

**Testimony of David T. Bellaire, Esq.
On Behalf of the Financial Services Institute
Before the New Jersey Bureau of Securities
July 17, 2019**

I. Introduction

Hello, my name is David Bellaire, Executive Vice President and General Counsel at the Financial Services Institute (FSI). FSI appreciates the opportunity to provide testimony today on this important issue. We thank Chief Gerold and the staff of the New Jersey Bureau of Securities for this chance to share our concerns with the proposal and our recommendation that it be abandoned.

II. Background on FSI Members

First, I would like to share some background on the Financial Services Institute, our members and the clients they serve because that information informs our perspective on the proposal. FSI is the trade association representing independent financial advisors and independent financial services firms. The independent financial services community has been an important and active part of the lives of American investors for more than 40 years. Our 100 member firms provide business support, supervision, execution and clearing services to the 160,000 independent financial advisors affiliated with them and the clients these advisors serve.

Independent financial advisors account for nearly 53% of all producing registered representatives.¹ These financial advisors are self-employed independent contractors, not employees of the firm.² As a result, they are small-business owners and job creators with strong ties to their communities. Independent financial advisors provide comprehensive and affordable financial services, including financial education, planning, implementation, and investment monitoring to middle-class and mass-affluent investors who want to ensure a dignified retirement, provide for the education of their children or achieve other Main Street economic goals.

FSI members make a significant contribution to the economy of New Jersey by generating \$2.2 billion of economic activity, supporting nearly 23,000 jobs and contributing \$10 million annually in state and local taxes. In fact, FSI members account for approximately 11% of the total financial services industry's contribution to the New Jersey economy.³

III. The Proposal burdens dual registrants and limits investors' choices.

Many of FSI's members are dual registrants – able to provide investors the support they need as a broker-dealer in exchange for a commission or as an investment adviser in exchange for an asset management fee. As dual registrants, our members are uniquely positioned to provide investors with advice, products, and services in their best interest. If an investor is just

¹ Cerulli Associates, Advisor Headcount 2016, on file with author.

² The use of the term "financial advisor" or "advisor" in this testimony is a reference to an individual who is a registered representative of a broker-dealer, an investment adviser representative of a registered investment adviser firm, or a dual registrant. The use of the term "investment adviser" or "adviser" in this letter is a reference to a firm or individual registered with the SEC or state securities division as an investment adviser.

³ Oxford Economics for the Financial Services Institute, The Economic Impact of FSI's Members (2016).

starting out and wants to open their first IRA with \$5,000 an independent financial advisor can offer through their broker-dealer a mutual fund or ETF in the most cost-efficient manner – the payment of a commission. If, however, a client needs more complex wealth management services our members are well-positioned to provide those services for an appropriate asset management fee. In other words, it is the independent financial advisors' dual registration status that allows them to do the most good for the most people.

Unfortunately, the Proposal contemplates holding a broker-dealer who also provides investment advice to a customer, to an ongoing fiduciary duty standard. The fiduciary duty would be applicable to the broker-dealer's entire relationship with the customer, regardless of the type of account that the customer holds.⁴ The proposal permits transaction-based compensation only if it is the best of the available fee options and presumes a breach of the duty of loyalty for certain recommendations that are not the so-called "best" of the reasonably available options.

Due to the increased costs associated with demonstrating compliance with the proposed New Jersey fiduciary standard, a broker-dealer would be discouraged from providing one-time or occasional investment advice to its brokerage clients even if such advice is in the clients' best interest. As a result, we believe the Proposal will deprive investors of the opportunity to choose the services and account type that best suits their needs and investment objectives. In addition, New Jersey investors with a smaller amount of investable assets may lose access to their chosen financial professional who can no longer afford to serve them. Each of these outcomes is contrary to the best interest of New Jersey investors.

IV. The Proposal is contrary to the congressional intent of the Investment Advisers Act of 1940, the position of the U.S. Securities and Exchange Commission, and the New Jersey Uniform Securities Law.

The Proposal would also impose a new regulatory structure that varies significantly from the current framework and would drastically alter the relationship between dual registrants and their retail clients. The Investment Advisers Act of 1940, the SEC, and the New Jersey Uniform Securities Law all recognize the fundamental differences between brokerage services provided in a broker-dealer capacity and advisory services provided in an investment adviser capacity. More specifically --

- The Advisers Act excludes from its registration requirements broker-dealers who provide advisory services that are "solely incidental to the conduct of their business as [brokers-dealers]," so long as they do not receive any special compensation for their advisory services.⁵
- The SEC reiterated this position in recent guidance that was issued as part of the Regulation Best Interest rulemaking package.

⁴ Fiduciary Duty of Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives, 51 N.J. Reg. 493(a) (April 15, 2019).

⁵ 15 U.S.C. § 80b-2(a)(11)(C).

- The New Jersey Uniform Securities Law excludes broker-dealers from the definition of an investment adviser.⁶

The Proposal would unnecessarily blur this critical distinction for dual registrants. These competing, conflicting and confusing regulatory burdens will harm investors by driving up costs and reducing access to financial advice, products, and services New Jersey investors need to achieve their financial goals.

V. The Proposal creates a confusing regulatory structure for broker-dealers who provide solely incidental investment advice.

The Proposal also creates a confusing regulatory structure for broker-dealers who provide solely incidental investment advice. It does not address the impact on consumers with respect to interstate issues, particularly where the rules or standard of conduct are different or incompatible. For example:

- How will the Proposal apply to financial advisors located in New Jersey who have clients who are located in states other than New Jersey?
- How would the Proposal apply to financial advisors who operate in states other than New Jersey, but provide advice to New Jersey residents?
- How would the Proposal apply to New Jersey financial advisors with clients who move to another state which has a different standard of conduct?
- How would the Proposal apply to New Jersey financial advisors with clients who split time between New Jersey and another state?

None of these important questions are answered by the current proposal.

VI. The Proposal imposes books and records requirements on broker-dealers that differ from, or are in addition to, federal requirements in violation of the National Securities Markets Improvement Act.

Avoiding confusing and duplicative regulatory burdens like these was Congress' intention when it passed the National Securities Markets Improvement Act (NSMIA) in 1996. Section 103 of NSMIA expressly preempts states from enacting regulations that impose new or different recordkeeping requirements than those established under the Securities and Exchange Act of 1934.⁷ While the proposal claims that it does not create new recordkeeping requirements for firms, this simply is untrue. The distribution of Reg Best Interest's Form CRS, the creation of the Reg BI required policies and procedures and other changes required by the SEC's recent rulemaking will accomplish many of the same purposes of the proposal. However, creating a state-specific fiduciary duty would require broker-dealers to create and maintain new records to demonstrate compliance with the state's unique fiduciary obligations. As a result, we believe NSMIA preempts New Jersey, and other states, from imposing such requirements.

⁶ N.J. Stat. Ann. § 49:3-49(g)(2)(iii).

⁷ Section 103 of the National Securities Markets Improvement Act of 1996, available at, <https://www.congress.gov/104/plaws/publ290/PLAW-104publ290.pdf>.

VII. Closing

In closing, FSI cannot support the proposal because:

- It burdens dual registrants and broker-dealers who provide solely incidental investment advice with a confusing and costly regulatory structure,
- It reduces investors' choices, raises the cost of investing, and deprives some investors of access to a financial advisor,
- It is in conflict with the congressional intent expressed in the Advisers Act, the position of SEC, and the New Jersey Uniform Securities Law, and
- It is preempted by NSMIA.

As a result, FSI calls on the New Jersey Bureau of Securities to abandon this proposal.

Thank you again for the opportunity to testify before the Bureau.