#### COMMONWEALTH OF MASSACHUSETTS

SUFFOLK, ss.

SUPERIOR COURT DEPARTMENT

ROBINHOOD FINANCIAL, LLC,

Plaintiff,

v.

WILLIAM F. GALVIN, SECRETARY OF THE COMMONWEALTH, in his official capacity, AND THE MASSACHUSETTS SECURITIES DIVISION OF THE OFFICE OF THE SECRETARY OF THE COMMONWEALTH,

Defendants.

Civil Action No. 2184 ev 00884 BLS2

BRIEF OF AMICUS CURIAE NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC. IN SUPPORT OF DEFENDANTS WILLIAM F. GALVIN AND THE MASSACHUSETTS SECURITIES DIVISION

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### **INTEREST OF AMICUS CURIAE**

Formed in 1919, the North American Securities Administrators Association, Inc. ("NASAA") is the non-profit association of state, provincial and territorial securities regulators in the United States, Canada and Mexico. NASAA has 67 members, including the securities regulators in all 50 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands. The Massachusetts Securities Division, a defendant in this matter, is a NASAA member.

The overriding mission of NASAA and its members is to protect investors, particularly retail investors, from fraud and abuse. NASAA's members are responsible for administering state securities laws, including by: qualifying and registering broker-dealers, investment advisers, and their agents and representatives; conducting routine and for-cause examinations and audits; and enforcing the securities laws in criminal, civil and administrative enforcement actions. NASAA supports its members in carrying out their investor protection and regulatory duties by, for example, promulgating model rules and statutes, coordinating examination sweeps and multi-state enforcement actions, and commenting on legislative and rulemaking processes. NASAA also offers its legal analyses and policy perspectives to state and federal courts as *amicus curiae* in cases involving the interpretation of state and federal securities laws.

NASAA has an interest in this case because it raises fundamental questions of the scope of authority of state securities regulators and a federal preemption challenge to a state securities law. As will be shown below, the Secretary has authority to impose fiduciary duties on broker-dealers in certain circumstances through 950 C.M.R. § 12.207 (hereinafter, the "Fiduciary Rule") because the Secretary has broad discretion to regulate the conduct of broker-dealers doing business in the state under the Massachusetts Securities Act, M.G.L. ch. 110A § 101 *et seq*. Further, there is no conflict between the Fiduciary Rule and federal law that would warrant preemption. Plaintiff thus

cannot meet its high burden to show that the Fiduciary Rule is preempted, either broadly as to all broker-dealers operating in Massachusetts or narrowly as to Plaintiff itself.

### **ARGUMENT**

# I. THE SECRETARY HAS THE AUTHORITY TO PROMULGATE THE FIDUCIARY RULE.

# A. The Fiduciary Rule Is Consistent with the Broad Rulemaking Authority Granted to State Securities Regulators.

Across most U.S. jurisdictions, including Massachusetts, state securities regulators have broad statutory authority to make, amend and rescind rules that are necessary to carry out the purposes and objectives of their state securities laws. *See* Uniform Securities Act of 2002 § 605(a); Uniform Securities Act of 1956 § 412; M.G.L. ch. 110A § 412(a). This includes the authority to define terms, regardless of whether they are used in the statute, as long as the definitions are "not inconsistent" with the purposes, objectives or provisions of the statute. *See id.* This authority is broad and connotes wide-ranging discretion to administer state securities laws, regulate the conduct of securities industry participants in each state, and determine what actions are in the public interest to achieve those objectives. *See*, *e.g.*, *Blinder*, *Robinson & Co. v. Bruton*, 552 A.2d 466, 475 (Del. 1989) (stating that Delaware Securities Commissioner "has discretion to impose any penalty deemed necessary to protect the public interest and further the [Delaware Securities] Act's prophylactic purpose"); *cf. Goldberg v. Bd. of Health of Granby*, 830 N.E.2d 207, 213 (Mass.

The Uniform Securities Act of 2002 is available at

https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFile Key=04ece01b-d3d9-751d-9925-e5c4ca6c104f&forceDialog=0. The Uniform Securities Act of 1956 is available at <a href="https://www.nasaa.org/wp-">https://www.nasaa.org/wp-</a>

content/uploads/2011/08/UniformSecuritesAct1956withcomments.pdf. The Massachusetts Uniform Securities Act, M.G.L. ch. 110A § 101 et seq., is based on the Uniform Securities Act of 1956 and Section 412 therein is substantively identical to its counterparts in both versions of the Uniform Securities Act.

