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October 13, 2023

North American Securities Administrators Association, Inc.
Broker-Dealer Market and Regulatory Policy and Review Project Group
Broker-Dealer Section Committee

Sent by email to NASAAComments@nasaa.org

RE: Proposed revisions to NASAA's model rule on Dishonest or Unethical Business Practices Of Broker-Dealers And Agents (the "Business Practices Rule")

Dear Sir or Madam:

On behalf of a group of firm clients, including brokerage firms, mutual funds, insurance companies, asset managers, and banks, I am writing to provide comments on the proposed revisions to NASAA's model rule on Dishonest or Unethical Business Practices Of Broker-Dealers And Agents (the "Business Practices Rule") issued on September 5, 2023. We very much appreciate the opportunity to comment.

This letter focuses on the near inevitability of a successful preemption lawsuit invalidating some or all of the proposal if adopted by any state. To demonstrate that inevitability, it is important to dispel two very prominent myths about federal preemption and its impact on the proposal.

MYTH #1: When the Massachusetts Supreme Judicial Court upheld the validity of the Massachusetts fiduciary rule,[1] that resolved the preemption issues, paving the way for a rule like the NASAA proposal.

FACTS:

- **Conflict preemption.** ***The Massachusetts decision is an outlier on the issue of conflict preemption,*** i.e., whether the Massachusetts fiduciary rule is preempted by reason of its direct conflicts with the national and uniform regulatory regime clearly contemplated by Congress and established by the Securities and Exchange Commission ("SEC") in Regulation Best Interest ("Reg BI"). ***The highest courts in New York, Illinois,***

[1] *Robinhood Financial LLC v. Secretary of the Commonwealth*, Mass. Sup. Judicial Court, SJC -13381, August 25, 2023.

Pennsylvania, and Minnesota have directly addressed this exact same issue in the context of a state conflict with another SEC rule and found the state rules to be preempted.

- **NSMIA preemption.** The Massachusetts decision does not even address the clear grounds for preemption under the National Securities Markets Improvement Act (“NSMIA”).

  ERISA preemption. Similarly, the Massachusetts decision does not even address the clear grounds for preemption under the Employee Retirement Income Security Act of 1974 (“ERISA”).

These preemption issues are addressed in detail in the Appendix to the letter, entitled: “FEDERAL LAW PREEMPTS NASAA’S BROKER-DEALER PROPOSAL.”

MYTH #2: The NASAA proposal essentially is just the same as Reg BI, so how can it be preempted?

FACTS: The NASAA proposal goes far beyond Reg BI, so that no broker-dealer we are aware of would be even close to compliance with this very different new regime. The industry is working on a comprehensive list of the many respects in which the NASAA proposal goes far beyond Reg BI. Here, we simply mention two of the more egregious examples of going beyond Reg BI.

- **NASAA’s proposal generally limits broker-dealers and agents to commissions; all other pay is presumed to be illegal, such as bonuses, awards, or other incentives. Nothing remotely like this is in Reg BI.** The NASAA proposal states: “The broker-dealer or agent will be presumed to have placed its financial interest ahead of the interest of the retail customer where the broker-dealer or agent . . . rewards the broker-dealer or agent with additional cash or non-cash compensation beyond the sales commission as the result of that recommendation.”
  - **This difference alone would require a restructuring of the entire broker-dealer business.**
  - **This difference also would cause many broker-dealers to cease doing business in any state that adopts the NASAA proposal.**
    - **Background.** There are two ways to provide investment advice. First, there is the brokerage model where the broker-dealer is only paid based on transactions entered into, such as commissions. Almost all small investors get their advice through the brokerage model. The second model is the advisory model where a registered investment adviser provides fiduciary advice on a year-round basis for a fee, such as 1% of assets. Subject to certain exceptions for robo-advice, this model is generally only available to larger accounts because advisers realistically cannot have a year-round fiduciary duty in exchange for, for example, $30 (1% of a $3,000 account).
    - **The NASAA proposal would harm the very investors it seeks to protect.** Frankly, firms do not make a profit on $3,000 brokerage

accounts, so if state regulators or the Department of Labor ("DOL") impose costly and burdensome new rules on the brokerage model, firms will (1) accelerate the shift, already underway, from that model, which is how low- and middle-income individuals get their assistance, and (2) simply focus on the advisory model, which by definition is for higher income individuals. This is what happened with DOL's 2016 fiduciary rule[2] and would happen with the NASAA rule. The regulators are hurting the very people that they are trying to help.

