different standards investment advisers and broker-dealers owe their respective clients,<sup>40</sup> to determine the extent of investor confusion.<sup>41</sup> The 913 Study's findings contained two principal recommendations. First, the SEC recommended consideration of a uniform fiduciary standard for both investment advisers and broker-dealers when providing investment advice to retail customers.<sup>42</sup> The second recommendation was that all investors should be given the same protections regardless of which type of investment professional provides them with advice.<sup>43</sup> Based on its findings, the SEC staff recommended that the it establish a uniform fiduciary duty standard for investment advisers and broker-dealers when providing investment advice about securities to retail customers that is consistent with the standard that currently applies to investment advisers.<sup>44</sup> The 913 Study found that a uniform fiduciary standard would protect investors by ensuring they can readily access unbiased advice

<sup>32</sup> See Certain Broker-Dealers Deemed Not to be Investment Advisers, Exchange Act Release No. 42,099, [Advisers Act Release No. 1845, 64 Fed. Reg. 61,226, 61,229](#) (proposed Nov. 4, 1999) (explaining that marketing by broker-dealers as advisers raises questions regarding how investors perceive broker-dealers' role).

<sup>33</sup> See Investment Adviser Oversight Act of 2012, H.R. 4624, 112th Cong. (2012).

<sup>34</sup> See *Id.*

<sup>35</sup> See FINRA, RULE 2111 (2012).

<sup>36</sup> 913 STUDY, *supra* note 3, at 139-140.

<sup>37</sup> See e.g. [SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 194 \(1963\)](#).

<sup>38</sup> Teresa Ghilarducci, *The Recession Hurt Americans' Retirement Accounts More Than Anybody Knew*, ATLANTIC, (Oct. 16, 2015), <https://www.theatlantic.com/business/archive/2015/10/the-recession-hurt-americans-retirement-accounts-more-than-everyone-thought/410791/> [<https://perma.cc/L287-A2YK>].

<sup>39</sup> SEC Oversight: Current State and Agenda, Hearing Before the Subcomm. on Capital Markets, Insurance and Government-Sponsored Enterprises of the House Comm. on Financial Services, 111th Cong. 62 (2009); See Ira D. Hammerman, Lecture, *SEC-Don't Throw Away Your Shot! A Renewed Call for a Uniform Fiduciary Standard to Protect Individual Investors*, [22 Fordham J. Corp. & Fin. L. 319-20 \(2017\)](#).

<sup>40</sup> Dodd-Frank not only required the performance of a study but also gave the SEC explicit rulemaking authority in connection with that study. See Dodd-Frank Wall Street Reform and Consumer Protection Act, **Pub. L. No. 111-203**, § 913(f), **124 Stat. 1376**, 1827-28 (2010) (codified at [15 U.S.C. § 78o](#) (2012)).

<sup>41</sup> See *Id.*

[\*312] from all financial professionals, regardless of whether that advice comes from an investment adviser or broker-dealer. <sup>46</sup>

On February 23, 2015, President Obama called for the Department of Labor ("DOL") to update the standard of care and the standard of loyalty for all financial professionals, <sup>47</sup> which the DOL proposed on April 14, 2016 <sup>48</sup> and finalized on April 6, 2016. <sup>49</sup> The new standards of care and loyalty, known as the "Fiduciary Rule," expanded the "investment advice fiduciary" definition under the Employee Retirement Income Security Act of 1974 ("ERISA") <sup>50</sup>, thereby enabling the SEC to impose the same fiduciary standard of conduct that applies to investment advisers to broker-dealers. <sup>51</sup> The Fiduciary Rule automatically elevated all financial professionals, including broker-dealers, who work with retirement plans or personalized investment advice to the level of a fiduciary, bound legally and ethically to meet the standards of that status. <sup>52</sup>

[\*313] If the DOL's expanded definition of fiduciary came into effect, it would have eliminated many commission structures that govern the industry, including being compensated on a per transaction basis. <sup>53</sup> Transaction-based compensation inherently generates conflict of interests because broker-dealers are able to be paid more by recommending and selling particular securities over ones they receive less compensation for. <sup>54</sup> Broker-dealers who wished to continue offering services or products on commission would have needed to provide clients with a disclosure agreement, called a Best Interest Contract Exemption, in circumstances where a conflict of interest could exist, such as the broker-dealer receiving a higher commission or special bonus for selling a certain product. <sup>55</sup> The disclosure agreement was required to explicitly state all compensation that was to be received by the fiduciary. <sup>56</sup>

Supporters applauded the new rule, saying it should increase and streamline transparency for investors, make conversations easier for broker-dealers, and, most of all, prevent abuses, such as excessive commissions. <sup>57</sup> However, the regulation met with staunch opposition from other financial professionals, including broker-dealers and planners. <sup>58</sup> By the DOL's estimate, stricter [\*314] fiduciary standards could have cost the financial services industry an estimated \$ 2.4 billion per year by eliminating conflicts of interest like front-end load

<sup>42</sup> See 913 STUDY, *supra* note 3.

<sup>43</sup> See *Id. at 129*.

<sup>44</sup> See *Id.*

<sup>45</sup> *Id.* at v-vi.

<sup>46</sup> See Senate Committee On Banking, Housing & Urban Affairs, 111th Cong., Restoring American Financial Stability Act: Chairman's Mark Text (2009), available at <https://www.congress.gov/bill/111thcongress/senate-bill/3217/text>.

<sup>47</sup> DOL, Department of Labor Proposes Rule to Address Conflicts of Interest in Retirement Advice, Saving Middle-Class Families Billions Every Year (2015), [https://www.calstrs.com/sites/main/files/fileattachments/factsheet\\_coi\\_4-14-15.pdf](https://www.calstrs.com/sites/main/files/fileattachments/factsheet_coi_4-14-15.pdf).

<sup>48</sup> DOL, EBSA News Release: US Labor Department seeks public comment on proposal to protect consumers from conflicts of interest in retirement advice (04/14/2015) available at: <https://www.dol.gov/newsroom/releases/ebsa/ebsa20150655>.

<sup>49</sup> Clay Akin, What is the Status of the DOL Fiduciary Rule? (June 14, 2018), <https://www.guidevine.com/roundtable/what-is-the-status-of-the-dol-fiduciary-rule>.

<sup>50</sup> Enacted in 1974, ERISA had never been revised to reflect changes in retirement savings trends, particularly the shift from defined benefit plans to defined contribution plans, and the huge growth in IRAs. There's little doubt that the 40-year-old ERISA rules were overdue for a change, and many industry groups had already jumped on board with the new plan, including the Certified Financial Planner Board of Standards, the Financial Planning Association, and the National Association of Personal Financial Advisors. See Letter from the Consumer Fed'n of Am. et al. to Mary L. Schapiro, Chairman, Sec. & Exch. Comm'n 1 (Mar. 28, 2012), <http://www.consumerfed.org/pdfs/SIFMA-FrameworkResponse3-29-12.pdf>.

commissions. <sup>59</sup>At the behest of the Secretary of Labor, the SEC issued a statement asking for public comments. <sup>60</sup>The SEC's goal was to "engage constructively" as both the DOL and SEC "pursue [their] ongoing analyses of the standards of conduct applicable to investment advisers and broker-dealers when they provide investment advice to retail investors." <sup>61</sup>

