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## The Seventeenth Annual A.A. Sommer, Jr. Lecture on Corporate, Securities and Financial Law at the Fordham Corporate Law Center

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## LECTURE

### THE SEVENTEENTH ANNUAL A.A. SOMMER, JR. LECTURE ON CORPORATE, SECURITIES AND FINANCIAL LAW AT THE FORDHAM CORPORATE LAW CENTER†

### SEC—DON'T THROW AWAY YOUR SHOT! A RENEWED CALL FOR A UNIFORM FIDUCIARY STANDARD TO PROTECT INDIVIDUAL INVESTORS

#### WELCOME AND INTRODUCTORY REMARKS

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† The lecture was held at Fordham University School of Law on November 16, 2016. It has been edited to remove minor cadences of speech that appear awkward in writing and to provide sources and references to other explanatory materials in respect to certain statements made by the speakers.

\* Matthew Diller is the Dean of Fordham University School of Law.

\*\* Ben Indek is a Partner at Morgan, Lewis & Bockius.

\*\*\* Ira D. Hammerman is the Executive Vice President and General Counsel for the Securities Industry and Financial Markets Association (“SIFMA”). The views expressed in this lecture are Mr. Hammerman’s personal views and do not necessarily reflect the views of SIFMA. Mr. Hammerman deeply appreciates the assistance of his longtime colleague, Kevin M. Carroll, in both the preparation of this lecture and his counsel on the long running fiduciary duty debate.

**WELCOME AND INTRODUCTORY REMARKS**

DEAN DILLER: Good evening. My name is Matthew Diller, and I have the honor of being the Dean of Fordham University School of Law. I would like to welcome all of you to the seventeenth Annual Sommer Lecture, which we are very proud to host here at the law school. In a few minutes, you will be hearing the lecture delivered by Ira Hammerman, and we are very excited to have you here with us tonight and very interested in hearing your remarks and your thoughts.

The Sommer Lecture is a great partnership between the firm of Morgan Lewis—and I am pleased to see so many Morgan Lewis representatives here with us tonight—and Fordham Law School, and in particular, with our Corporate Law Center here at Fordham.

That marriage is not an incidental or accidental result; rather, it stems from the work of the great John Peloso. I want to acknowledge and thank you, John. John is a graduate of our school from the Class of 1960. He is a founder of the Corporate Law Center here at Fordham. The Corporate Law Center is a key part of our business law programs. We are one of the great business law schools in this country, and that is in good measure due to the work that we do through the Corporate Center, which is our major hub of activity around corporate law.

John had the foresight and vision to help us found the Center and help build it and grow it to where it is now. He has also taught here as a member of our adjunct faculty, and it is always a pleasure to see you and to collaborate with you, John.

I am also grateful to Ben Indek, a Partner at Morgan Lewis. Thank you for your support and your collaboration, both tonight and into the future in this greater collaboration between our school and your great law firm.

I want to say a couple of more things about the Corporate Law Center, and then we can get on with this evening's main event. I do want to point out that the Center was established in 2001. There are three areas that it focuses on: the first is public lectures; to wit, roundtable discussions, expert panels, conferences, and programs that help educate those in the legal community, business community, and the public at large on important issues around corporate governance and corporate law. The Center is also a platform that showcases and supports the work of our fabulous faculty—a number of whom are with us tonight—in the field of corporate law. Corporate law has played a key role in bringing our faculty together and projecting our research and work out into the world. Third,

and extremely importantly, the Center is a resource for students here at Fordham Law School. It connects them to our alumni through the business law practitioner series and through a variety of other mentoring programs that bring our students on board and help carry forth our school's tradition in corporate law.

Finally, I will mention one more aspect of the Corporate Law Center, which is a relatively new initiative: our corporate compliance initiative. We have seen the tremendous growth in compliance as a field. Given our strength in corporate law and financial regulation, we have established the first LL.M. degree in corporate compliance, and we have followed that by establishing what is called an M.S.L. degree, a Master of Studies in Law, a one-year Master's degree for non-lawyers who want to specialize, focus, and build careers in compliance. That program started in January. We have a number of exciting upcoming events. I will not list them all; instead I will direct you to the Corporate Law Center website.