- **NASAA's proposal covers far more than the recommendations covered by Reg BI.** Unlike Reg BI, the NASAA proposal applies not just to recommendations, but also to "any means, method or mechanism to feature or promote an account type, specific security or investment strategy to a retail customer." So, if a broker-dealer's website simply describes its advisory services or its types of accounts, that is presumably "featuring or promoting an account type," making that normal part of every firm website subject to the NASAA proposal. Another example would be if an e-mail promotes increasing monthly contributions to a retirement savings account, a positive investment behavior now subject to unnecessary regulation. These communications are already covered by the SEC's Marketing Rule, which went into effect 10 months ago and has been incorporated into a number of state statutes. This is another major departure from Reg BI.

We urge you to withdraw this harmful proposal in order to avoid costly and ultimately unsuccessful litigation for the states and to avoid the great harms described in footnote 2.

Sincerely,

Kent A. Mason

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[2] In 2017, Deloitte studied institutions representing 43 percent of U.S. financial advisers and 27 percent of the retirement savings assets in the market. Deloitte found that, as of the 2016 fiduciary rule's first applicability date, 53 percent of study participants reported limiting or eliminating access to brokerage advice for smaller retirement accounts, impacting an estimated 10.2 million accounts and $900 billion in savings. Deloitte Study Prepared for the Securities Industry and Financial Markets Association: The DOL Fiduciary Rule: A study on how financial institutions have responded and the resulting impacts on retirement investors (Aug. 9, 2017), available at: https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00599.pdf.

A 2021 study sponsored by the Hispanic Leadership Fund shows how badly a resurrection of the 2016 rule would hurt small savers, especially in communities of color. The study shows that the racial wealth gap with respect to IRAs would increase by 20% over 10 years if the 2016 rule is resurrected. Hispanic Leadership Fund Study: Analysis of the Effects of the 2016 Department of Labor Fiduciary Regulation on Retirement Savings and Estimate of the Effects of Reinstatement (Nov. 8, 2021), available at: https://hispanicleadershipfund.org/wp-content/uploads/2021/11/FINAL_HLF-Quantria_FiduciaryRule_08Nov21.pdf.

cc:
Broker-Dealer Market and Regulatory Policy and Review Project Group Chair Amy Kopleton (kopletona@dca.njoag.gov)

Broker-Dealer Section Chair Stephen Bouchard (stephen.bouchard@dc.gov)

All state regulators

APPENDIX

FEDERAL LAW PREEMPTS NASAA'S BROKER-DEALER PROPOSAL

On September 5, 2023, the North American Securities Administrators Association ("NASAA") issued proposed revisions to its model rule regarding Dishonest or Unethical Business Practices of Broker-Dealers and Agents ("Proposed Revisions"). According to NASAA, the Proposed Revisions are intended to update NASAA's model rules in light of the Securities and Exchange Commission's ("SEC's") 2019 adoption of Regulation Best Interest ("Reg BI"). However, the Proposed Revisions materially differ from Reg BI in ways that would cover broker-dealer practices that are well beyond the scope of Reg BI and impose obligations on broker-dealers that are far more onerous than Reg BI.

Given these material differences, if any state adopts NASAA's Proposed Revisions, such action would be invalidated by a court as preempted because it would create an obstacle to the accomplishment and execution of congressional objectives – namely, entrusting the SEC to establish a national and uniform system for the regulation of broker-dealers in accordance with the Securities Exchange Act of 1934 ("the Exchange Act"). The standards of care that apply to broker-dealers under that system are embodied in Reg BI, and any attempt by states to disrupt this national system, such as by adopting the NASAA Proposed Revisions, would be flatly preempted, based on clear case law from the highest courts of four states.