### C. Regulation Best Interest

The Fiduciary Rule was put on hold in February 2017, when President Trump issued a memorandum that delayed the Fiduciary Rule's implementation by 180 days, which was later delayed by another 60 days by the DOL. <sup>62</sup>The Fiduciary Rule never was implemented because the Fifth Circuit Court of Appeals vacated it in a 2-to-1 decision, finding it constituted "unreasonableness," <sup>63</sup>and that the DOL's implementation of the rule constitutes "an arbitrary and capricious exercise of administrative power." <sup>64</sup>The case was brought by the U.S. Chamber of Commerce, the Financial Services Institute, and other parties. <sup>65</sup>The basis of the suit was that the <sup>[\*315]</sup>DOL overstepped its congressional mandate in the Dodd-Frank Act. <sup>66</sup>In place of the Fiduciary Rule, in June 2019, the SEC promulgated a rule, known as Regulation Best Interest ("Reg BI"). <sup>67</sup>Reg BI removed the restrictive language found in the Fiduciary Rule while expanding the scope of who and what type of recommendations should be covered under the best interest standard. <sup>68</sup>

Reg BI is designed to hold any individual or financial institution that provides investment advice to retail consumers -- regardless of account type -- to a heightened standard of three obligations: 1) disclosure, 2) care, and 3) conflict of interest. <sup>69</sup>The first obligation under Reg BI is one of disclosure, which provides that when an investment professional makes a recommendation, they are required to "disclose to the retail customer, in writing, the material facts relating to the scope and terms of the relationship with the retail customer and all material conflicts of interest associated with the recommendation." <sup>70</sup>The second obligation proposed <sup>[\*316]</sup>under Reg BI is the care obligation. <sup>71</sup>Within this obligation resides an expectation that financial professionals will "exercise reasonable diligence, care, skill, and prudence" when making investment recommendations. <sup>72</sup>The final

<sup>51</sup> Definition of the Term "Fiduciary"; Conflict of Interest Rule--Retirement Investment Advice, [81 Fed. Reg. 20,946, 20,950](#) (Apr. 8, 2016) (to be codified at 29 C.F.R. pts. 2509, [2510](#), [2550](#)).

<sup>52</sup> See *Id* at 20,946. See Employee Retirement Income Security Act of 1974, [Pub. L. No. 93-406](#), [88 Stat. 829](#) (1974) (current version codified in scattered sections of 29 U.S.C.).

<sup>53</sup> See generally [Nat'l Ass'n for Fixed Annuities, 217 F. Supp. 3d at 19](#) (highlighting the sale of a commission based product could subject that product to the restrictions of Best Interest Contract Exemption).

<sup>54</sup> See Ian S. Kopelman, DOL Issues Final Fiduciary Rule and Related Exemptions, DLA Piper (Apr. 18, 2016), <https://www.dlapiper.com/en/us/insights/publications/2016/04/dol-issues-final-fiduciary-rule/> (noting that the fiduciary rule prohibits a financial institution's use of "quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation or other actions or incentives that are intended or would reasonably be expected to cause advisers to make recommendations that are not in the best interest of a Retirement Investor").

<sup>55</sup> Best Interest Contract Exemption, [81 Fed. Reg. 21,002, 21,007](#) (Apr. 8, 2016) (to be codified at [29 C.F.R. pt. 2550](#)).

<sup>56</sup> *Id.*

<sup>57</sup> Mark Schoeff Jr., Obama directs Labor Department to move ahead on fiduciary rule, INVESTMENTNEWS (Feb. 23, 2015), <https://www.investmentnews.com/article/20150223/FREE/150229979/obama-directs-labor-departmentto-move-ahead-on-fiduciary-rule>.

<sup>58</sup> See InvestmentNews, BlackRock and Vanguard urge delay in Department of Labor's fiduciary rule ( Mar. 27, 2017), <https://www.investmentnews.com/article/20170327/FREE/170329932/blackrock-andvanguard-urge-delay-in-department-of-labors-fiduciary>.

obligation under Reg BI is the conflict of interest obligation.<sup>73</sup> There are two requirements to the obligation that apply directly to financial institutions.<sup>74</sup> First, the company must maintain written policies and procedures disclosing material conflicts of interest as they relate to the recommendations being made to customers.<sup>75</sup> Second, financial companies must disclose any financial incentives resulting from the sale of a recommendation.<sup>76</sup>

Supported by the financial industry, the rule relies largely on disclosures to investors and will preserve broker-dealers' commission-based sales model.<sup>77</sup> The SEC says Reg BI will give investors more information about broker-dealers' complex pay incentives.<sup>78</sup> The agency did not impose the higher fiduciary duty that applies to investment advisers, whose requirements were spelled out through a separate regulatory notice, on broker-dealers.<sup>79</sup> While broker-dealers will have to meet a higher bar than the current suitability standard, the rule does not spell out specific conflicts that would violate the best-interest standard.<sup>80</sup> Consequently, broker-dealers will need [\*317] to write policies to reduce conflicts of interest, such as supersize commissions for hitting higher sales targets.

Following the release of the proposed rulemaking, several states and state securities regulators -- including those in Connecticut, Illinois, Maryland, Massachusetts, Nevada, New Jersey and New York -- signaled a willingness to implement their own broker-dealer conduct rules that will be more rigorous than the standard set out in Reg BI.<sup>81</sup> Unlike the state proposals, discussed below, the Reg BI does not outlaw sales contests and other practices that reward broker-dealers for steering customers. In particular, Reg BI falls short because it does not explicitly create a private cause of action for investors if they feel their broker-dealer falls short of federal standards,<sup>82</sup> which was a primary concern of the financial services industry.<sup>83</sup> The final rule benefited brokerage firms by scaling back some proposed requirements, such as the need to reduce all financial conflicts of interest.<sup>84</sup> The SEC said it agreed that a uniform fiduciary standard could have caused firms to offer fewer products or complicate their pay practices.<sup>85</sup> Instead, under Reg BI, broker-dealers will need to mitigate a narrower set of conflicts, including [\*318] the harmful effects of offering a limited range of products.<sup>86</sup> Firms will have to comply with Reg BI by June 30, 2020.<sup>87</sup>

<sup>59</sup> DOL, Regulating Advice Markets: Regulatory Impact Analysis For Final Rule and Exemption, (Apr. 2016) at 220, <https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-andregulations/completed-rulemaking/1210-AB32-2/ria.pdf>.

<sup>60</sup> Alexander Acosta, *Deregulators Must Follow the Law, So Regulators Will Too*, WALL ST. J., May 23, 2017, at A19.

<sup>61</sup> Jay Clayton, Chairman, SEC, Public Statement: Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers (June 1, 2017), <https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31>.

<sup>62</sup> Memorandum from Donald J. Trump, President, U.S., to Edward Hugler, Acting Sec'y of Labor, U.S. Dep't of Labor (Feb. 3, 2017), available at: <https://www.whitehouse.gov/presidential-actions/presidentialmemorandum-fiduciary-duty-rule>; U.S. DEP'T OF LABOR, Field Assistance Bull. No. 2017-01, Temporary Enforcement Policy On Fiduciary Duty Rule (2017).

<sup>63</sup> *Chamber of Commerce v. U.S. Dep't of Labor*, 885 F.3d 360, 388 (5th Cir. 2018) (holding that the SEC did not have the authority to rewrite the terms of the statutory exclusion in the Advisers Act because the text of the exception was unambiguous).

<sup>64</sup> *Id. at 385* (observing the Fiduciary Rule was the result of the "DOL's decision to outflank two Congressional initiatives to secure further oversight of broker/dealers handling IRA investments and the sale of fixed-indexed annuities.").

<sup>65</sup> *Id.*

<sup>66</sup> See *Id. at 385-386* ("Rather than infringing on SEC turf, DOL ought to have deferred to Congress's very specific Dodd-Frank delegations and conferred with and supported SEC practices to assist IRA and all other individual investors.").