I also want to thank Vera Korzun for putting together and coordinating tonight's program and for all the work that you do as Director of the Center. At this point, I want to introduce Ben Indek of Morgan Lewis, who will then introduce Mr. Hammerman. Thank you all.

MR. INDEK: Good evening, everybody. On behalf of Morgan Lewis, I wanted to offer my own welcome to the seventeenth Annual A. A. Sommer, Jr. Lecture.

In 1979, Al Sommer started Morgan Lewis' securities regulatory practice. We created this lecture series in his name as a way to honor his contribution to our firm and his enduring legacy at Morgan Lewis.

The last several years have been very exciting for our firm. We elected a new chair, Jami McKeon, an incredible leader for Morgan Lewis and a true visionary in the changing landscape of the law firm world. She is also fully and enthusiastically committed to our securities regulatory practice. We welcomed hundreds of lawyers through our combination with Bingham, including many exceptional attorneys in the securities enforcement, regulatory, and class action practices. We expanded internationally as well, merging with one of the most prominent firms in Singapore and adding a vibrant new office in Shanghai. Tonight we pause to thank Al and his colleague Lloyd Feller, who is here tonight, for creating this practice area at Morgan Lewis more than three decades ago. We stand on their broad shoulders.

A little history: Al was a Morgan Lewis partner from 1979 until 1994 when he became counsel to the firm. He was a tireless public servant, a Securities and Exchange Commission ("SEC") commissioner, Chairman

of the Public Oversight Board, and a public member of the American Institute of Certified Public Accountants.

As a private practitioner, Al was a trusted adviser, a prolific author, and an expert on many securities laws, regulations, and rules. We were lucky to have Al participate in the first two lectures, but unfortunately he passed away in 2002. We are delighted that his family continues its close relationship with Morgan Lewis and Fordham and that they are here with us again this evening. We are also pleased by the continuing support of the SEC Historical Society and its Executive Director, Carla Rosati, for their contribution to this lecture series. Al gave the Society his time and some of his papers to help make the organization a terrific historical resource.

Turning to tonight's speaker, Ira Hammerman: Ira is the executive vice president and general counsel for the Securities Industry and Financial Markets Association ("SIFMA"). Since 2004, Ira has overseen SIFMA's legal advocacy efforts, including its response to the 2008 financial crisis and the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"). Prior to joining SIFMA, Ira was a partner at Clifford Chance, where he represented a wide range of financial services companies in regulatory and enforcement matters. In short, Ira has devoted his career to the securities industry and is one of its most passionate, articulate, and persuasive advocates.

On a more personal note, I like to think that Ira is like the movie star Kevin Bacon, not because of his dance moves—although I am sure they are stellar—but because he is an icon of interconnectedness. If you will indulge me, I would like to explain with a version of the parlor game *Six Degrees of Kevin Bacon*, featuring Ira Hammerman in the role of Kevin Bacon. For those of you not familiar with this pastime, because Bacon has been in so many different types of Hollywood movies, the premise of the game is that he can be connected to almost any actor with only a few steps; the number of steps is a person's "Bacon number."

For example, Marlon Brando can be connected to Kevin Bacon in just two steps: Brando was in the movie *The Score* with Robert De Niro, who was in *Sleepers* with Kevin Bacon; Brando's Bacon number is two.

But back to Ira: Ira is connected to Morgan Lewis in many ways, leading to Hammerman number possibilities. Ira's father, Steve Hammerman, like Al, was a senior leader at the SEC. Steve served as Regional Director of the SEC's New York office. As General Counsel at Merrill Lynch, Steve was a mentor to several lawyers who later became partners at Morgan Lewis and was a longtime client of the firm. He

worked with our own John Peloso and literally dozens of others at the firm on one of Merrill Lynch's greatest legal challenges, the bankruptcy of Orange County, California; Hammerman number—two.

Ira's brother, Charlie Hammerman, was an associate at Morgan Lewis before he went on to create and run an outstanding nonprofit organization called The Disability Opportunity Fund. It helps disabled people throughout the country in the areas of housing, education, and training. Our former partner, Anne Flannery, who is also here tonight, serves on the organization's board of directors; Hammerman numbers—two and three.