If any state adopts NASAA's Proposed Revisions, such action would also be invalidated by a court as expressly preempted under the National Securities Markets Improvement Act ("NSMIA"). NSMIA prohibits states from imposing recordkeeping burdens on broker-dealers beyond the recordkeeping burdens imposed by federal law. While NASAA's Proposed Revisions include a purported "savings clause" that is intended prevent NSMIA preemption, that savings clauses is invalid. In effect, the Proposed Revisions impose numerous new recordkeeping burdens. The savings clause then says that nothing in the Proposed Revisions shall be construed to impose new recordkeeping burdens. A court would have little trouble invalidating the Proposed Revisions, since there is no way to reconcile the recordkeeping requirements of the Proposed Revisions with the bizarre savings clause that is in direct conflict with rest of the Proposed Revisions.

Finally, the very limited exemption for broker-dealers functioning as fiduciaries under the Employee Retirement Income Security Act ("ERISA") reflects a basic misunderstanding of the fact that ERISA preemption applies without regard to whether a person is a fiduciary.

I. <u>NASAA's Proposed Revisions Go Far Beyond Reg BI</u>

Although NASAA describes its Proposed Revisions as incorporating Reg BI, its proposal goes well beyond Reg BI and the SEC staff guidance issued to help firms with implementation and compliance. The following examples illustrate this impermissible expansion.

- **<u>Broker-Dealer Compensation.</u>** Reg BI requires broker-dealers to eliminate sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sale of specific securities or specific types of securities within a limited period of time. For other forms of compensation, Reg BI requires broker-dealers to *mitigate* conflicts of interest that create an incentive for a natural person to place its interest (or its firm's interest) ahead of the interest of the retail customer.

  By comparison, NASAA's Proposed Revisions would impose a much more onerous limitation on broker-dealers by presuming a violation, if, as a result of a recommendation, a broker-dealer receives "any cash or non-cash compensation beyond the sales commission."[1] Although this standard is technically only a presumption, NASAA's explanatory materials make it virtually impossible to rebut this presumption.

  Relevantly, NASAA states that, when broker-dealers receive these forms of non-commission compensation, it "exacerbates rather than mitigates the potential for customer harm, as each incentive affirmatively places firm and agent financial interests incrementally ahead of the interests of their retail customers."[2] With this explanation, the proposal's presumption is most reasonably interpreted as a de facto prohibition that exceeds the limits imposed by Reg BI. Effectively, this presumption requires firms to eliminate forms of compensation for which Reg BI merely requires conflict mitigation.

  This is a dramatic departure from Reg BI and would trigger a complete restructuring of the entire brokerage industry by effectively prohibiting bonuses, awards, or other non-commission incentives. It is hard to imagine a more powerful case for conflict preemption than a state rule that disrupts an entire industry and renders a national system of regulation basically moot.

- **<u>Application.</u>** Reg BI details the standard of care that applies when broker-dealers make a "recommendation" to a retail customer. For this purpose, the term recommendation is supposed to be interpreted consistent with its traditional meaning within the context of broker-dealer regulation.

  By comparison, NASAA's Proposed Revisions would apply much more broadly to not only cover these traditional recommendations, but also to "any means, method or mechanism to feature or promote an account type, specific security or investment strategy to a retail customer."[3] This would include entirely benign communications, such as descriptions on a firm's website of its advisory services. Thus, NASAA's Proposed Revisions would regulate a vast amount of broker-dealer conduct that is not covered by Reg BI, in addition to broker-dealer conduct that is covered by Reg BI.

[1] Proposed Revisions, Part 1(d)(2)(b).

[2] Request for Public Comment on Proposed Revisions to NASAA's Dishonest or Unethical Business Practices of Broker-Dealers and Agents Model Rule (September 5, 2023), at 4.

[3] Proposed Revisions, Part 1(d)(5).

