

A Spring Into Chaos: Massachusetts Adopts Fiduciary Rule

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The standard of conduct for broker-dealers is quickly becoming a crazy quilt of securities regulation. Apparently unsatisfied with the standard established under SEC Regulation Best Interest (Reg BI), some state securities regulators have proposed — and, in the case of Massachusetts, adopted — a fiduciary duty even before the June 30, 2020, Reg BI compliance date.

The new Massachusetts fiduciary regulation amends the Massachusetts Uniform Securities Act to impose a fiduciary duty on broker-dealers and their agents when providing investment advice or recommending investment strategies to customers. The Massachusetts regulation requires each broker-dealer and agent registered and transacting business in Massachusetts to adhere to duties of utmost care and loyalty to the customer. The duty of care requires a broker-dealer or agent to use the care, skill, prudence, and diligence that a person acting in a like capacity and familiar with such matters would use.

Disclosure of conflicts of interest alone does not satisfy the duty of loyalty. Instead, the Massachusetts regulation requires broker-dealers and agents to “[m]ake all reasonably practicable efforts to avoid conflicts of interest, eliminate conflicts that cannot reasonably be avoided, and mitigate conflicts that cannot reasonably be avoided or eliminated.” The Massachusetts regulation also creates a presumption that a recommendation made in connection with any sales contest is a breach of the duty of loyalty.

The fiduciary duty runs “during the period in which incidental advice is made in connection with the recommendation of a security to the customer.” Under certain circumstances, however, the fiduciary duty extends beyond the recommendation, such as when a broker-dealer has discretionary authority over a customer’s account or an agreement with a customer calls for ongoing monitoring.

As adopted, the Massachusetts regulation applies to securities but not to insurance products. Based on enforcement history in Massachusetts, however, there was a question about whether the Massachusetts regulation would apply to the sale of variable annuities. Variable annuities are not securities under Massachusetts law. The financial press reports that, according to Securities Division personnel, the Massachusetts regulation does not apply to variable annuities.

As proposed, the Massachusetts regulation would have applied to investment advisers and their investment adviser representatives registered in Massachusetts. Commenters voiced opposition, including that advisers are already subject to a fiduciary duty under securities law. Accordingly, Massachusetts securities regulators removed investment advisers and their investment adviser representatives from the final regulation.

The Massachusetts regulation went into effect on March 6, 2020. The Massachusetts Securities Division will begin enforcing the rule on September 1, 2020.