### **Part III. Arguments For and Against Applying a Uniform Fiduciary Standard to All Financial Services Professionals**

#### **A. Legal and Factual Bases for Applying a Fiduciary Standard to Broker-Dealers**

While there may be a variety of products that are technically "suitable" for the investor based on the client's risk profile, Reg BI does not require the broker-dealers to disclose that there may be lower-cost options available or that the broker-dealer's recommendation may be driven by potential incentives creating a conflict of interest.<sup>88</sup>A press release from Americans for Financial Reform states, "Every day that conflicted advice continues costs them [Americans] \$ 46 million a day, \$ 1.9 million per hour, and \$ 532 a second."<sup>89</sup>According to a 2015 analysis by the United States Council of Economic Advisers, conflicted advice costs Americans about \$ 17 billion in foregone retirement earnings each year.<sup>90</sup>The DOL estimated that underperformance due to conflicted investment advice could cause individual retirement account investors in the mutual funds segment alone to lose up to \$ 189 billion over the next ten years and \$ 404 billion [\*319] over the next twenty.<sup>91</sup>Thus, having uniform fiduciary standards will likely have a positive economic impact on investors.

The current prevalence of conflicted payments is interfering with low balance investors' ability to get quality advice.<sup>92</sup>While the cost of advice has been reducing over the years, it may be difficult for new broker-dealers providing quality, unconflicted, low-cost advice to compete on price when other advice erroneously appears to be free.<sup>93</sup>Conflicts are only magnified when a firm favors proprietary products or products for which the firm receives revenue sharing payments to the detriment of customer interests.<sup>94</sup>The prevalence of hidden fees and conflicted payments may make it more difficult for low-cost, high-quality alternatives to compete on a level playing field, reducing moderate-income Americans' available options for inexpensive advice.<sup>95</sup>As a result of the competitive nature of the industry, to retain business, firms may lower the costs to clients. Investors may also save money in terms of investment choices since, under a fiduciary duty, broker-dealers will now have to offer lower-cost, similar investment options, which will potentially generate savings for investors.

<sup>67</sup> Although the name "Regulation Best Interest" suggests that the proposal would effectuate a fiduciary standard of care, which would require broker-dealers to act in their customers' best interest, multiple Commissioners say the new proposals merely tweak the existing suitability standard. Ed Beeson, SEC Unveils Plans for "Best Interest" Standard for Brokers, LAW360 (Apr. 18, 2018, 9:40 PM), <https://www.law360.com/articles/1034840/sec-unveils-plans-for-best-interest-standard-for-brokers>.

<sup>68</sup> See PwC Fin. Servs. Reg. Prac., *Five Key Points from the SEC's "Best Interest" Rule Proposal*, PwC: First Take (Apr. 26, 2018), <https://www.pwc.com/us/en/financial-services/regulatorservices/publications/assets/pwc-sec-best-interest-rule-proposal.pdf> (explaining Reg BI will cover all investment recommendations made to retail customers but will not yield on restrictions as to how investment professionals are compensated).

<sup>69</sup> Regulation Best Interest, [83 Fed. Reg. 21,574](#) (proposed May 9, 2018) (to be codified at [17 C.F.R. pt. 240](#)) [hereinafter Reg BI] (providing that all broker-dealers and natural persons who are associated persons of a broker-dealer (unless otherwise indicated, together referred to as "broker-dealer"), when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer, act in the best interest of the retail customer at the time the recommendation is made without placing the financial or other interest of the broker-dealer or natural person who is an associated person making the recommendation ahead of the interest of the retail customer.).

<sup>70</sup> While the SEC does not explicitly call the writing a contract, if it is incorporated as part of an investment advisory agreement or is a condition of engaging a customer in a financial relationship, it does leave to question whether it could be considered an enforceable agreement between two parties. Furthermore, the silence within Reg BI on this issue leads to the possibility that a breach of the writing could be contested in a court of law. *Id.* at 21,599.

<sup>71</sup> *Id.* at 21,608.

<sup>72</sup> *Id.* at 21,608.

Perhaps the most common justification in support of a uniform standard is that investors are simply confused as to the difference in roles between investment advisers and broker-dealers.<sup>73</sup>

In support of this justification is the 913 Study, which found that investors do not [\*320] understand the differences between investment advisers and broker-dealers or the standards of care applicable to them.<sup>74</sup>

The average investor finds the different standards of care and loyalty confusing and is uncertain about the meaning of the various titles and designations used by investment advisers and broker-dealers, such as "money-manager," "wealth-manager," "financial advisor," etc.<sup>75</sup>

The 913 Study found that a majority of investors surveyed incorrectly believed that stockbrokers and "financial advisors" are held to a fiduciary duty, 66% and 76% of investors surveyed, respectively.<sup>76</sup>

The 913 study also asked whether participants agreed with the statement that "when you receive investment advice from a financial professional, the person providing the advice should put your interests ahead of theirs and should have to tell you upfront about any fees or commissions they earn and any conflicts of interest that potentially could influence that advice," finding that 85% of participants strongly agreed, 12% somewhat agreed, and 1% somewhat disagreed or strongly disagreed.<sup>77</sup>

Thus, it can be inferred that an overwhelming majority of the public would welcome a uniform fiduciary standard.

There may be an initial increased cost to broker-dealers as they modify policies and procedures or provide training to their employees.<sup>78</sup>

There may also be additional costs associated with hiring attorneys to ensure compliance with the rule.<sup>79</sup>

However, a 2012 study conducted by academics Michael Finke and Thomas P. Langdon in the Journal of Financial Planning took advantage of variations in state common law fiduciary advice standards to gauge [\*321] whether stricter standards within states resulted in fewer registered representatives doing business in those states, and whether reps there felt constrained in their ability to offer services to lower-wealth clients.<sup>80</sup>

In both cases, the researchers found no statistical differences among states, no matter the advice standard.<sup>81</sup>

Based on the 913 Study, I think, even if there are increased costs to broker-dealers, the

<sup>73</sup> The conflict of interest obligation does appear to be the most flexible of the three as it permits financial institutions to make their own decision on which conflicts of interest to disclose. In addition, the SEC is encouraging broker-dealers to develop compliance systems that fit within their own business model. See *id.* at 21,617-2618.

<sup>74</sup> *Id.* at 21,617.

<sup>75</sup> See *id.* (describing what is necessary to have a fully compliant company policy on conflicts of interest).

<sup>76</sup> See *id.* ("Establish, maintain, and enforce written policies and procedures reasonably designed to identify, and disclose and mitigate, or eliminate, material conflicts of interest arising from financial incentives associated with such recommendations.").

<sup>77</sup> *Id.*

<sup>78</sup> See *id.*

<sup>79</sup> See Commission Interpretation Regarding Standard of Conduct for Investment Advisors, 84 C.F.R. 276 (2019).

<sup>80</sup> See generally Reg BI, *supra* note 69.

<sup>81</sup> See *Fiduciary Governance: A Fiduciary's 2018 Retrospective (and Predictions for 2019)*, Stradley Ronon: Risk&Reward 2 (Jan. 7, 2019), [https://www.stradley.com/-/media/files/publications/2019/01/risk\\_and\\_reward\\_jan7\\_2019.pdf](https://www.stradley.com/-/media/files/publications/2019/01/risk_and_reward_jan7_2019.pdf).

public's interest in protecting the welfare of investors and instilling greater confidence in the industry outweighs the potential negative economic impact to broker-dealers.

