BETTER MARKETS

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Amicus Brief Filed By Better Markets and the Consumer Federation of America in Support of Legal Challenge to the SEC's Regulation "Best Interest"

FEDERAL AGENCIES:
Securities and Exchange Commission (SEC)

DESCRIPTION:
On June 5, 2019, the SEC adopted Regulation Best Interest ("Reg BI") under the Securities Exchange Act of 1934. On Sept. 10, 2019, XYPN, et al. filed a complaint with the U.S. District Court for the Southern District of New York. Better Markets and the Consumer Federation of America subsequently filed an amicus brief with the court on January 3, 2020.

THE RULE PROTECTS THE BROKERAGE INDUSTRY, NOT INVESTORS.

January 6, 2020 — In June last year, the SEC adopted its so-called "Regulation Best Interest," proclaiming that it would protect investors from the rampant conflicts of interest among broker-dealer advisers that cost everyday American investors tens of billions of dollars a year in lost savings. A group of financial planners—who are subject to a higher duty under the law as registered investment advisers—and a group of states rightly challenged the rule in the U.S. Court of Appeals for the Second Circuit. On Friday, January 3, 2020, Better Markets and the Consumer Federation of America joined together and filed a "friend of the court" brief siding squarely with the challengers and urging the court to invalidate the rule on numerous grounds:

Most investors have to rely on financial advisers for investment guidance.

Every year, millions of vulnerable retail investors who lack financial expertise place their trust in financial professionals and seek advice to help them plan for a secure and dignified retirement, a child's college education, or other long-term goals. Investors reasonably expect that, regardless of what type of financial professional they turn to—either a broker-dealer or a registered investment adviser—the advice they receive will be in their best interest, untainted by harmful conflicts of interest.

The SEC has allowed broker-dealers to exploit their clients by providing self-serving advice.

Unfortunately, the SEC has for decades perpetuated a regulatory framework that applies different standards to the same advisory services and fails to ensure that all investors receive advice in their best interest. The agency's approach has fostered widespread confusion among investors regarding the standards of conduct applicable to their trusted financial professionals. Worse, it has allowed broker-dealers to market themselves as advisers and to function as such, while also allowing them to act on powerful conflicts of interest by recommending over-priced and under-performing investments that line the broker-dealers' pockets but cost investors tens of billions of dollars a year in lost savings.

Congress gave the SEC authority to solve the problem in the Dodd-Frank Act.

Congress recognized these profound shortcomings in the SEC's regulation of financial advice, and it responded by granting the agency ample authority to cure those deficiencies through a rulemaking pursuant to Section 913 of the Dodd-Frank Act. Section 913 was written and widely understood as a framework for the SEC to adopt a uniform fiduciary standard for broker-dealers and investment advisers who give personalized investment advice to retail investors, one that would effectively protect investors from conflicts of interest.

The SEC failed, issuing a weak and misleading rule that violates Congress's letter and intent.

After years of delay, the SEC issued Reg. BI, Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 Fed. Reg. 33,318 (July 12, 2019) ("Release"), but it did so in clear violation of Congress's explicit language and remedial intent under Section 913. The SEC chose to promulgate a weak and confusing rule applicable solely to broker-dealers, which solves none of the problems confronting investors in need of sound financial advice: The Rule will not impose a uniform standard of conduct on broker-dealers and investment advisers; it will not eliminate investor confusion; and it will not protect investors from the conflicts of interest and resulting financial harm that continue to plague the market for financial advice.

- **Two different standards.** The Rule preserves an anti-investor regulatory environment in which different financial professionals who provide functionally identical services will continue to be subject to different standards of conduct.

- **Investor confusion.** The burden of cutting through this regulatory web of confusion will fall on investors, yet many investors will be unable to make heads or tails of the regulatory landscape or make informed decisions about which professionals they should trust.

• **Investor deception.** Worse, many investors will be lulled into a false sense of security that they are receiving high-quality "best interest" advice that is untainted by conflicts of interest, but in reality, the Rule will allow brokers to dispense highly conflicted sales recommendations that undermine the financial security of those investors.

• **The harm continues.** If the Rule remains in place, investors will continue to suffer very real financial harm as a result of broker conflicts of interest, and the harm will be magnified by virtue of the Rule's misleading nature. The Rule adds virtually nothing to the rules already in place that provide little protection against conflicts of interest. It does not actually require advisers to act in the best interest of their clients, and it relies heavily on disclosure, despite ample evidence that disclosure does not and will not protect investors from adviser conflicts of interest.

The SEC relied on a bogus justification, catered to industry, and betrayed the investors it was established to protect.

The SEC attempted to justify this weak, confusing, and misleading regulatory approach with the pretense that it would actually help investors by preserving investor "choice," a claim endlessly repeated in the Release accompanying the Rule. This was a spurious rationale, since the record does not support the notion that a strong and uniform rule would destroy the broker-dealer business model or deprive investors of valuable choices regarding investment options or payment models. In reality, no investor needs the "choice" to be exploited by their adviser or sold poor-performing, over-priced products that enrich brokers at their own expense.

The court should vacate the rule.

A rule so clearly at odds with Congress's plain language and intent, born of such badly skewed priorities, and lacking a credible analysis and justification, is both unlawful and arbitrary and capricious under the Administrative Procedure Act ("APA"). The Petitioners' challenge to the Rule is well-founded and the Rule should be vacated.

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