

**Written Testimony of
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Opposing SB 786 - Financial Consumer Protection Act of 2019
Before the Maryland Senate Finance Committee
1:00 PM - East Miller Senate Building, Room 3, Annapolis, MD
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Introduction

Thank for the opportunity to comment on the Maryland Financial Consumer Protection Act, which contains a provision imposing a fiduciary duty on broker-dealers, broker-dealer representatives, insurance producers, investment advisers, federal covered advisers, and on investment adviser representatives (the Maryland Fiduciary Provision).¹

My name is Dale Brown. I am the President and Chief Executive Officer of the Financial Services Institute (FSI). My comments address FSI's members' concerns with the possible implementation of a fiduciary standard of care in Maryland.

Background on FSI and Its Members

By way of background, FSI is an advocacy association comprised of members from the independent financial services industry. FSI consists of independent financial advisor members who are self-employed independent contractors, rather than employees, of our independent firm members. This means they are small-business owners with strong ties to their communities. They hire and pay their own employees, pay all of their own overhead costs, pay self-employment taxes, and embody the entrepreneurial spirit.

These independent financial advisors provide comprehensive and affordable financial services to individuals, families, small businesses, associations, organizations, and retirement plans. They assist these entities with services such as financial education, financial planning, and investment monitoring. Due to their unique business model, FSI independent firm members and their affiliated financial advisors are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their investment goals.

FSI has 635 financial advisor members operating in Maryland, as well as two firm members. According to a 2016 study by Oxford Economics, FSI members in Maryland support approximately \$1 billion in economic output.² This activity, in turn, supports 9,413 jobs including direct employees, those employed in the FSI supply chain (indirect), and those supported in the

¹ See Maryland Financial Consumer Protection Act of 2019, SB 786 (Feb. 4, 2019) (Maryland Fiduciary Provision).

² See Oxford Economics for the Financial Services Institute, The Economic Impact of FSI's Members p. 28 (2016), available at <https://financialservices.org/wp-content/uploads/2017/03/FSI-Impact-Report-Final.pdf>.

broader economy (induced).³ In addition, FSI members contribute over \$51 million annually to Maryland state and local government tax collections.⁴

FSI Position on the Fiduciary Provision

To be clear, FSI believes that all financial advisors, regardless of business model, should be obligated to act in their clients' best interest. Therefore, we support imposing an explicit best interest standard on broker-dealers, investment advisers, and their representatives. Nonetheless, FSI also believes that investors will only benefit from that heightened protection if the standard is effectively implemented, administered, and enforced. In this case, "effective" means a standard implemented, administered, and enforced on a federal level by the U.S. Securities and Exchange Commission (SEC). Moreover, FSI contends that uniformity is best achieved by imposing *equivalent* standards on investment advisers and broker-dealers rather than imposing *identical* standards that fail to account for the unique nature of those relationships and, similarly, fail to account for the different regulatory frameworks governing those financial professionals. Most importantly, the Maryland Fiduciary Provision would likely cause Marylanders to lose access to affordable professional financial services and advice because it would increase cost and complexity for financial advisors and clients. Finally, the provision may be preempted by federal law. If the provision is not preempted by federal law, effective enforcement would be impossible

Federal Best Interest Standard Is the Best Option

Since before Dodd-Frank became law, FSI supported a federal uniform standard of care for broker-dealers and investment advisers. In May 2018, the SEC published a comprehensive rulemaking package that includes rules establishing a standard of conduct for broker-dealers (SEC Proposed Regulation Best Interest) and enhancing investment advisers' disclosure obligations.⁵ The proposal maintains the nature and scope of investment advisers' fiduciary duty.⁶ The SEC intends to finalize those rules within the next six months.

Importantly, the SEC's proposal considers the distinction between clients' investment advisory relationships and their brokerage relationships.⁷ It also considers that investment advisers are regulated under the Investment Advisers Act of 1940 (Advisers Act); while broker-dealers are regulated under the Securities and Exchange Act of 1934 (Exchange Act) and are required to comply with self-regulatory organization rules.⁸ The Maryland Fiduciary Provision, conversely, combines broker-dealers, broker-dealer agents, investment advisers, federal covered advisers, investment adviser representatives, and insurance producers. The provision then groups those

³ *Id.*

⁴ *Id.*

⁵ See Letter from David T. Bellaire, Executive Vice President & General Counsel, Financial Services Institute, to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission at fn. 9 (August 7, 2018) available at <https://www.sec.gov/comments/s7-07-18/s70718-4181966-172528.pdf> (FSI Comment Letter in Response to SEC Proposed Regulation Best Interest).

⁶ See FSI Comment Letter in Response to SEC Proposed Regulation Best Interest, fn. 5, *supra*, at pgs. 43 – 44.

⁷ *Id.* at pgs. 7, 11 & 43.

⁸ See, generally, *id.* at p. 63.

financial professionals together and applies a single standard, despite important differences in each of the relationships, products, and applicable regulatory regimes.⁹ For instance, investment advisers, who offer advice for a fee, under the Advisers Act have a different relationship with their clients than the buy-sell brokerage relationship governed by the Exchange Act.