And, oh yes, there is Ira himself. At Morgan Lewis we have had the privilege of working closely with Ira on several important initiatives at SIFMA, including most recently his efforts in the area of fiduciary duty in the securities industry. We have had a long and productive relationship with Ira and his team at SIFMA, where a couple of our former colleagues work. I am not good at math, so I have lost track of the Hammerman numbers. We look forward to continuing to assist SIFMA in the years ahead. Now that you know how he is connected, we are thrilled that Ira is here to speak tonight.

Last year's speaker, former SEC Commissioner Joe Grundfest, gave us a speech with the catchy title, "Is the SEC Afraid of Federal Juries and Judges?" Not to be outdone, tonight Ira gives a nod to pop culture and Lin-Manuel Miranda's Broadway hit *Hamilton* and is set to deliver, "SEC—Don't Throw Away Your Shot! A Renewed Call for a Uniform Fiduciary Standard to Protect Individual Investors." It promises to be a blockbuster. Incidentally, if you want to know Miranda's Bacon number, see my colleague Ariel Gursky at the reception—she has the answer.

In any event, I know that Al would have loved to be here tonight to listen to Ira take his shot and, if we are lucky, rap a little chorus. Morgan Lewis is proud of Al Sommer's dedication to the securities bar and his affiliation with our firm, and we are pleased to sponsor this annual lecture in his honor. I am delighted to turn the podium over to our speaker tonight, Kevin—I mean Ira—Hammerman. Thank you.

## LECTURE

IRA D. HAMMERMAN: Thank you, Ben, for that kind and funny introduction. Oh, and by the way, my Bacon number is four. You see, a few months ago I met Lin-Manuel Miranda—that is one; Lin was in *The Polar Bears*, a movie with Armie Hammer—that is two; Hammer was in *The Social Network* with Jason Flemyng—that is three; and Jason was in *X-Men: First Class* with Kevin Bacon—that is four. Do you follow all that?

Now that we got that out of the way, let me say I am very honored and humbled to join you today to deliver the seventeenth Annual A. A. Sommer, Jr. Lecture. I would like to thank both Morgan Lewis and Fordham Law for giving me the privilege of addressing you this evening, and it is extra special to deliver this lecture in front of Starr and some of Al's other family members who I had the pleasure to meet a few moments ago. As we all know, Al Sommer was a leader and pioneer at Morgan Lewis and began that fine firm's focus and preeminence in securities law and in serving the financial services industry.

At the risk of inadvertently leaving anyone out, Morgan Lewis gave us an earlier generation of leaders that I have come to know and respect, many of whom are here tonight: folks like Lloyd Feller, John Peloso, Anne Flannery, Bob Romano, John Hartigan, and Bob Mendelson, among many others, and today's leaders, like Ben Indek, Steve Stone, John Ayanian, Sam Shaulson, Dan Kleinman, and Jon Roelke, who continue that fine tradition. So thank you, Morgan Lewis, for thinking of me for this honor.

I would also like to thank Fordham Law School, which has partnered with Morgan Lewis since 2000, when this important lecture series to honor Al began.

I am embarrassed to say it has been over thirty-one years since I visited Fordham. But I have a really, really good excuse. You see, the last time I was here, July 30 and 31 of 1985, it was a traumatic couple of days. Yes, I had the lucky privilege of sitting for the New York bar exam right here at Fordham. Now, I say "lucky" intentionally because that was the summer that 542 bar exam answer sheets were lost—or is stolen the right word?—from the Pier 90 location where so many other law school graduates took the exam that summer, thirty-one years ago. That is a true story—you can Google it—so, believe me, I love Fordham.

I remember Al Sommer, not from his SEC Commissioner days of 1973 to 1976—I was a Long Island teenager back then, more focused on

the New York Knicks and their 1973 championship team—but as a young securities lawyer in the 1980s. I do remember seeing Al on various securities law panels at conferences, and I would read his writings from the SEC and from when he was at Morgan Lewis.

Al was a giant among securities lawyers. He was a forward thinker. In fact, the topic that I have chosen to address this evening is both a tribute to the forward thinking of Al and an important story that remains very much in progress. My address is entitled, “SEC—Don’t Throw Away Your Shot!” It is both a nod to the Broadway smash hit *Hamilton*—with which I admit I am a bit obsessed, having seen it now five times—but, more importantly, it is a renewed call for the SEC to create a uniform fiduciary standard to protect individual investors.