2005) (stating that a state administrative agency in Massachusetts "has considerable leeway in interpreting a statute it is charged with enforcing ....") (internal quotations omitted). Further, Massachusetts law "requires substantial deference to the expertise and statutory interpretation of [the] agency charged with ... administering a statute" and "regulations are not to be declared void unless their provisions cannot by any reasonable construction be interpreted in harmony with the legislative mandate." *Id.* (internal quotations omitted).

The Fiduciary Rule is in accord with the fundamental purposes and objectives of state securities laws. Although state securities laws provide a variety of civil, criminal and administrative remedies for various infractions, they are largely silent as to the broader standards of conduct applicable to broker-dealers, investment advisers and their respective agents and representatives, including whether broker-dealers should be required to adhere to fiduciary duties. The determination of those standards is instead left to the judgment of state securities regulators. State securities laws provide "significant latitude and deference" to regulators to supervise the conduct of the securities industry in their states and to determine what is in the public interest. See, e.g., Johnson-Bowles Co., Inc. v. Div. of Sec. of Dep't of Commerce of State of Utah, 829 P.2d 101, 114 (Utah Ct. App. 2001); cf. Krull v. SEC, 248 F.3d 907, 912 (9th Cir. 2001) (stating that "where Congress has entrusted an administrative agency with the responsibility of selecting the means of achieving the statutory policy the relation of remedy to policy is peculiarly a matter for administrative competence") (citation omitted). For example, when promulgating rules, state securities regulators generally have the discretion and authority to identify the persons subject to regulation and to prescribe requirements for those persons. See Uniform Securities Act of 2002 § 605(a)(3); Uniform Securities Act of 1956 § 412(a); M.G.L. ch. 110A § 412(a). State securities laws also generally grant administrators substantial discretion to interpret what conduct is

"unethical or dishonest" in the securities business. *See Johnson-Bowles*, 829 P.2d at 114 (holding that Utah's analogue to M.G.L. ch. 110A, § 204 "bespeaks a legislative intent to delegate the interpretation of what constitutes dishonest and unethical practices in the securities industry to the Division"); Uniform Securities Act of 2002, Comment 13 to Section 412 (citing *Johnson-Bowles*, 829 P.2d at 114, for same).

Further, like other state and federal securities laws, the Massachusetts Uniform Securities Act is a remedial statute intended to protect investors from all manner of fraudulent, abusive and harmful conduct and practices involving securities and investment advice. It is well-established that state and federal securities laws must be construed liberally to effectuate their remedial purposes. *See Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 151 (1972); *Cox v. Garvin*, 607 S.E.2d 549, 552 (Ga. 2005); *cf. Roberts v. Enterprise Rent-A-Car Co. of Boston, Inc.*, 779 N.E.2d 623, 627 (Mass. 2002) (stating that "we interpret consumer protection statutes broadly to effectuate their remedial purposes"); and *Batchelder v. Allied Stores Corp.*, 473 N.E.2d 1128, 1130-31 (Mass. 1985) (stating that the rule for construction of remedial statutes is that "cases within the reason, though not within the letter, of a statute shall be embraced by its provisions ....") (internal quotations omitted).

When applied to the Fiduciary Rule, these principles make clear that the Secretary acted within the scope of his mandate. The interpretation of definitions necessary to effectuate legislative purposes is precisely what securities administrators are empowered to do. Further, it is difficult to imagine an administrative action more aligned with the remedial goals of the securities laws than to require that those who provide investment advice and recommendations regarding some of the most consequential financial decisions a person can make to do so with the "utmost care and loyalty." 950 C.M.R. § 12.207(2).

### B. The Fiduciary Rule Is Consistent with Massachusetts Common Law.

Plaintiff argues that the Fiduciary Rule improperly abrogates Massachusetts common law, under which Plaintiff contends that a broker-dealer cannot be a fiduciary unless, by contract or practice, it makes investment decisions for the customer. Memorandum of Law in Support of Plaintiff's Cross-Motion for Partial Judgment on the Pleadings and in Opposition to Defendants' Motion for Partial Summary Judgment on the Pleadings ("Plaintiff's Memo") at 7 (citing *Patsos v. First Albany Corp.*, 741 N.E.2d 841 (Mass. 2001)). Plaintiff's reading of *Patsos* is flawed, and therefore its argument that the Fiduciary Rule abrogates common law is not correct.