II. Federal Securities Law Preempts Patchwork Regulation of Broker-Dealers

Under longstanding Supreme Court precedent, federal law will not only preempt a state law when Congress expressly indicates its intention to preempt state law, but also when the state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[4] This is known as "conflict preemption," and if a state were to adopt NASAA's proposal, such action would be preempted as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress. In this regard, there are at least two congressional objectives that would be impeded if a state were to adopt NASAA's proposal: (1) Congress's objective to create a national system for the regulation of broker-dealers; and (2) Congress's objective for the SEC, and not the states, to determine the standards of care that apply to broker-dealers.

National Regulation of Broker-Dealers. The application of conflict preemption to state broker-dealer regulation is not a new issue and prior court rulings provide a clear roadmap for the preemption of NASAA's Proposed Revisions.

In the 1990s, for example, a series of courts were tasked with considering whether state fiduciary standards could compel broker-dealers to make compensation disclosures regarding order flow payments that were not required by SEC rules. On this issue, the highest courts of four states concluded that federal law preempted state fiduciary standards that would have compelled broker-dealers to take actions that were more exacting than the standards applicable under SEC rules.[5]

According to those decisions, any state fiduciary standards that are more stringent than the SEC's rules are preempted because, if permitted, they would create an obstacle to the accomplishment and execution of the full purpose and objectives of Congress – namely, Congress's objective of entrusting the SEC to establish a national and uniform system for the regulation of broker-dealers in accordance with the Exchange Act. Most notably, the Exchange Act expressly directs the SEC to "facilitate the establishment of a national market system for securities" in accordance with Congress's finding that "[t]he securities markets are an important national asset" and it is in the public interest to assure "economically efficient execution of securities transactions" and "fair competition among broker and dealers."[6]

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[4] *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941).

[5] *See Guice v. Charles Schwab & Co., Inc.*, 674 N.E.2d 282 (N.Y. 1996) (concluding that federal law preempted state fiduciary standards because state-by-state fiduciary standards would defeat Congress's intent for the SEC to develop a national market system); *Orman v. Charles Schwab & Co., Inc.*, 688 N.E.2d 620 (Ill. 1997) (holding that federal disclosure rules for broker-dealers preempted state fiduciary standards that would obstruct the national market system Congress intended to foster); *Shulick v. PaineWebber, Inc.*, 722 A.2d 148 (Pa. 1998) (concurring) (concluding that state fiduciary standards were preempted because allowing states to impose more stringent requirements on broker-dealers would render the federal scheme "largely nugatory" and would require brokers "to craft their disclosures to meet potentially dozens of different state standards"); *see also Dahl v. Charles Schwab & Co., Inc.,* 545 N.W.2d 918 (Minn. 1996) (concluding that federal law preempted state fiduciary standards for broker-dealers because Congress intended the SEC to regulate the securities markets and state law would effectively eliminate a form of compensation permitted by federal law).

[6] 15 U.S.C. § 78k-1.

As these courts explained, if states were permitted to impose obligations on broker-dealers that are more exacting than the standards imposed by the SEC, states could prevent the SEC from developing a national and coherent regulatory structure, and the resulting patchwork of state regulation would result in broker-dealers abandoning practices that would otherwise be permitted under SEC rules. If each state were permitted to impose its own standards of care for broker-dealers, national firms would need to tailor their practices to each state's laws. As a result, SEC rules such as Reg BI and the policy decisions reflected in those rules, would be supplanted by each state's own standard.

As an example, under NASAA's Proposed Revisions, a broker-dealer will be presumed to have committed a violation if a recommendation creates any cash or non-cash compensation for the broker-dealer beyond a sales commission. This would apparently create a presumption against the receipt of order flow payments, in addition to bonuses, awards, or other incentives. As explained above, however, order flow payments were at the heart of the four state supreme court cases concluding that federal law preempts state fiduciary standards that would otherwise subject broker-dealers to disclosure rules that are more exacting than the standards applicable under SEC rules. This example should give state securities regulators clear notice of the preemptive effect that federal securities law will have on any attempt to adopt NASAA's Proposed Revisions.