## B. Potential Negative Consequences of the Proposed Fiduciary Rule

Opponents of the idea of a uniform fiduciary standard find the underlying reasoning flawed because investment advisors and brokers provide distinct services -- financial advice, and sale and distribution of securities, respectively. Thus, they do not find it fair to subject different professions to the same standard of care and loyalty when they perform different tasks and are compensated differently. Moreover, opponents argue that advocates have exclusively focused on broker-dealers' standard of care and loyalty while ignoring numerous investorprotection obligations imposed on broker-dealers but not on advisors.<sup>105</sup> Critics of holding broker-dealers to a fiduciary standard also point out that they may "already be subject to significant fiduciary-like obligations when acting as more than mere order takers for their [\*322] customers."<sup>106</sup> Indeed, the infrequency with which advisers currently are examined and disciplined is cause for concern.<sup>107</sup>

The Fiduciary Rule was expected to increase compliance costs for broker-dealers.<sup>108</sup> The Fiduciary Rule would have been particularly harsh on smaller, independent broker-dealers who might not have had the financial resources to invest in the technology and the compliance expertise to meet the requirements. Thus, it is possible that some of these smaller firms would have had to disband or be acquired.<sup>109</sup> Even the substantially-sized brokerage operations of MetLife Inc. and American International Group were sold off in anticipation of these rules and its related costs.<sup>110</sup> The negative consequences of the Fiduciary Rule were further substantiated by a Deloitte & Touche study that found that, in response to the rule, 53 percent of the 21 firms surveyed had adopted plans to discontinue offering certain commission-based retirement [\*323] planning services.<sup>111</sup> Moreover, it found that "start-up" compliance costs for the Fiduciary Rule alone cost broker-dealers approximately \$ 4.7 billion in 2016, and estimated that ongoing costs to comply with the rule will be around \$ 700 million dollars annually -- assuming then, of course, that the rule would not be vacated.<sup>112</sup>

<sup>82</sup> Consumers might be able to bring causes of action such as breach of fiduciary duty, breach of contract, and other state-based deceptive trade practices claims against Reg BI in state courts without fear of removal over a federal jurisdictional question. See [Merrill Lynch, Pierce, Fenner & Smith Inc. v. Manning, 136 S. Ct. 1562 \(2016\)](#).

<sup>83</sup> See Paul Foley & John Sanders, *Fiduciary Rule Creates Breach of Contract Claim, But No Private Right of Action*, Lexology (June 12, 2017), <https://www.lexology.com/library/detail.aspx?g=9d4dcada-155d-43c6-8020-0e74dcd5572c>.

<sup>84</sup> See Reg BI, *supra* note 69, at 21,574, 21,617.

<sup>85</sup> See Reg BI, *supra* note 69, at 21,576.

<sup>86</sup> For example, Reg BI provides that broker-dealers are to "establish[], maintain[], and enforce[] written policies and procedures reasonably designed to... [i]dentify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time." Thus, a broker-dealer can still offer only proprietary products, place material limitations on the menu of products, and incentivize representatives to sell such products through its compensation practices, so long as the incentive is not based on the sale of specific securities or types of securities within a limited period of time. See Reg BI, *supra* note 69, at 21,641.

<sup>87</sup> See *Id.* at 21,574.

<sup>88</sup> See generally Polina Demina, Note, *Broker-Dealers and Investment Advisers: A Behavioral-Economics Analysis of Competing Suggestions for Reform*, [113 MICH. L. REV. 429, 459 \(2014\)](#) (relying on a behavioral-economics analysis to argue that the SEC should adopt a uniform fiduciary standard for broker-dealers and investment advisers)

<sup>89</sup> Press Release, Americans for Financial Reform, *AFR Event: Retirement Ripoff Counter Shows Losses of \$ 532 Each Second Without Fully Enforced Fiduciary Law* (Apr. 5, 2017).

Organizations like the Securities Industry and Financial Markets Association ("SIFMA"), Wall Street's trade group, lobbied against the uniform fiduciary standard by arguing that a fiduciary standard for brokers could limit consumer access to financial services products and drive up the costs to deliver services, because they would potentially have to spend more time gathering information from and analyzing each client before making a recommendation.<sup>113</sup> SIFMA estimated in 2017 that the Fiduciary Rule would have cost nearly \$ 5 billion for firms to implement and come with an annual price tag steeper than \$ 1 billion.<sup>114</sup> Undoubtedly implementing a uniform fiduciary rule would require broker-dealers to rework their supervision protocols, hiring practices, paperwork, and training.

#### **Part IV. State Fiduciary Action**

##### **A. New Jersey's Proposed Rule**

In the wake of the demise of the Fiduciary Rule, New Jersey proceeded with a plan to impose its own fiduciary rule on brokerage and advisory professionals. Attorney General Gurbir S. Grewal and the New Jersey Bureau of Securities announced on April 15, 2019, a proposed <sup>[\*324]</sup> new uniform fiduciary standard for investment firms to protect investors.<sup>115</sup> The proposed rule amendment to [N.J.A.C. 13:47A-6.3](#) and proposed rule N.J.A.C. 13:47A-6.4 (collectively, "NJ's Proposed Rule") establish, by regulation, the common law fiduciary duty and applies it to broker-dealers and codifies it for investment advisers.<sup>116</sup> NJ's Proposed Rule is the first formal response from a specific state in the wake of Reg BI.<sup>117</sup>

The proposed rule, N.J.A.C. 13:47A-6.4, would require all investment professionals registered with the Division of Consumer Affairs' Bureau of Securities to place customers' interests above their own when recommending securities or providing investment advice.<sup>118</sup> The scope of the duty is more significant than Reg BI as it would require all registered financial service professionals to act in accordance with a fiduciary duty to their customers when providing investment advice, recommending investment strategy, opening or transferring their assets to any type of account, or making the purchase, sale, or exchange of any security.<sup>119</sup> Conduct falling short of this

<sup>90</sup> Council of Econ. Advisors, Exec. Office of the President, *The Effects of Conflicted Investment Advice on Retirement Savings* 13 (2015).

<sup>91</sup> A 2015 report on the effects of conflicted investment advice on retirement savings, President Obama's Council of Economic Advisors cited a range of studies showing conflicted advice can lead to higher fees, biased advice, inappropriate risk-taking, inappropriate account rollovers, inappropriate diversification, asset misallocation, and market mistiming, and thus lower investment returns. *Id.*

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> [\*Id. at 23.\*](#)

<sup>95</sup> The Council of Economic Advisers reported that investors affected by hidden fees and conflicted payments lose approximately 1% in investment returns annually. *Id.*

<sup>96</sup> See generally Knut Rostad, *Strengthen Disclosures by Limiting Their Role in the Delivery of Investment and Financial Advice*, 30 REV. BANKING & FIN. L. 141, 144-46 (2011) (reviewing studies regarding investor confusion about the difference between investment advisers and broker-dealers); See generally Gary A. Varnavides, Note, *The Flawed State of Broker-Dealer Regulation and the Case for an Authentic Federal Fiduciary Standard for Broker-Dealers*, [16 Fordham J. Corp. & Fin. L. 203, 204 \(2011\)](#) ("[B]roker-dealers and investment advisers offer virtually identical services to investors, resulting in considerable confusion for both investors and regulators.").

<sup>97</sup> See 913 STUDY, *supra* note 3, at 101.

<sup>98</sup> *Id.*

fiduciary duty would, under the proposed rule, constitute a "dishonest and unethical practice."<sup>120</sup> Furthermore, parts of this rule go even farther than the Fiduciary Rule, such as not having an exception to establishing a brokerage or advisory [\*325] relationship for onetime investment advice.<sup>121</sup> While the Rule does not create a private cause of action, for investment professionals doing business in New Jersey or with New Jersey customers, the rule imposes a regulatory standard and may, in practice, set the standard of care expected of investment professionals in other contexts, including defending civil claims.