Patsos does not stand for a general proposition that broker-dealers are not fiduciaries. On the contrary, the Supreme Judicial Court recognized that "in Massachusetts a relationship between a stockbroker and a customer may be either a fiduciary or an ordinary business relationship," Patsos, 741 N.E.2d at 848, and it acknowledged a "general agreement" among courts that "the scope of a stockbroker's fiduciary duties in a particular case is a factual issue that turns on the manner in which investment decisions have been reached and transactions executed for the account." Id. at 849 (citing federal and state decisions). In other words, Massachusetts common law as expressed in Patsos stands for the proposition that certain activities engaged in by broker-dealers are fiduciary in nature.

In its analysis, the *Patsos* court also specifically cautioned that "there is 'no bright-line' distinction between the fiduciary duty owed customers in discretionary as opposed to nondiscretionary accounts." *Id.* (citing and quoting *Romano v. Merrill Lynch, Pierce, Fenner & Smith*, 834 F.2d 523, 530 (5th Cir. 1987)). Instead, the court described a variety of circumstances which indicate that a broker-dealer has assumed fiduciary responsibilities. *See Patsos*, 741 N.E.2d at 850.

The Fiduciary Rule is faithful to the *Patsos* court's approach to determining when broker-dealer activities are fiduciary in nature. The Fiduciary Rule does not apply fiduciary obligations onto broker-dealers generally. Instead, it requires broker-dealers to adhere to fiduciary duties specifically when providing investment advice or making a recommendation, while having or exercising discretion, or while otherwise contractually obligated to act as a fiduciary. *See* 950 C.M.R. § 12.207(1). That is precisely what the *Patsos* court did; namely, it identified activities that are fiduciary by nature, and held that broker-dealers act as fiduciaries when they engage in those activities. The Fiduciary Rule is consistent with Massachusetts common law because it takes the same approach.

#### II. THE FIDUCIARY RULE IS NOT PREEMPTED BY FEDERAL LAW.

Plaintiff's preemption argument rests on a single theory that the Fiduciary Rule is "conflict preempted because it stands as an obstacle" to U.S. Securities and Exchange Commission ("SEC") Regulation Best Interest ("Reg. BI"). Plaintiff's Memo at 19 (citation omitted).<sup>2</sup> Plaintiff cites two objectives allegedly frustrated by the Fiduciary Rule: (1) "customers' ability to choose between fiduciary and non-fiduciary firms;" and (2) the promotion of clarity, consistency and ease of compliance. *Id.* at 21-22. This argument fails because Plaintiff cannot show that the Fiduciary Rule reduces investors' choices, and the second alleged objective is not an articulation of federal policy.

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Plaintiff makes clear that it is "only arguing that the rule is conflict preempted" and is "not arguing that the rule is express or field preempted." Plaintiff's Memo at 18 n.8. Plaintiff also does not argue that the Fiduciary Rule is conflict preempted because it is impossible to comply with both federal and state standards. *See id.* at 19.

## A. Plaintiff Cannot Show that the Fiduciary Rule Reduces Investor Choice.

Plaintiff mischaracterizes Reg. BI in order to assert a conflict. Reg. BI did not seek to preserve a choice between "fiduciary and non-fiduciary firms." Plaintiff's Memo at 21. Instead, Reg. BI seeks to preserve investor choice between transaction-based services typically offered by broker-dealers and fee-based services typically offered by investment advisers, the former of which are commonly thought to be lower cost than the latter. *See Regulation Best Interest: The Broker-Dealer Standard of Conduct*, SEC Rel. No. 34-86031 (June 5, 2019), 84 Fed. Reg. 33318, 33323 (July 12, 2019) (hereinafter, the "Reg. BI Adopting Release"). The SEC crafted a broker-dealer conduct standard less stringent than the fiduciary standard applicable to investment advisers because it was concerned that doing so would "risk reducing investor choice." *Id*.

However, it is important to understand that this facet of Reg. BI is based on an <u>assumption</u> that a uniform standard would reduce investor choice. Also, there is nothing that prevents a broker-dealer from offering transaction-based services under a fiduciary standard, particularly one in which the scope of those fiduciary obligations is limited to specified activities, as the Fiduciary Rule does. Indeed, as is made clear throughout this brief, the laws of Massachusetts and other states recognize that certain broker-dealer activities are fiduciary in nature, and that broker-dealers are bound to fiduciary standards of care and loyalty when acting in those circumstances.

Further, the Fiduciary Rule has been in effect since March 6, 2020, and broker-dealers – like Plaintiff – continue to operate in Massachusetts. There is no record before this Court which shows that the Fiduciary Rule has had any effect on the availability of transaction-based brokerage accounts to Massachusetts residents. Yet, without such evidence, Plaintiff cannot show that the Fiduciary Rule interferes with investor choice. This is not a showing that can be established as a matter of law; the conflict that Plaintiff asserts would require Plaintiff to produce "hard evidence

of conflict <u>based on the record</u>." *Sawash v. Suburban Welders Supply Co.*, 553 N.E.2d 894, 896 (1990) (citation and internal quotation omitted) (emphasis added).