Very much like these previous cases, if any state were to adopt NASAA's Proposed Revisions, that action would very likely be preempted because it would create an obstacle to the accomplishment of Congress's objective of creating a national market system for the regulation of broker-dealers. This is because, as summarized above, the Proposed Revisions would cover broker-dealer practices that are well beyond the scope of Reg BI and impose obligations on broker-dealers that are far more onerous than Reg BI.

Congress Entrusted the SEC to Develop Broker-Dealer Standards of Care

Through section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), Congress charged the SEC with studying whether the existing regulation of investment advice to retail customers by broker-dealers was effective. In addition, Dodd-Frank authorized the SEC to promulgate rules, as necessary, to address such standards, including an authorization for the SEC to establish a fiduciary duty of care for broker-dealers akin to the standard that applies to investment advisers. As part of this potential standard, Dodd-Frank stated that, "The receipt of compensation based on commission *or other standard compensation* for the sale of securities shall not, in and of itself, be considered a violation of such standard applied to a broker or dealer."[7]

In 2019, through its publication of Reg BI, the SEC fulfilled this congressional direction and expressly declined to subject broker-dealers to the fiduciary standards imposed on investment advisers. In reaching this decision, the SEC cited how such a standard would reduce retail investors' access to services and products, reduce retail investor choice, and increase costs for

[7] Dodd-Frank Wall Street Reform and Consumer Protection Act § 913(k)(1) (emphasis added).

retail investors.[8] Furthermore, in the release accompanying Reg BI, the SEC explained that it would not be appropriate to incorporate the additional or different regulatory approaches that had been advocated by groups, including NASAA.[9]

If a state were to adopt NASAA's Proposed Revisions, it would create an obstacle to Congress's clear objective through Dodd-Frank of entrusting the SEC – and not the states – to determine the standards of care that apply to broker-dealers when providing investment advice, which the SEC did through Reg BI. Effectively, NASAA's Proposed Revisions are an attempt to resurrect some of the additional and different regulatory approaches that the SEC rejected when implementing Dodd-Frank. This is especially concerning, for example, in the case of the Proposed Revisions that would presume a violation when a broker-dealer receives cash or non-cash compensation beyond a sale commission. As noted above, through Dodd-Frank, Congress expressly stated its desire to preserve these forms of "other standard compensation."

III. <u>Massachusetts Is on an Island</u>

Notwithstanding the authorities and analysis summarized above, a recent decision from the Massachusetts Supreme Judicial Court ("MA Court") upheld a 2020 Massachusetts regulation that creates a fiduciary duty of care for broker-dealers that is more exacting than the obligations imposed on broker-dealers through Reg BI ("MA Fiduciary Rule"). That decision, however, was very flawed because it only provided a cursory review of the federal securities laws discussed above and below, and it completely failed to account for ERISA. Thus, it failed to appreciate the preemptive effect that federal securities laws and ERISA have on state broker-dealer regulation. Notwithstanding this cursory review of the relevant authorities, the MA Court was purportedly somehow able to divine congressional intent regarding the preemptive effect of federal laws on the MA Fiduciary Rule.

As demonstrated by the rulings from the highest courts of four states concluding that federal securities laws preempt inconsistent broker-dealer regulation by states,[10] Massachusetts is on an island in terms of its views on the ability of state securities regulators to impose broker-dealer obligations that exceed the standards imposed through the Exchange Act, SEC rules, and, as applicable, ERISA. It is very unlikely that future courts – especially federal courts -- considering similar issues, such as the preemption of NASAA's Proposed Revisions, will follow Massachusetts and recognize state authority to regulate broker-dealers in ways that contradict the express intentions of Congress and stand as an obstacle to congressional objectives.