Proposed new N.J.A.C. 13:47A-6.4(b) provides that, to meet the fiduciary duty, a broker-dealer, agent, or adviser shall satisfy both the duty of care and the duty of loyalty.<sup>122</sup> The proposed duty of care would require broker-dealers and advisers to (1) "use with the care, skill, prudence and diligence of a prudent person in a like capacity" and (2) "make reasonable inquiries into the risks, costs and conflicts of interest related to the recommendation or investment advice; the customer's investment objectives, financial situation and needs; and any other relevant information."<sup>123</sup> Unlike Nevada's proposed fiduciary rule, discussed below, NJ's Proposed Rule is consistent with the longstanding common law rule that broker-dealers do not generally owe an ongoing duty to monitor economic or financial developments that could affect the portfolio of a nondiscretionary customer.<sup>124</sup>

The proposed duty of loyalty requires that any recommendations or advice given by the broker-dealer must be "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."<sup>125</sup> Harmful incentives, such as sales contests that [\*326] encourage and reward conflicted advice, are presumed invalid by the rule. Accordingly, subparagraph (b)(2)(i) establishes a presumption of a breach of the duty of loyalty for "offering or receiving direct or indirect compensation to or from the broker-dealer, its agent, or adviser for recommending the opening of or transfer of assets to a specific type of account, or the purchase, sale, or exchange of a specific security that is not the best of the reasonably available options."<sup>126</sup> A broker-dealer would still be able to

99                  *Id. at 101.*

100                *Id.*

101                Richard J. Kubiak, *Off-Key Regulation: Examining the SEC's and the DOL's Dissonant Regulation of Broker-Dealers*, [68 EMORY L.J. 369, 399 \(2018\)](#).

102                *Id.*

103                Michael Finke & Thomas P. Langdon, *The Impact of the Broker-Dealer Fiduciary Standard on Financial Advice*, FIN. PLANNING ASS'N, <https://www.onefpa.org/journal/Pages/The%20Impact%C20of%C20the%20Broker-Dealer%20Fiduciary%C20Standard%C20on%C20Financial%20Advice.aspx> (last visited Oct. 20, 2018).

104                *Id.*

105                Broker-dealers have other various duties owed to their clients, such as a duty of fair dealing, a duty of best execution, suitability requirements, and various disclosure requirements. Morrison & Foerster LLP, News Bulletin, *A Fiduciary Duty For Broker-Dealers? How Dodd-Frank May Change The Way Broker-Dealers Conduct Business* 1 (2010), <http://www.mfo.com/files/Uploads/Images/100719DoddFrank>; See William A. Nelson, *Broker-Dealer: A Fiduciary By Any Other Name?*, [20 Fordham J. Corp. & Fin. L. 637 \(2015\)](#).

106                For example, when a broker has discretion over an account, the broker owes a fiduciary duty. David Serchuk, *Suitability: Where Brokers Fail*, FORBES, June 24, 2009, <http://www.forbes.com/2009/06/23/suitability-standards-fiduciary-intelligent-investingbrokers.html>

107                *Compliance Program of Investment Companies and Investment Advisers, Investment Company Act Release No. 25925, 68 Fed. Reg. 7038, 7039* (proposed Feb. 11, 2003) ("Our current resources permit us to conduct routine examinations of each of the 966 fund complexes and each adviser only once every five years, and during these examinations we are unable to review

charge a commission so long as the fee was reasonable, was the best of the available fee options, and the duty of care was met.

Opponents of the proposed duty of loyalty take particular issue with the concept of the "best" recommendation or the "best" fee structure.<sup>127</sup> Many say this is not a fiduciary concept, as it suggests that there can only be one correct recommendation for an individual consumer when making a fiduciary recommendation requires the inherently subjective weighing of relevant factors leading to a prudent recommendation from among many similarly prudent options.<sup>128</sup> Some also argue that the "without regard to" language creates a legally untenable position for financial professionals because it requires them to prove a negative.<sup>129</sup>

In subparagraph (b)(2)(ii), the rule specifies that there "shall not be a presumption that disclosing a conflict of interest in and of itself will satisfy the duty of loyalty."<sup>130</sup> In contrast, under Reg BI, some, but not all, duty of loyalty type conflicts can be mitigated through proper disclosure to the investor.<sup>131</sup> Simply disclosing conflicts does not provide adequate protection [\*327] and does not shield investors from potential financial harm of conflicted advice.<sup>132</sup> Disclosure may even have unintended effects, such as making a consumer more confident that a financial professional is meeting a higher standard than he or she is actually meeting.<sup>133</sup>

If adopted, which seems likely, New Jersey could be the first state to establish a fiduciary standard for broker-dealers through rulemaking.<sup>134</sup> With the most brokers of any state that has yet taken action to raise the standard of care and loyalty -- there were nearly 5,000 brokerage offices in 2018 -- New Jersey's action is being closely watched.<sup>135</sup>

## B. Other States' Fiduciary Actions

Although common-law broker-dealer standards of care and loyalty have differed among states for decades,<sup>136</sup> specific fiduciary laws and regulations have been initiated by several states [\*328] in the last few years and

<sup>108</sup> every transaction."); See Mark Schoff Jr. & Bruce Kelly, *Finra: Who's watching the watchdog?*, INVESTMENTNEWS (Sep. 2, 2017), <https://www.investmentnews.com/article/20170902/FEATURE/170909996/finra-whos-watching-the-watchdog>.

<sup>109</sup> Bruce Kelly, *DOL Fiduciary Rule Compliance Costs Exceed \$ 4.7 Billion: SIFMA Study*, INVESTMENTNEWS (Aug. 10, 2017, 2:00 PM), [http://www.investmentnews.com/article/20170810/FREE/170819991/dol-fiduciary-rule-compliance-costs-exceed-4-7-billion-sifmastudy?mod=article\\_inline](http://www.investmentnews.com/article/20170810/FREE/170819991/dol-fiduciary-rule-compliance-costs-exceed-4-7-billion-sifmastudy?mod=article_inline) (finding that a new SIFMA study projected the DOL's fiduciary rule to cost \$ 4.7 billion as opposed to the \$ 2 billion cited by the DOL).

<sup>110</sup> Pinar Çebi Wilber, Am. Council For Capital Formation Ctr. For Policy Research, *DOL'S Retirement Advice Rule: Helping Or Harming Sound Retirement Planning?* 11 (2015) (finding "[t]he prospect of increased record-keeping and paperwork for compliance purposes, as well as the possible increase in litigation volumes, will push up the cost for brokerage services, making them uneconomical, especially for small account sizes.").

<sup>111</sup> Stephanie Colestock, *Trump Nixes the Fiduciary Rule... Is This A Good Idea?*, Consumerism Commentary (July 23, 2019), <https://www.consumerismcommentary.com/trump-set-to-overturnfiduciary-rule/>.

<sup>112</sup> See Deloitte, *The DOL Fiduciary Rule: A Study On How Financial Institutions Have Responded And The Resulting Impacts On Retirement Investors* 3, 6 (2017).

<sup>113</sup> *Id.* at 19.

<sup>114</sup> See Michael Finke & Thomas P. Langdon, *The Impact of the Broker-Dealer Fiduciary Standard on Financial Advice*, FIN. PLANNING ASS'N, <https://www.onefpa.org/journal/Pages/The%20Impact%C20of%C20the%20Broker-Dealer%C20Fiduciary%C20Standard%C20on%C20Financial%C20Advice.aspx> (last visited Oct. 20, 2018).

<sup>115</sup> Letter from Ira D. Hammerman, Senior Managing Dir. & Gen. Counsel, SIFMA, to Mary L. Schapiro, Chairman, Sec. & Exch. Comm'n 1-2 (July 14, 2011), available at: <http://www.sec.gov/comments/4-606/4606-2952.pdf>.

remain in varying degrees of progress. New Jersey is one of several states seeking to set their own investment advice standards.

