CENTER FOR CAPITAL MARKETS COMPETITIVENESS

MONEY MANAGEMENT INSTITUTE

December 14, 2018

Christopher W. Gerold
Bureau Chief, Bureau of Securities
P.O. Box 47029
Newark, New Jersey 07101

RE: Notice of Pre-Proposal: Amendment to N.J.A.C. 13:47A-6.3 (Fiduciary Duty)

Dear Chief Gerold:

We, the undersigned financial services trade associations, appreciate your continued engagement with the industry on your pre-proposal of a fiduciary duty for broker-dealers in New Jersey. As you are aware, there has been significant federal activity on this issue and great interest in pursuing a federal solution for most of the last decade.

As you consider moving forward with a proposed rule, we would like to bring the following to your attention:

- **There is Significant, Ongoing Federal Activity on an Enhanced Standard of Care for Broker-Dealers.** Shortly after the DOL's Fiduciary Rule was vacated by the Fifth Circuit, the SEC proposed its version of an enhanced standard of care for broker-dealers: Regulation Best Interest ("Reg. BI") and Form CRS. The SEC's comment period closed in August 2018. The SEC is currently evaluating the thousands of comments it received and intends to issue a final rule next year.[1]

[1] The full list of comments is available at: https://www.sec.gov/comments/s7-07-18/s70718.htm.

- **<u>Any State-Level Fiduciary Duty Faces Significant Pre-emption Hurdles</u>.** As you know, the National Securities Markets Improvement Act of 1996 added Section 15(i)(1) to the Securities Exchange Act of 1934, which precludes a State from enacting regulations relating to the making and keeping of records "that differ from, or are in addition to, the requirements in those areas established under [the Exchange Act]" (emphasis added). 15 U.S.C. §78o(i)(1). In turn, under the Exchange Act, Rule 17(a)-4 requires BDs to keep a record of "all communications … by the member … relating to its business as such…." 17 CFR §§ 240.17a-4(b)(4). These two federal provisions, taken together, raise significant questions about the ability to draft state-specific fiduciary regulations that do not violate NSMIA. In fact, we believe the difficulties around NSMIA pre-emption are one of the leading reasons that Nevada, despite having a state-specific fiduciary law on the books for over a year, has not yet proposed implementing regulations.

- **<u>Developing A State-Specific Fiduciary Standard is Problematic</u>.** As you know, the industry is already subject to a comprehensive regime of federal and state regulation that is enforced by multiple regulators. We remain concerned that state-specific fiduciary standards will result in inconsistent definitions and interpretations as to what constitutes a fiduciary – and subject investors, financial professionals, and firms to a confusing and potentially contradictory array of requirements. Should you decide it is necessary to move forward with a proposal, we encourage you to tie any specific requirements to FINRA Rule 2111, FINRA Regulatory Notice 12-25 and various interpretive guidance.

  We further understand that you may be considering using the fiduciary rule that was finalized by the U.S. Department of Labor and then vacated by the Fifth Circuit as a basis for your state regulation. That DOL Rule had significant flaws, including limiting investor choice in how to pay for retirement services, reducing access to investment advice, and limiting investor choice in retirement products. There were also fundamental differences between the DOL Rule and current securities regulation that would lead to investor confusion and create ambiguity for financial services firms.

  SIFMA also commissioned a study by Deloitte (summary) which found that, because of the now-vacated DOL Fiduciary Rule:

  - 53% of study participants had eliminated or limited access to brokerage advice services;

  - the shift of retirement assets to fee-based or advisory programs was accelerated; and

  - virtually all study participants had made changes to products available to retirement investors, with, for example, 29% eliminating No Load funds from their brokerage platform.

  The U.S. Chamber of Commerce also commissioned a study along with an impact analysis, which produced similar findings on the harm the DOL Rule caused to small savers. Specifically, the analysis found that 13.4 million accounts lost access to financial products as a result of the DOL Rule.

Mirroring the DOL Fiduciary Rule – particularly if you intend to apply it beyond retirement accounts – would exacerbate the harm caused by pushing financial professionals to fee-based or advisory models.

The increasing movement by firms and financial professionals to a fee-based business model could result in many lower and middle-market investors being without access to financial products and professional advice and services. Because of the nature and structure of the fee-based model, these accounts generally have higher fees and minimum asset requirements for investors of $250,000 or more. This will result in many lower and middle-market investors who typically have $50,000 to $100,000 to invest losing access to both financial products and professional advice and services.

Given the intense federal activity on this issue and sweeping changes that it has brought/is expected to bring to the industry and the capital markets, we strongly urge you to wait until the SEC's final rule is released and the nation's new regulatory landscape is set before pursuing any state-specific activity. The precise specifics of Reg. BI and Form CRS are particularly important in this case, especially due to the NSMIA constraints outlined above. For this reason in particular, we urge you to consider waiting for Reg. BI and Form CRS to be finalized before proposing any new state-specific rule.

Thank you for your time and consideration.

Sincerely,

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