For example, in arriving at its decision, the MA Court relied heavily on the fact that state fiduciary standards exist and states play a complementary role to the SEC in some securities regulation and enforcement. This is not disputed. However, this disproportionate emphasis on some state and federal overlap mistakenly fails to distinguish between the valid enforcement of state fiduciary standards that are consistent with federal broker-dealer regulation, and invalid attempts to create and enforce a patchwork of state-by-state standards that go well beyond the

[8] 84 Fed. Reg. 33318, 33322 (July 12, 2019).

[9] 84 Fed. Reg. at 33322-23, n. 36 (July 12, 2019).

[10] *See* footnote 7.

federal standards. While states may play a role in preventing activity that violates both state and federal securities rules, such as fraud, states clearly cannot be creating and enforcing broker-dealer standards that exceed the federal securities rules in ways that would contradict express congressional intent or disrupt the national market system envisioned by Congress. Furthermore, states cannot circumvent these constraints and attempt to assert their traditional police powers by simply labeling broker-dealer conduct that has been specifically considered and permitted by the SEC as fraudulent, dishonest, or unethical, when the targeted conduct cannot be reasonably associated with such labels.

As another example of the MA Court's flawed reasoning, instead of analyzing the MA Fiduciary Rule through the framework previously applied by the highest courts of four states, the MA Court instead relied heavily upon a series of cases that considered the preemptive effect of U.S. Department of Transportation regulations on state seat-belt requirements for car manufactures. In this regard, there was no meaningful consideration of how the express terms and structure of the Exchange Act reflect Congress's desire for a national and uniform regulation of broker-dealers. Whatever analogies the MA Court may have drawn from those automobile safety cases, the court's mistaken reliance on those cases is no substitute for a meaningful consideration of very clear precedent in four states that has specifically considered the intersection of state and federal securities rules as they relate to broker-dealer standards of care.

IV. NSMIA Preempts Proposed Revisions

Given the significant differences between the Proposed Revisions and Reg BI, if a state were to adopt the Proposed Revisions, such action would be invalidated by a court as expressly preempted under NSMIA. That is, through NSMIA, Congress amended the Exchange Act to expressly preempt certain state securities regulation by prohibiting states from subjecting broker-dealers to any state requirement involving the "making and keeping [of] records," if such requirements "differ from, or are in addition to," the requirements already imposed by federal law.[11] As the congressional managers of the Conference Committee for that law explained, NSMIA's preemption provisions are intended to "eliminate duplicative and unnecessary regulatory burdens [imposed by the states] while preserving important investor protections by reallocating responsibility over the regulation of the nation's securities markets in a more logical fashion between the Federal government and the states."[12]

The express congressional directive on broker-dealer recordkeeping was clearly intended to preempt any state regulations that would, in effect, require broker-dealers to collect and keep different or additional records to document compliance with state laws that differ from or add to federal rules, which NASAA's Proposed Revisions would clearly do. After all, any case brought by states or individual plaintiffs to enforce the Proposed Revisions would be highly dependent on the broker's books and records regarding compliance steps, which have been declared "off limits" to the states by Congress.

[11] 15 U.S.C. § 78o.

[12] H.R. REP. NO. 104-864, at 39-40 (Conf. Rep.).

NASAA's Proposed Revisions are drafted in a way that unsuccessfully attempts to avoid NSMIA's express preemption provisions by stating that it shall not "be construed to establish any requirements for capital, custody, margin, financial responsibility, making and keeping of records, bonding, or financial or operational reporting for any broker-dealer or agent that differ from, or are in addition to, the requirements established under [federal securities laws]."[13] This part of the Proposed Revisions is in irreconcilable conflict with the rest of the proposal, which requires extensive recordkeeping to demonstrate compliance with rules that differ from and add to federal regulation. Thus, this purported limitation is invalid and will not prevent preemption.

Even assuming for the sake of argument that the Proposed Revisions' savings clause could prevent NSMIA from expressly preempting a state rule that incorporates NASAA's proposal, it will make the state's rules unconstitutionally vague because it would fail to provide adequate notice to the regulated community about the conduct that is prohibited or required.[14] Regulated firms will feel compelled to collect and keep records to document compliance with state rules that differ from and are in addition to federal standards. Simultaneously, however, the purported savings clause tells firms that nothing in the Proposed Revisions may be construed as requiring them to keep such records. What is such a firm to do?