For this reason, Plaintiff's reliance on Geier v. American Honda Motor Co., 120 S. Ct. 1913 (2000), is misplaced. Geier held that a common law state tort claim was preempted where the success of that claim would necessarily contradict a federal motor vehicle safety standard. See id. at 1922 ("The basic question, then, is whether a common-law 'no airbag' action like the one before us actually conflicts with FMVSS 208. We hold that it does."). That sort of conflict is not at issue here; the Fiduciary Rule does not exclude broker-dealers from providing transaction-based services in Massachusetts.<sup>3</sup> Nor is there any reason that broker-dealers cannot operate in Massachusetts under the terms of the Fiduciary Rule.<sup>4</sup> Because a broker-dealer is able to do so, it is not possible to find conflict preemption in this case. See Madeira v. Affordable Housing Foundation, Inc., 469 F.3d 219, 241-42 (2d Cir. 2006) (concluding that "the principle is thoroughly established that the exercise by the state of its police power, which would be valid if not superseded by federal action, is superseded only where the repugnance or conflict is so direct and positive that the two acts cannot be reconciled or consistently stand together") (citations and internal quotations omitted). Certainly, Plaintiff cannot meet the high burden required for preemption set by the Supreme Judicial Court of Massachusetts. See Sawash, 553 N.E.2d 896 ("Preemption ... is not

Perhaps the most salient example of this point is that Plaintiff states in its Complaint that it provides commission-free, transaction-based brokerage accounts to approximately 500,000 Massachusetts residents. *See* Complaint for Injunctive and Declaratory Relief, ¶¶ 1, 8.

Under the Fiduciary Rule, a broker-dealer can provide services and receive compensation on a transactional basis as long as it discloses and takes steps to address conflicts. See 950 C.M.R. § 12.207(2)(b); Mass. Sec. Div., Adopting Release Re: Amendments to Standard of Conduct Applicable to Broker-Dealers and Agents – 950 M.C.R. 12.200, 5-6 (Feb. 21, 2020), available at <a href="https://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/Adopting-Release.pdf">https://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/Adopting-Release.pdf</a>.

favored, and State laws should be upheld unless a conflict with Federal law is clear") (internal citation omitted).

## B. Plaintiff Cites No Other Federal Policy in Conflict with the Fiduciary Rule.

Without support or explanation, Plaintiff states that the Fiduciary Rule "conflicts with the federal policy set forth in Reg BI of 'promoting clarity, establishing greater consistency in the level of retail customer protections provided, and easing compliance across the regulatory landscape and the spectrum of investment professionals and products." Plaintiff's Memo at 22 (quoting Reg. BI Adopting Release at 33327) (emphases removed). This is not a statement of policy. The entire quotation from the SEC reads as follows:

<u>We believe</u> that Regulation Best Interest, Form CRS, and the related rules, interpretations and guidance that the Commission is concurrently issuing <u>will serve as focal points</u> for promoting clarity, establishing greater consistency in the level of retail customer protections provided, and easing compliance across the regulatory landscape and the spectrum of investment professionals and products.

Reg. BI Adopting Release at 33327 (emphases added). At most, this sentence (which is a summary of the overall package of releases of which Reg. BI was a part) expresses the SEC's hope for its efforts, but it cannot be characterized as a pronouncement of federal policy; the SEC does not state here, or elsewhere in the Reg. BI Adopting Release, that these are the objectives of the regulation. Further, administrative dicta is not a sufficient basis for preemption. The Supreme Court has expressed wariness for giving weight, particularly on questions of preemption, to superficial statements in the preamble of an agency's rulemaking. *See Wyeth v. Levine*, 555 U.S. 555, 577 (2009) (declining to defer to language of rule preamble and stating that "[t]he weight we accord the agency's explanation of state law's impact on the federal scheme depends on its thoroughness, consistency, and persuasiveness").

# C. Neither Congress nor the SEC Has Expressed an Intent to Preempt State Laws Like the Fiduciary Rule.

Plaintiff correctly declines to argue that the Fiduciary Rule is expressly preempted by federal law, but Plaintiff nevertheless suggests as much by arguing that Reg. BI is "intended" to have a preemptive effect. Plaintiff's Memo at 25. That is incorrect. As Defendants forcefully argue, the expression of a federal intention to preempt state law must be clear. *See* Defendants' Memorandum of Law in Support of Motion for Partial Summary Judgment on the Pleadings at 16-17. There is no such clear federal statement here.