For those of you who have not yet seen the megahit *Hamilton*, here’s a very quick dose of the show honoring our founding father. At any rate, Al foretold the emergence and expansion of fiduciary duties in the securities industry, and that was nearly four decades ago in 1978 when he penned a law review article entitled, “Fiduciary Duties: The Search for Content.”<sup>1</sup> Al began that article with a celebrated quote from Justice Frankfurter that is as relevant today as it was back then:

To say that a man is a fiduciary only begins the analysis. It gives direction to further inquiry: To whom is he a fiduciary? What obligations does he owe as a fiduciary? In what respect has he failed to discharge those obligations? And what are the consequences of his deviation from the duty?<sup>2</sup>

This quote touches on a key concept in today’s fiduciary debate, i.e., while there are some fundamental and uniform elements of a fiduciary duty no matter the context, it is equally true that the manner in which fiduciary duty is applied in any specific context has elements of uniqueness that justify separate consideration.

As the General Counsel of SIFMA, I am reminded of this duality every day. Our members include broker-dealers, banks, and investment advisers, who recognize that they must act in their clients’ best interests every day or risk losing those very clients. There is, however, no one-size-fits-all best interest or fiduciary standard that now applies, or that could ever apply, to the diverse group of business models and functions that our members follow and perform. And yet, for many years now SIFMA has

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1. A. A. Sommer, Jr., *Fiduciary Duties—The Search for Content*, 9 LOY. U. CHI. L.J. 525 (1978).

2. *Id.* at 525.



been calling for the SEC to create a uniform fiduciary standard. How can that be? How did that come to pass? Or, as Lin-Manuel Miranda's *Hamilton* might have phrased it, "How does a broker, dealer, intensely regulated firm operate so smart yet debate whether he has his client's best interest at heart?"<sup>3</sup> I know, I know. This white, Jewish, middle-aged securities lawyer cannot rap at all—I get that.

Our story may not be quite as dramatic as *Hamilton*'s, but let me provide a roadmap of three key points that I would like you to take away from tonight's lecture. First, let us understand what problem a uniform fiduciary standard is intended to solve and where things stand today; second, let us present a solution to the problem of what is the optimal path forward; third and finally, let us consider how we can remove impediments to the solution, and here I will touch on why SIFMA is suing the Department of Labor ("DoL").

Let us start with the functions that investment advisers and brokers perform. The core function of an investment adviser is to provide continuous investment advice to its clients. Some also provide financial planning services and reports on securities. Brokers, on the other hand, operate across a far broader spectrum. While many brokers provide investment advice, others do not. Instead, they focus their business activities on clearing and settling trades, underwriting securities, or serving as market makers, for example.

Why is this important? Because the fiduciary debate focuses on the narrow overlap in services provided by brokers and advisers, i.e., when they each provide personalized investment advice to their retail clients. Yet, even when brokers and advisers engage in the same service, there are important differences between the kinds of investment advice they provide. Advisers, on the one hand, provide continuous and regular investment advice to their clients, which entails an ongoing duty to supervise the account regardless of whether any trading occurs. In contrast, brokers typically provide episodic investment advice incidental to a specific transaction and are compensated through commissions or similar transaction-based arrangements. Most retail investors, including retirement savers, choose brokerage accounts because they are buy-and-hold investors, and brokerage accounts are a more cost-effective choice.

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3. Ira D. Hammerman, PowerPoint Presentation for the Seventeenth Annual A. A. Sommer, Jr. Lecture on Corporate, Securities & Financial Law (Nov. 10, 2016) (on file with the Fordham Journal of Corporate and Financial Law).

Another key difference is that advisers generally exercise investment discretion over their client accounts, meaning that the adviser has the power granted by the client to trade on the client's behalf without even speaking with the client. Brokers, on the other hand, provide nondiscretionary advice. A broker generally cannot trade on his or her client's behalf; instead the broker makes an investment recommendation, and the client is free to take it or leave it. Of course, the biggest difference between brokers and advisers is the way they are regulated today under regulatory schemes that trace their roots back to the 1930s and 1940s with the passage of the federal statutes that govern brokers and advisers.