For instance, Nevada sent broker-dealers reeling with a set of proposed regulations to protect retirees from biased advice and supplant Reg BI.<sup>137</sup> Draft regulations released 3 months before New Jersey's Rule Proposal, in January 2019, would have subjected broker-dealers to the fiduciary standard under a definition of qualifying "investment advice" that includes passing along securities analyses or reports, providing limited securities options, making discretionary trades, or managing assets.<sup>138</sup> However, it remains unclear whether investment advice to plan participants, fiduciaries, investment managers, or entities would fall within the scope of the proposal.<sup>139</sup> Essentially, the regulations, in specific scenarios, would apply a fiduciary standard to broker-dealers.<sup>140</sup> The proposed regulation does not include a definition of fiduciary duty but, unlike NJ's Proposed Rule, does provide for a private right of action.<sup>141</sup> Currently, the proposed regulation is still waiting to be finalized but is expected to be completed before Fall 2020.<sup>142</sup>

Maryland took New Jersey's more straightforward approach by explicitly naming broker-dealers as fiduciaries regardless of how they interact with customers.<sup>143</sup> Maryland legislators and [\*329] the state attorney general put forward a bill, which consumer advocates see as model legislation proposing statutory fiduciary duties not only for broker-dealers and advisers but insurance agents as well.<sup>144</sup> On April 4, 2019, the fiduciary legislation did not receive the necessary votes.<sup>145</sup> It should be noted that unlike Maryland, New Jersey does not need congressional approval to enact their proposed rule, it need only follow their administrative law in promulgating a regulation.

On June 14, 2019, Massachusetts began seeking preliminary comments on a regulation that would apply a uniform fiduciary standard on broker-dealers, investment advisers, and their representatives.<sup>146</sup> The scope of the duty has not been yet determined, but the preproposal is very similar to New Jersey's Proposed Rule.

<sup>115</sup> Press Release, The State of New Jersey Office of The Attorney General, New Jersey Bureau of Securities Proposes New Rule Requiring NJ Financial Industry to Put Investors' Interest First (Apr. 15, 2019) (on file with author).

<sup>116</sup> See Fiduciary Duty, 51 N.J.R. 493(a) (Apr.15, 2019) (to be codified at N.J.A.C. 13:47A-6.4) (hereinafter "NJ Proposed Rule"); See Dishonest or Unethical Business Practices, 51 N.J.R. 493(a) (April. 15, 2019) (to be codified at [N.J.A.C. 13:47A-6.3](#)) (hereinafter "NJ Amended Rule").

<sup>117</sup> The rule proposal made numerous criticisms of the SEC rulemaking, including: Reg BI did not define "best interest"; Reg BI "sets ambiguous requirements for how longstanding conflicts in the securities industry must be addressed under the new rule"; and Reg BI failed "to indicate whether some of the most problematic practices in the securities industry would be prohibited under the new rule." See *Id.*

<sup>118</sup> See *Id.*

<sup>119</sup> See Melanie Waddell, *NJ Fiduciary Plan 'Far Exceeds' Other Rules: Lawyers*, 225 N.J. LAW J., 25 (2019).

<sup>120</sup> NJ Amended Rule, *supra* note 116.

<sup>121</sup> See Melanie Waddell, *supra* note 119, at 2.

<sup>122</sup> NJ Proposed Rule, *supra* note 116.

<sup>123</sup> NJ Proposed Rule, *supra* note 116.

<sup>124</sup> [\*De Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293, 1295 \(2d Cir. 2002\)\*](#) ("A securities broker ordinarily has no duty to monitor a nondiscretionary account, or to give advice to such a customer on an ongoing basis. The broker's duties ordinarily end after each transaction is done, and thus do not include a duty to offer unsolicited information, advice, or warnings concerning the customer's investments.")

<sup>147</sup>The fact that the proposal is so similar to New Jersey's may suggest an emerging model of regulation for uniform standards of conduct, which would mean a reduced "patchwork" of state fiduciary rules.

State-based fiduciary rule implementation timelines across the U.S. could be either extended or accelerated, depending on a number of factors. <sup>148</sup>To date, legislation for broker-dealer fiduciary duty is pending in 3 states -- Nevada, New Jersey, and Massachusetts. New or pending state fiduciary action may slow down to see what affect Reg BI has on investor protection when it goes into effect on June 30, 2020. Another factor that could impact states' timelines is that state legislatures reshaped to favor Democrats in the 2018 elections could **[\*330]** choose to move faster in the direction of strengthening conflict-of-interest regulations ahead of the 2020 elections. <sup>149</sup>

### C. Anticipated Litigation

Financial service professionals are vehemently opposed to state fiduciary action because they believe substantial inconsistencies between the federal standard and the proposed state rules will create confusion for consumers and financial professionals and come with high operational and compliance costs. <sup>150</sup>They argue that Reg BI should be fully implemented before moving forward with state-specific fiduciary rules.

Groups like SIFMA will likely challenge state fiduciary action on preemption grounds. Arguments used in a letter from SIFMA to Nevada officials after they released their draft rule could foreshadow arguments used in future litigation. <sup>151</sup>SIFMA's chief argument against state action to make broker-dealers fiduciaries will come under the National Securities Markets Improvement Act ("NSMIA"). <sup>152</sup>NSMIA delegated the authority to regulate the U.S. securities industry to federal agencies, forcing states to conform their financial regulation and recordkeeping requirements to federal law. <sup>153</sup>

Section 103 of NSMIA preempts states from establishing capital, margin, financial responsibility, and books and records requirements on broker-dealers that differ from, or are in **[\*331]** addition to, federal requirements. <sup>154</sup>Nevada's initiative, in particular is alleged to require additional recordkeeping to prove compliance with its rule,

<sup>125</sup> NJ Proposed Rule, *supra* note 116.

<sup>126</sup> *Id.*

<sup>127</sup> See Letter from Marc Cadin, President & CEO, Ass'n For Advanced Life Underwriting, to Christopher Gerold, Bureau Chief, N.J. Div. of Consumer Affairs (June 14, 2019) (on file with author)

<sup>128</sup> See *Id.*

<sup>129</sup> See *Id.*

<sup>130</sup> NJ Proposed Rule

<sup>131</sup> See Reg BI, *supra* note 69, at 14.

<sup>132</sup> SEC Inventory Advisor Com. On The Proposed CRS Relationship Summary Form, 115th Cong. 8 (2018) (Statement of David Certner on Behalf of AARP) (noting that "[r]ecent behavioral science studies have shown that disclosures are largely ineffective because they tend to increase conflict in advisers and make the investor more likely to trust the adviser and thus follow biased advice"); See Sunita Sah, *Gray Matter: The Paradox of Disclosure*, N.Y. TIMES, July 8, 2016: See Robert A. Prentice, *Moral Equilibrium: Stock Brokers and the Limits of Disclosure*, 2011 WIS. L. REV. 1059, 1105 (2011) ("There are now many, many studies which tend to indicate that mandated disclosure as a remedy--whether one addresses physicians' disclosures to patients, lenders' disclosures to borrowers, broker-dealers' disclosure to investors, or cops' disclosures to criminals (the Miranda warnings)--is often ineffective.").

<sup>133</sup> See Donald C. Langevoort, *Selling Hope, Selling Risk: Some Lessons for Law from Behavioral Economics About Stockbrokers and Sophisticated Customers*, 84 CALIF. L. REV. 627, 676 (1996).

so, eventually, when state regulators request materials confirming compliance with state regulations, broker-dealers may refuse to comply, which would bring the issue of preemption to the courts.<sup>155</sup> NSMIA does not entirely preempt state authority; Section 103 of NSMIA enumerates very specific and limited areas in which federal law preempts the ability of states from imposing additional obligations on broker-dealers.<sup>156</sup> I think the principal factor determining a court's holding, in adjudicating whether a state law or regulation governing broker-dealer conduct is preempted by Reg BI, is a court's interpretation and application of NSMIA.