As we pointed out above, uniformity is best achieved by well-tailored, equivalent standards rather than imposing inapplicable, identical standards. In particular, FSI is concerned that this non-tailored approach may, unintentionally, put the Maryland's Commissioner of Financial Regulation in the unenviable position of having to craft regulations imposing a single identical standard to vastly different business models. The result will likely be regulations too expansive to provide actual investor benefit. Instead, the broad standard would likely confuse investors and, over time, that confusion would be vastly exacerbated by the creation of a patchwork of standards across the various states.

As the primary regulator of both investment advisers and broker-dealers, the SEC is uniquely positioned to articulate a uniform standard of care for both and to ensure that the standard is effectively implemented, administered, and enforced. An SEC uniform standard will help provide investors throughout the country with clarity. Thus, Maryland should refrain from the imposition of a fiduciary duty and instead await implementation of the SEC's Proposed Regulation Best Interest.

Moreover, the U.S. Department of Labor (DOL) announced plans to issue a revised final fiduciary rule package to replace the one vacated in spring 2018 by the U.S. Court of Appeals for the 5th Circuit. DOL has indicated it plans to issue this revised package in tandem with the SEC's final release of Regulation Best Interest. This should result in a comprehensive and consistent federal best interest standard that protects all retail investors.

Investors are Protected While the SEC Works on Its Final Rule

Maryland investors are currently protected and have recourse against financial advisors who do not act in their best interest. Investment advisers and dual registrants are already subject to a fiduciary duty under Section 206 of the Advisers Act, as interpreted by the U.S. Supreme Court in *SEC v. Capital Gains Research Bureau*. Similarly, independent broker-dealer firms are required to comply with the Financial Industry Regulatory Authority, Inc.'s (FINRA) suitability rule, which has been interpreted to require broker-dealers to act in their customers' best interest.¹⁰ In fact, prior FINRA guidance provided a host of examples where the SEC and FINRA found that broker-dealers who place their interests ahead of their customers' had violated FINRA's suitability rule.¹¹

⁹ See Maryland Fiduciary Provision, Sec. 5 Art. 11-803.

¹⁰ See, e.g., FINRA Regulatory Notice 12-25 at pgs. 3-4 (Additional Guidance on FINRA's New Suitability Rule) (explaining that "[t]he 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"), available at http://finra.complinet.com/net_file_store/new_rulebooks/f/i/FINRANotice12_25.pdf.

¹¹ *Id.* at pgs. 3-4 and fn. 15.

The Maryland Fiduciary Provision Would Negatively Impact Main Street Investors

FSI is concerned that the imposition of a fiduciary duty would result in Maryland investors losing access to much needed financial advice. FSI's mission is to ensure Main Street investors have access to affordable and competent financial advice and guidance.

Our dedication to this mission led to our participation in litigation that ultimately resulted in the DOL fiduciary rule being vacated by the U.S. Court of Appeals for the 5th Circuit. FSI's main objection to the DOL rule was that it was too complex and costly. In fact, the increased costs of that pending rule led several firms, including some of our members, to adopt plans to stop offering retirement planning services in exchange for commission revenue. Since the vast majority of retirement investors choose to pay for advice via commission, the provision of affordable, competent financial advice and guidance to Main Street Americans was diminished.

The adoption of a state-specific fiduciary standard in Maryland and other states would have the same flaws as the DOL fiduciary rule by significantly increasing costs that would eventually be passed on to investors. A state-specific standard would also likely lead some firms to stop offering commission-based financial planning services. Such a result would be unfortunate because studies indicate that investors who work with financial advisors save more, are better prepared for their retirement, and have greater confidence in their retirement planning.

Possible Federal Preemption

Section 103 of the National Securities Markets Improvement Act of 1996 (NSMIA) expressly pre-empts states from enacting regulations that impose new or different record keeping requirements than those established under the Exchange Act.¹² The provision states that it will not impose additional recordkeeping requirements on firms.¹³ If that is true, Maryland is, ultimately, introducing a provision that it will be unable to enforce because recordkeeping is a fundamental part of enforcing any law. Records offer proof of compliance, and without them demonstrating compliance – or even noncompliance – would be difficult, if not impossible. In addition to NSMIA, the Maryland Fiduciary Provision is likely preempted by other federal statutes.

However, if this provision is passed, in spite of these considerations, FSI urges the inclusion of a provision making it clear that registered broker-dealers and broker-dealer representatives who follow the rules and standards of their primary regulator will be deemed to be in compliance with the Maryland Fiduciary Provision.

Conclusion

We are committed to constructive engagement in this process and welcome the opportunity to work with the Senate Finance Committee on these efforts. We look forward to continued engagement and collaboration.

¹² Section 103 of the National Securities Markets Improvement Act of 1996, available at, <https://www.congress.gov/104/plaws/publ290/PLAW-104publ290.pdf>

¹³ See Maryland Fiduciary Provision at Sec. 5 Art. 11-803 (D).