As this group well knows, the Investment Advisers Act of 1940 (“Advisers Act”)<sup>4</sup> does not expressly mandate a fiduciary duty, but one was read into the Act by the famous 1963 Supreme Court case in *Capital Gains*.<sup>5</sup> In that case, the court held that Section 206 of the Advisers Act imposes fiduciary duties on advisers by operation of law.<sup>6</sup> Brokers, on the other hand, are governed by the Securities Exchange Act of 1934 (“Exchange Act”),<sup>7</sup> which recognizes that a broker who provides personalized investment advice and recommendations to retail clients is generally not a fiduciary but owes a duty of fair dealing to her clients.

Why then, you may ask, when brokers engage in the same conduct as advisers—namely, providing investment advice—do they not need to comply with the presumptively higher fiduciary standard under the Advisers Act?<sup>8</sup> The answer lies in the broker-dealer exclusion. In passing the Advisers Act, Congress saw fit to provide an exclusion for the episodic nondiscretionary advice that brokers typically provide to their clients.<sup>9</sup> Thus, under the Advisers Act, brokers are excluded from the definition of adviser where the advice they provide is solely incidental to their brokerage business and when they receive no special compensation for the advice.<sup>10</sup> The broker-dealer exclusion reflects Congress' clear understanding that there is a natural interrelationship between brokerage services and providing investment advice and that brokers are already comprehensively regulated under the Exchange Act.<sup>11</sup>

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4. Investment Advisers Act of 1940, 15 U.S.C. §§ 80b-1 to 80b-21 (2012).

5. SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180 (1963).

6. *Id.* at 184-85.

7. Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78kk.

8. 15 U.S.C. §§ 80b-1 to 80b-21.

9. 15 U.S.C. § 80b-2.

10. *See id.*

11. *See generally* 15 U.S.C. §§ 78a-78kk.

Indeed, over the intervening eight-plus decades, the SEC, the Financial Industry Regulatory Authority (“FINRA”), and the state securities regulators who oversee brokers have developed a fulsome regulatory regime based on a broker’s duty of fair dealing, including the obligation to make suitable recommendations; achieve best execution; observe high standards of commercial honor, and just and equitable principles of trade, a concept which itself embodies fiduciary principles.

Brokers, as you know, are also subject to routine and regular exams from the SEC and FINRA, as opposed to visits by the SEC only once every eleven years or so for the adviser community. Thus, brokers and advisers currently operate under high, although somewhat different, standards of conduct that have developed under separate statutory and regulatory schemes over many decades.

So far, so good. So, what happened; what changed? The short answer is that the brokerage community changed. It was once as simple as this:

Commissions = Broker  
No Fiduciary  


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Assets under mgmt = RIA  
Yes Fiduciary

Figure 1<sup>12</sup>

But in the late 1980s and early 1990s, brokerage firms first started to introduce new types of full-service accounts—known as fee-based accounts—that emphasized the importance of the investment advice they provided and that changed their compensation structure to a fee-based model, just like investment advisers.

A few years later, in May 1994, then-SEC Chair Arthur Levitt—the inaugural Sommer lecturer in 2000—formed a broad-based committee led by Dan Tully, then the Chairman and CEO of Merrill Lynch, to recommend best practices for managing conflicts of interest in the brokerage industry. In April of 1995, the Tully Report identified as a best practice that brokers should be compensated using asset-based fees

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12. Hammerman, *supra* note 3.

instead of commissions.<sup>13</sup> The thinking was that commissions created an incentive for brokers to trade frequently, or “churn” the account, and that often the best advice a broker can give a client is to do nothing. The Tully Report viewed fee-based brokerage as a means to better align the interests of brokers and their clients.<sup>14</sup> The Tully Report encouraged fee-based brokerage accounts to proliferate.<sup>15</sup> As they did, concerns arose among brokers and regulators that this form of compensation could be viewed as “special compensation,” thereby invoking the Advisers Act.<sup>16</sup>

In 1999, the SEC stepped in and proposed a rule that would exempt brokers offering fee-based brokerage accounts from being deemed investment advisers if they satisfied certain conditions. The proposed rule is very controversial. Independent advisers represented by the Financial Planning Association (“FPA”) did not like the heightened and more direct competition from brokers that the proposed rule would allow. Regardless, the SEC adopted the rule in April of 2005.<sup>17</sup> But shortly thereafter, the FPA sued the SEC to invalidate the rule, and in 2007 the D.C. Circuit Court did just that, ruling that the SEC had exceeded its authority when it adopted the rule.<sup>18</sup>