Those who would oppose a fiduciary state law could argue that Section 103 of NSMIA preempts even those requirements that are not explicitly enumerated within a state's law. They could also argue that the state law would undermine congressional intent -- Section 103 of NSMIA was enacted to prevent a patchwork of state regulations that would impose duplicative and unnecessary regulatory burdens on broker-dealers.<sup>157</sup> In contrast, states could claim that Congress did not intend Section 103 of NSMIA to have a broad preemptive impact on states' regulation by noting Section 18 of the Securities Act of 1933, providing that the federal [\*332] government will not claim jurisdiction of a states securities commissions.<sup>158</sup> They would also point to the Exchange Act, which unambiguously established that state regulation of broker-dealers is only to be preempted to the extent that it conflicts with federal law.<sup>159</sup>

The legislative history of NSMIA offers both proponents and opponents of preemption with supporting arguments. A House committee report accompanying the NSMIA legislation states, "[t]he Committee does not intend [to] restrict or limit [State regulators'] ability to [enforce] State laws that prohibit fraud and deceit or that govern broker-dealer sales practices in connection with securities or securities transactions."<sup>160</sup> On the other hand, the conference report accompanying the final congressional passage of NSMIA states that the law is intended to prevent state laws from burdening financial professionals and increasing costs to consumers.<sup>161</sup>

What is important is that NSMIA does not completely preclude a state from any form of regulation over broker-dealers. Therefore, a preemption challenge would hinge on if a court finds: (1) compliance with both Reg BI and the

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<sup>134</sup> See Greg Iacurci, *New Jersey Fiduciary Rule Could Be First of Many Among States Post-DOL*, INVESTMENTNEWS: FIDUCIARY FOCUS (Sept. 26, 2018, 3:03 PM), <https://www.investmentnews.com/article/20180926/FREE/180929933/new-jersey-fiduciary-rulecould-be-first-of-many-among-states-post> [<https://perma.cc/S229-VB5S>].

<sup>135</sup> FINRA, 2019 FINRA Industry Snapshot, Annual Report, <https://www.finra.org/sites/default/files/2019%20Industry%20Snapshot.pdf> (last visited Oct. 17, 2019).

<sup>136</sup> In California, Missouri, South Carolina and South Dakota, brokers are already held by courts to fiduciary standards in varying degrees. In contrast, courts in 14 states have expressly held that a fiduciary duty does not exist between a client and a broker, according to the Connecticut legislative research report. The 14 states are Arizona, Arkansas, Colorado, Hawaii, Massachusetts, Minnesota, Mississippi, Montana, New York, North Carolina, North Dakota, Oregon, Washington and Wisconsin. Also, in Minnesota and Wisconsin there is flexibility where a broker doesn't owe a fiduciary duty to clients unless there is a special agreement between the parties. See Michelle Kirby, "Broker-Dealers' Standard of Care," Research Report 2017-R-0033, Conn. Office of Leg. Research (Jan. 26, 2017).

<sup>137</sup> Two of the nation's top brokerage firms -- Morgan Stanley and TD Ameritrade -- warned the Nevada Securities Division that if the state moved ahead with its fiduciary rule in its current form, they would stop serving customers in the state. See Melanie Wadell, Nevada Fiduciary Rule Would Scare Off Morgan Stanley, TD Ameritrade, ThinkAdvisor (Mar. 18, 2019) <https://www.thinkadvisor.com/2019/03/18/nevada-fiduciary-rule-would-scare-off-morgan-stanley-tdameritrade/>.

<sup>138</sup> Nevada, Notice of Draft Regulations and Request for Comment (Jan. 18, 2019), available at <https://www.nvsos.gov/sos/home/showdocument?id=6156>.

<sup>139</sup> See S. 383, 1st Sess., at Sec. 1.2 (Nv. 2017)

<sup>140</sup> See *Id.* at Sec. 2.

state law at issue is impossible; or (2) the state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Reg BI.<sup>162</sup> Reg BI certainly would preempt a state's heightened standard of conduct [~~333~~] for broker-dealers if the explicit terms of the state law were to violate any of the specific prohibitions in Section 103 of NSMIA. Less certain is how broadly or narrowly courts will interpret Section 103 for burdens that are not explicitly required by a state law, but are implicit with respect to how a broker-dealer would need to act to demonstrate compliance with it. I believe a court will interpret NSMIA as a guide on how to construct a state law or regulation that would not impose additional obligations on broker-dealers by enumerating specific areas in which states' ability to regulate broker-dealers is preempted. Because courts have not yet faced legal challenges to state regulations of broker-dealers under Section 103, there currently is no guidance as to how a court may interpret the NSMIA language.

Opponents of state fiduciary rules will also claim that their actions directly conflicts with ERISA.<sup>163</sup> State fiduciary rules may be preempted by ERISA § 514(a) if it creates fiduciary obligations with respect to qualified ERISA retirement plans.<sup>164</sup> It seems likely that the two provisions in NJ's Proposed Rule, carving out ERISA fiduciaries and stating that no additional recordkeeping requirements are imposed upon broker-dealers, were included in anticipation of preemption challenges.<sup>165</sup> Section (d) of NJ's Proposed Rule provides that the rule does not apply to a person acting in the capacity of a fiduciary to an Employee Benefit Plan, its participants, or beneficiaries, as those terms are defined in ERISA.<sup>166</sup> Section (e) provides that nothing in the proposed rule "shall be construed to establish any capital, custody, margin, [~~334~~] financial responsibility, making and keeping of records, bonding, or financial or operation reporting requirements for any broker-dealer or agent of any broker-dealer that differ from, or are in addition to, the requirements established under NSMIA."<sup>167</sup> However, in order to comply with NJ's Proposed Rule, such as showing that its recommendation is the best, it could be argued that a broker-dealer must keep records and take actions beyond those required by ERISA or NSMIA.

<sup>141</sup> See *Id.* at Sec. 9.

<sup>142</sup> Mark Schoeff Jr., *State securities regulators back Nevada's fiduciary rule proposal* (Mar. 7, 2019), <https://www.investmentnews.com/article/20190307/FREE/190309942/state-securities-regulators-backnevadas-fiduciary-rule-proposal>.

<sup>143</sup> See H.R. 786, 439th Gen. Assemb., Reg. Sess. (Md. 2019).

<sup>144</sup> *Id.*

<sup>145</sup> Mark Schoeff Jr., *Maryland fiduciary bill killed in committee*, INVESTMENTNEWS (Apr. 4, 2019), <https://www.investmentnews.com/article/20190403/FREE/190409963/maryland-fiduciary-bill-killed-incommittee>.

<sup>146</sup> William Galvin, *Preliminary Solicitation of Public Comments: Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives* (June 14, 2019), <http://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/fiduciaryconductstandardidx.htm>.

<sup>147</sup> See NJ Proposed Rule, *supra* note 116.

<sup>148</sup> Kenneth Corbin, "As SEC's Reg BI looms, states chart their own fiduciary path," Financial Planning (Feb. 4, 2019), available at <https://www.financial-planning.com/news/as-secs-regulation-best-interestlooms-states-chart-their-own-fiduciary-path>.

<sup>149</sup> See Kenneth Corbin, "Will fiduciary wave follow Democrat statehouse victories?," Financial Planning (November 7, 2018), available at <https://www.financial-planning.com/news/democrats-set-to-reintroducefiduciary-regulations>.