V. <u>ERISA Preempts Application to Employee Benefit Plans</u>

ERISA is a comprehensive federal statute regulating employer-sponsored retirement and welfare benefit plans. When Congress passed ERISA, it included an explicit and far-reaching preemption provision. According to that provision, and except as otherwise provided by law, title I and title IV of ERISA "*shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan*" (emphasis added).[15]

Because of ERISA's express preemption provision, if NASAA's Proposed Revisions are adopted by any state, such action will very likely be invalidated by a court as expressly preempted to the extent such rules relate to an employee benefit plan. This would occur, for example, if a state attempts to apply the Proposed Revisions in the context of a broker-dealer making rollover recommendations to employees participating in ERISA-covered retirement plans. In this context, the Proposed Revisions would clearly "relate to" an employee benefit plan.

NASAA's Proposed Revisions are apparently drafted in a way that attempts to avoid ERISA preemption by making its changes inapplicable to persons acting as "fiduciaries" within the meaning of ERISA, a term that has a very special and limited scope under Department of Labor regulations. This purported savings clause, however, does not avoid ERISA preemption because ERISA's preemptive power does not depend on whether a regulated party is an ERISA fiduciary

[13] Proposed Revisions, Part 1(d)(8).

[14] *See Gen. Elec. Co. v. U.S. E.P.A.*, 53 F.3d 1324, 1328–29 (D.C. Cir. 1995) ("In the absence of notice—for example, where the regulation is not sufficiently clear to warn a party about what is expected of it—an agency may not deprive a party of property by imposing civil or criminal liability.").

[15] ERISA § 514.

or not.[16] The only relevant preemption question is whether NASAA's Proposed Revisions "relate to" employee benefit plans, which they clearly would by creating new obligations for broker-dealers when making recommendations to retail customers, including participants in ERISA-covered retirement plans.[17]

As the Supreme Court has said, whether a state law "relates to" an employee benefit plan depends on the objectives of ERISA and the effect of state laws on ERISA plans.[18] And relevant to that determination in this context, ERISA carefully delineates who is a fiduciary for an employee benefit plan and who is not, and it sets forth the relevant standards of care. In doing so, Congress clearly declined to impose either fiduciary status or best interest obligations on ERISA plan service providers that are not ERISA fiduciaries. The Proposed Revisions would completely override Congress' decisions and assign best interest obligations to ERISA plan service providers that are not subject to any such obligations under ERISA.

In the context of employee benefit plans, states cannot choose to impose any new obligations on persons in their capacity as service providers to ERISA plans. Any such obligations clearly "relate" to ERISA plans. It is hard to imagine a clearer case for ERISA preemption. If this approach were successful in avoiding ERISA preemption, state laws could, contrary to Congressional intent, completely disrupt the national framework of laws applicable to ERISA plans by re-writing the duties of persons serving such plans.

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[16] *See Faulman v. Sec. Mut. Fin. Life Ins. Co.*, 353 Fed. Appx. 699, 702 (3d Cir. 2009) (explaining that ERISA fiduciary status is only one of several factors used to determine whether claims "relate to" an ERISA plan for preemption purposes); *Glaziers and Glassworkers Union Loc. No. 252 Annuity Fund v. Newbridge Securities, Inc.*, 93 F.3d 1171, 1185 (3d Cir. 1996) (even if a defendant is not an ERISA fiduciary, "state law claim[s] may 'relate to' an ERISA plan and be preempted").

[17] *See Kollman v. Hewitt Associates, LLC*, 487 F.3d 139 (3d Cir. 2007) (concluding that state law malpractice claims against a plan administrator who was not an ERISA fiduciary were preempted because the state law claims went to the "essence of the function of an ERISA plan").

[18] *Egelhoff v. Egelhoff ex rel. Breiner*, 532 U.S. 141, 147 (2001).