The D.C. Circuit decision caused the SEC to reconsider the distinction between brokers and advisers, and so in 2008 it commissioned a study from the RAND Corporation,<sup>19</sup> which found that while investors were generally happy with the service provided by their broker or adviser, these investors generally did not understand, or were even confused by, the differences between the duties owed by brokers and advisers under securities laws.<sup>20</sup>

Throughout the following year, in 2009, numerous members of Congress and senior officials at the SEC and FINRA expressed their desire and intent to harmonize the regulatory regime for brokers and advisers. At that time, there was widespread acceptance that the harmonized standard should be a fiduciary one, under the belief that it

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13. DANIEL P. TULLY ET AL., SEC. & EXCH. COMM’N, REPORT OF THE COMMITTEE ON COMPENSATION PRACTICES 1 (1995).

14. *Id.* at 7, 10.

15. *See id.*

16. *See* 15 U.S.C. § 80b-2(a)(11).

17. 17 C.F.R. § 275.202 (2016).

18. *Fin. Planning Ass’n v. SEC*, 482 F.3d 481 (D.C. Cir. 2007).

19. ANGELA A. HUNG ET AL., RAND CORP., INVESTOR AND INDUSTRY PERSPECTIVES ON INVESTMENT ADVISERS AND BROKER-DEALERS (2017), [https://www.sec.gov/news/press/2008/2008-1\\_randiabdreport.pdf](https://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf) [<https://perma.cc/SDU2-63KT>].

20. *Id.* at 118.

represents the highest standard and that investors deserve no less. SIFMA and its members were keenly aware that change was in the air. We wanted to be part of the conversation and, more importantly, part of a positive and constructive solution. Particularly in the wake of the financial crisis, we wanted to make very clear and public that our industry firmly supports consistent and high standards for interacting with individual clients, including putting the clients' best interests first.

Thus, in July of 2009, SIFMA's Private Client Group convened and, in an act of leadership, passed a one-page resolution declaring SIFMA's support for a fiduciary standard. Here you see the resolution:

ACTION ITEM¶

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Presented at: → Private Client Group Steering Committee, July 15, 2009¶

Presented by: → John Taft, Chairman, Private Client Group Steering Committee¶

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¶  
**Whereas,** the SIFMA Private Client Group is closely aligned with services to individual investors,¶  
 ¶  
**Whereas,** the Private Client Group Steering Committee has actively discussed and debated the topic of harmonized standards applicable to providers of investment services to individual investors,¶  
 ¶  
**Whereas,** the Private Client Group Steering Committee understands, appreciates, and supports the likely regulatory shift underway to have similar services provided by broker-dealers and investment advisers regulated in a similar fashion,¶  
 ¶  
**Whereas,** the Private Client Group Steering Committee continues to embrace high standards for interacting with its individual clients, including putting the client's interest first,¶  
 ¶  
**Whereas,** the Private Client Group Steering Committee believes that clients should have the option to receive the integrated services they want, and pay as they choose, with their consent to conflicts of interest related to the integrated services,¶  
 ¶  
**Whereas,** the Private Client Group Steering Committee understands that client choice must be fully considered and preserved in any harmonization of standards,¶  
 ¶  
**Therefore, it is resolved,** that the Private Client Group Steering Committee embrace the creation of a new federal securities fiduciary standard of care, to be promulgated by the SEC, for all financial services professionals providing personalized investment advice to individual clients.¶  
 ¶  
**Therefore, it is further resolved,** that a new federal securities fiduciary standard of care, to be promulgated by the SEC, should: 1) not subject financial professionals to obligations under other federal or state laws; 2) provide adequate flexibility to preserve and enhance client choice, product and service innovation, and capital formation; 3) provide for conflict management; 4) apply only to, and be tailored for, those services and activities involving personalized advice to individual clients.¶

Figure 2<sup>21</sup>

In fact, my colleague Kevin Carroll, who is here with us tonight, was a key draftsperson of that. Kevin has been with me for nearly ten years as we continue to debate and discuss the fiduciary rule. One year later, on

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21. Hammerman, *supra* note 3.