<sup>150</sup> See Melanie Waddell, *State Fiduciary Rules on a 'Collision Course'*, 26 N.J. Law J. 225 (2019).

<sup>151</sup> See Letter from **Kevin** Carroll, Managing Director & Associate General Counsel, The Securities Industry and Fin. Markets Ass'n, to Diana Foley, Nevada Secretary of State's Office, Securities Div. (Mar. 1, 2019) (on file with author).

Finally, opponents could argue that the commerce clause precludes states' fiduciary rule or regulation proposals because they impose a burden on interstate commerce that might be excessive in relation to the putative local benefits. I think this argument will almost certainly be unsuccessful because, as discussed previously, establishing broker-dealer fiduciary duty provides quantifiable benefits to the investing public.<sup>168</sup> Furthermore, it is well established, through the Exchange Act and state common law, that states may regulate broker-dealers.<sup>169</sup>

The ultimate outcome of whether Reg BI will preempt a state's action to impose its own standards of conduct on broker-dealers remains uncertain. However, I believe NJ's Proposed Rule will survive a preemption challenge because a court will find (1) its broker-dealer fiduciary standard is akin to the current investment adviser standard, so broker-dealers can comply with it while complying with Reg BI like investment advisers, and (2) it does not provide for additional compliance requirements. If New Jersey adopts its New Rule, the only outcome that is certain is that more resources there will be litigation to come.

No matter the outcome of these suits, at least one organization, the Certified Financial Planner Board of Standards ("CFP Board"), is taking action by establishing its own standard that [\*335] its members are required to abide by.<sup>170</sup> The CFP Board has long had a Code of Ethics and Standards governing the conduct of its members in providing financial planning services. In 2019, the CFP Board extended the standards to include a fiduciary duty owed to clients to cover financial advice to clients.<sup>171</sup> However, unlike a law or regulation, the standards would not create an enforcement right for regulators or investors; instead, a violation would only lead to disciplinary action by the CFP Board.<sup>172</sup> Nevertheless, given the value that advisers place on the CFP designation, it will likely have a significant impact on their practices.

## Part V. Conclusion

For multistate broker-dealers having to cope with different standards of care and loyalty in different states would be very complex and could lead to the strictest rule becoming, by default, a national standard. Experts are suggesting that national or regional firms that find themselves under a patchwork quilt of broker-dealer conduct

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<sup>152</sup> See NSMIA § 102(a), [15 U.S.C. § 77r\(a\)\(1\)](#) (2000).

<sup>153</sup> See *Id.*

<sup>154</sup> "No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall establish capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements for brokers, dealers, municipal securities dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this chapter." Section 103 of NSMIA; [15 U.S.C. § 78o\(i\)\(1\)](#).

<sup>155</sup> See Waddell, *supra* note 150 .

<sup>156</sup> "Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, over any security or any person." 73 Cong. Ch. 38, [48 Stat. 74](#), 85 (May 27, 1933).

<sup>157</sup> National Securities Markets Improvement Act of 1996, **Pub. L. No. 104-290**, 110 Stat. 3416 (codified as amended in scattered sections of 15 U.S.C. (2006)).

<sup>158</sup> "Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, over any security or any person." 73 Cong. Ch. 38, [48 Stat. 74](#), 85 (May 27, 1933).

<sup>159</sup> "Except as otherwise specifically provided in this chapter, nothing in this chapter shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations under this chapter." [15 U.S.C. § 78bb\(a\)\(1\)](#) (2016).

standards should develop policies and procedures that comport with the most restrictive standard.<sup>160</sup> The reasoning is that even if there never is a federal uniform fiduciary standard, policies, and procedures that comply with the most rigorous conduct standards will satisfy regulators' compliance expectations. Certainly, broker-dealers that do business in multiple states will find what the industry calls a "patchwork of rules" challenging to meet. However, as presidential administrations change, and with them, [\*336] rules finalized by previous agencies, confidence in even one set of federal rules becoming longstanding could be misplaced.

Conversely, it is possible that investors will seek financial services in states with less strict standards. Some like the National Association of Insurance & Financial Advisors - New Jersey ("NAIFA NJ") maintain that a fiduciary rule could push broker-dealers into denying access to commission-based accounts for those who hold small account balances.<sup>161</sup> They argue that the fiduciary standard may result in middle-income New Jersey residents being driven toward online brokerage services and losing out on quality investment guidance since some fee-based accounts have high minimum asset thresholds.<sup>162</sup> While some New Jersey investors may turn to online

<sup>160</sup> H.R. Rep. No. 104-622, at 30 (1996).

<sup>161</sup> *Id.*

<sup>162</sup> The SEC notes the following as unknown factors that will shape future judicial determinations in regard to the question of preemption: "(1) the final language in any proposed state legislation or regulation adopting a fiduciary or other standard for broker-dealers; (2) whether that language would constitute the type of law, rule, or regulation that is expressly preempted by the securities law or impliedly preempted under principles applied by courts; and (3) whether, if there was preemption, that preclusion of state law would have any positive or negative effects on investors when compared with the economic effects of Regulation Best Interest." Regulation Best Interest: The Broker-Dealer Standard of Conduct, [84 Fed. Reg. 33318, 33435](#) n. 1163 (July 12, 2019) (codified at 17 C.F.R. § 40).

brokerage accounts, I believe the benefit of NJ's Proposed Rule to the average investor will be substantial in the aggregate.

Customers deserve these reforms and broker-dealers will ultimately benefit from a fiduciary standard in the form of greater investor reliance on and confidence in their services. Broker-dealers should also benefit from lower litigation costs as they create improved supervisory systems and procedures to comply with the new obligations, leading to the discovery and correction of problems at an earlier stage. The marketplace needs a uniform fiduciary standard for broker-dealers to restore public trust in all financial professionals. Since the federal government has failed to protect investors adequately, New Jersey should take the helm by imposing a fiduciary standard on broker-dealers.

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163       *Id.* at 6-13.

164       Section 514 provides, in part, that ERISA "shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan" covered by ERISA. ERISA § 514(a).

165       NJ Proposed Rule,       *supra*, note 116, at § e. (providing that "nothing in N.J.A.C. 13:47A-6.4 shall be construed to establish any capital, custody, margin, financial responsibility, making and keeping of records, bonding, or financial or operation reporting requirements for any broker-dealer or agent of any broker-dealer that differ from, or are in addition to, the requirements established under [15 U.S.C. § 78o\(i\)](#).)

166       NJ Proposed Rule,       *supra*, note 116, at § d

167       *Id.*

168       See *supra* § III.A.

169       See *supra* § II.A.

170       See Bruce Kelly,       *Forget the SEC advice rule -- broker-dealers more concerned with CFP Board expanded fiduciary standard*,       INVESTMENTNEWS       (       Jun.       7,       2019),  
<https://www.investmentnews.com/article/20190607/FREE/190609945/forget-the-sec-advice-rule-broker-dealers-more-concerned-with-cfp>.

171       New Code of Ethics and Standards of Conduct, CFP Board, available at <https://www.cfp.net/for-cfpprofessionals/professional-standards-enforcement/code-and-standards>.

172       *Id.*

173       See Ghillaine Reid & Kurt Wolfe,       *Firms Should Stay Course Amid New Broker Standard Suits*, LAW 360 (Sep. 25, 2019), <https://www.law360.com/articles/1202473/firms-should-stay-course-amid-newbroker-standard-suits>.

174       NAIFA Trustee Testifies at New Jersey Fiduciary Hearing, Nat'l Ass'n Ins. and Fin.Advisors July, 18, 2019),  
<https://www.naifa.org/news-publications/naifa-blog/july-1/naifa-trustee-testifies-at-new-jerseyfiduciary-hearing>.

175       *Id.*