Moreover, the Reg. BI Adopting Release preamble – from which Plaintiff seeks to find preemptive intent – is agnostic as to whether or when preemption will become an issue. Despite recognizing that "that there is substantial variation in the sources, scope, and application of state fiduciary law," Reg. BI Adopting Release at 33435, the SEC did not state that any state law or regulation ran afoul of Reg. BI. Nor did the SEC state that any aspect of any state law or regulation would be or should be preempted. On the contrary, the SEC recognized as part of its economic analysis that state laws or regulations might be <u>complementary</u> to Reg. BI by stating that "[t]o the extent that state-level law incorporates fiduciary principles similar to those reflected in Regulation Best Interest," the cost for broker-dealers to comply with Reg. BI in those jurisdictions "will be correspondingly reduced." *Id.* It cannot reasonably be argued that the federal government intended to preempt state law regarding broker-dealer conduct generally when it embraced the possibility that Reg. BI will be easier to apply in jurisdictions that have already paved the way for it by incorporating fiduciary principles into their broker-dealer conduct regulations.<sup>5</sup>

In fact, it may be that the Fiduciary Rule has already made Massachusetts a jurisdiction in which it is easier for broker-dealers to comply with Reg. BI.

The preamble language from the Reg. BI Adopting Release cited by Plaintiff does not express a clear intent to preempt state law. Instead, it shows only that the SEC recognized that the issue of preemption may come up in the future and, if it does, the outcome "would be determined in future judicial proceedings based on the specific language and effect of that state law." *Id.* at 33327. This language is nothing more than an acknowledgement that the potential for conflict preemption exists.

D. The Fiduciary Rule is Consistent with the Tradition of Federal and State Broker-Dealer Conduct Regulation Under Which States Sometimes Impose Higher Standards on Broker-Dealers than Exist Under Federal Law.

Since their inception, the federal securities laws have existed side-by-side with state securities laws. States began regulating securities at least as early as 1911, more than two decades before Congress. *See* I Loss, Seligman and Paredes, SECURITIES REGULATION 1.B.1 (6th ed. 2021). When Congress began regulating securities in the 1930s, 47 states – including Massachusetts – were already doing so. *See id.*; *see also McGray v. Hornblower*, 10 N.E.2d 501 (Mass. 1937). With the exceptions of clear instances of express or field preemption, none of which apply here, Congress has preserved the dual regimes of federal and state securities regulation. Further, because the federal securities laws have always existed against a backdrop of preceding state regulation, there has always been a degree of variation in broker-dealer conduct standards across the country. Indeed, like Massachusetts, other states have recognized and imposed fiduciary standards on certain broker-dealer activities. *See*, *e.g.*, *Apollo Capital Fund v. Roth Capital Partners*, 158 Cal. App. 4th 226, 246 (Cal. Ct. App. 2007) ("the rule is long settled [in California] that a stockbroker owes a fiduciary duty to his or her customer"); *Holmes v. Grubman*, 691 S.E.2d 196, 201 (Ga.

2010) (stating a broker-dealer's duties under Georgia law are "fiduciary in nature"). 6 Whether state broker-dealer regulations are less rigorous, more rigorous or identical to those under federal law, it is not impossible for broker-dealers to comply with both. Indeed, that has been the practice of compliant broker-dealers across the United States for decades. Without express evidence of an intention to preempt state regulation in this area, which Plaintiff neither offers nor purports to argue (because they simply do not exist), this Court should recognize that the history of dual regulation of broker-dealers is neither meant to be upset by Reg. BI, nor does the Fiduciary Rule stray outside of multiple instances in in which broker-dealers are already held to fiduciary standards under state securities laws.

#### **CONCLUSION**

For the reasons outlined above, the Secretary had authority to issue the Fiduciary Rule and Plaintiff has not met its burden of showing the Fiduciary Rule is preempted by federal law. Accordingly, Plaintiff's motion for partial judgment on the pleadings should be denied.

Respectfully Submitted

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

By its attorney,

For more information on federal and state broker-dealer conduct standards, see Arthur Laby, Fiduciary Obligations of Broker-Dealers and Investment Advisers, 55 VILL. L. REV. 701, 722-26 (2010) (retracing the framework of federal/state broker-dealer conduct regulation, stating

that courts "look to a number of factors to determine whether brokers are fiduciaries," and noting that some states impose fiduciary duties on broker-dealers even with respect to nondiscretionary accounts).

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Dated: September 15, 2021