July 15, 2010, Congress passed the Dodd-Frank Act.<sup>22</sup> With respect to fiduciaries, Section 913 of the Dodd-Frank Act authorizes the SEC to write rules to implement a new uniform fiduciary standard of conduct applicable to both brokers and advisers when they provide personalized investment advice about securities to retail clients.<sup>23</sup> Section 913 requires the uniform fiduciary standard to be no less stringent than the general fiduciary implied under Section 206 of the Advisers Act.<sup>24</sup> The SEC has no deadline to act, and—as we are all painfully aware, more than six years later—is not required to take any action at all.

What is SIFMA asking the SEC to do with its Dodd-Frank Section 913 authority? We want the SEC to do precisely what Congress intended and what Section 913 requires—namely, to articulate the fiduciary duty implied under Section 206 of the Advisers Act through new rule-making for brokers under the Exchange Act.<sup>25</sup> The SEC should issue the necessary rules and guidance to enable brokers to apply the standard to their distinct operational model.<sup>26</sup> The plain language of Section 913 together with the legislative history of Dodd-Frank makes clear that the requirement that the uniform fiduciary standard be no less stringent than the general fiduciary duty implied under Section 206 does not require the SEC to impose Advisers Act rules, guidance, and legal precedence on broker-dealers.<sup>27</sup>

Do not take our word for it. Congressman Barney Frank, then a primary author of the Dodd-Frank Act, said so explicitly in a letter to the SEC Chair, Mary Schapiro, back in 2011.<sup>28</sup> So, what is the problem with extending the Advisers Act guidance and precedent to brokers? The problem is that such guidance and precedent is based upon the specific type of services provided and disclosures made by investment advisers and, thus, it is inherently not directly applicable to broker-dealers.<sup>29</sup>

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22. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (codified as amended in scattered sections of 7, 12, and 15 U.S.C.).

23. 15 U.S.C. § 78o(k) (2012).

24. *Id.*

25. Memorandum from Ira D. Hammerman to Mary L. Schapiro, Chairwoman, Sec. & Exch. Comm'n (July 14, 2011) (on file with SIFMA).

26. *Id.*

27. *Id.*

28. Memorandum from Barney Frank to Mary L. Schapiro, Chairwoman, Sec. & Exch. Comm'n (Sept. 28, 2011) (on file with author).

29. Memorandum from Ira D. Hammerman, *supra* note 25.

This is a critically important point, and it is the same point that Al Sommer wrote about nearly four decades ago—namely, that establishing an intermediary, a fiduciary who is required to act in the best interests of the investor is only the beginning of the analysis, not the end.<sup>30</sup> Because of fundamental differences between brokers' and advisers' roles and business models, attempting to apply the Advisers Act guidance and precedent to brokers without further clarification by the SEC would create a high risk of confusion and misapplication, resulting in unnecessary legal and compliance costs under the new standard.<sup>31</sup> At a minimum, SEC rules and guidance should adequately address a wide range of common scenarios that brokers face in their daily dealings with clients.<sup>32</sup>

As we have limited time this evening, allow me to articulate just one scenario that is very common today and that the SEC would need to address in clear guidance at the time any uniform fiduciary standard of care would be formally adopted. This slide is called “The Holistic Review of a Client Relationship”:

#### Holistic Review of “Client Relationship”

- **Transaction:** As a result of several months of market volatility, Lucy and Jon ask their broker to meet with them to provide a review of the overall performance of all of the family's accounts held at the firm. The broker responds and provides the Smiths with a review of the fee-based as well as other accounts including transactional brokerage and self-directed accounts.

Figure 3<sup>33</sup>

This is very common. Because of several months of market volatility, Lucy and John Smith ask their broker to meet with them to provide a review of the overall performance of all five of the family's accounts held at the firm. The broker responds and provides the Smiths with a review of the fee-based discretionary account as well as the transactional brokerage account, a self-directed account, an IRA, and the 529 college plan accounts. We need SEC guidance to address the following: if the broker chooses to provide the Smiths with a holistic review, including the no-advice brokerage and the self-directed accounts, which are not subject to

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30. See *supra* note 2 and accompanying text.

31. Memorandum from Ira D. Hammerman, *supra* note 25.

32. *Id.*

33. Hammerman, *supra* note 3.

a fiduciary duty, would the broker potentially create a new fiduciary obligation for the no-advice accounts by simply doing the right thing and meeting with the client to discuss all of the accounts?

Even though there are many unanswered questions, SIFMA has laid the foundation, provided the data, and presented a compelling case for the SEC to exercise its Section 913 authority over these past seven years.<sup>34</sup> Many of the prior comment letters and testimony that we have provided are on the SIFMA website. We have a statute that authorizes it, an industry that wants it, and two consecutive SEC chairs who say it is a top priority. So, why do we not have a uniform fiduciary standard today?

At this moment, I hope we can achieve a moment of clarity, leadership, and forward thinking. My hope is that the SEC and its leaders take a cue from the *Hamilton* cast, performing eight shows a week a few blocks from here, and do not “throw away their shot.”<sup>35</sup> At the risk of continuing my homage to *Hamilton*, I am reminded of the famous line that Hamilton raps when speaking of his friend, rival, nemesis, and ultimate dueling partner, Aaron Burr: “If you stand for nothing, Burr, what will you fall for?”<sup>36</sup>

To our colleagues at the Commission, be they the current occupants of the tenth floor or the next crew to be nominated by President-Elect Trump, I sincerely hope you can take a stand and produce some tangible action on this important investor protection issue. In the meantime, what else can SIFMA do to further pave the way for an eventual uniform fiduciary standard from the SEC? I am glad you asked. That is what our legal challenge to the DoL fiduciary rule is intended to do.

As should be crystal clear now, our pending lawsuit with the DoL is not a fight against a fiduciary standard; rather, our lawsuit is necessary because of the botched way the DoL is attempting to achieve its goal. The DoL has, unfortunately, injected itself into the fiduciary debate covered by Dodd-Frank and created a rule that applies to just one sliver of

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34. Memorandum from Kevin M. Carroll to Brent J. Fields, Sec’y, Sec. & Exch. Comm’n (Aug. 8, 2016) (on file with SIFMA).

35. See *Lin-Manuel Miranda—My Shot Lyrics*, MUSIXMATCH (last updated Jan. 22, 2017), <https://www.musixmatch.com/lyrics/Lin-Manuel-Miranda/My-Shot> [<https://perma.cc/9ANB-BFBZ>].

36. *Lin-Manuel Miranda—Aaron Burr, Sir (Off-Broadway) Lyrics*, GENIUS, <https://genius.com/Lin-manuel-miranda-aaron-burr-sir-off-broadway-lyrics> [<https://perma.cc/EVE9-BERD>].



investment advice in the only space it has jurisdiction, and that is certain retirement accounts.<sup>37</sup>

The DoL rule creates a confusing, bifurcated system for both financial advisers and their clients, and it stands in direct conflict with the uniform fiduciary standard contemplated under Dodd-Frank. Moreover, the DoL rule will be extremely costly and will limit Americans' access to retirement-planning advice.<sup>38</sup> Some clients, particularly small accounts, may become too expensive to service and will likely get dropped. Others will likely be forced into asset-based accounts, where they will pay more for their advice.

So, DoL got it wrong. But does that mean it violated the law? In this case, yes. Our lawsuit details several violations and causes of action.<sup>39</sup> I will just quickly highlight two. First, the DoL exceeded its statutory authority in promulgating this rule. The rule over-broadly redefines who is a fiduciary, and in doing so it sweeps in every person who sells a retirement-related product and then prohibits them from receiving commissions that have been a mainstay of their business model for decades.<sup>40</sup> The DoL rule improperly intrudes upon the jurisdiction of the SEC, which was directed by Congress to create a uniform fiduciary standard.<sup>41</sup> The SEC's jurisdiction applies to all investment advice, whereas DoL is limited to only retirement accounts.<sup>42</sup> The SEC has extensive enforcement and exam authority; the DoL, however, has no enforcement or exam authority over individual retirement accounts. The DoL rule is like the tail wagging the dog. The DoL must yield to the SEC in this already claimed space.

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37. Definition of the Term "Fiduciary"; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. 20,946 (Apr. 8, 2016) (to be codified at 29 C.F.R. pt. 2509, 2510, 2550).

38. *See id.*

39. Carol Danko, *Lawsuit Filed to Challenge New Department of Labor Rule That Prevents Financial Professionals from Best Serving Retirement Savers*, SIFMA (June 2, 2016), <http://www.sifma.org/newsroom/2016/lawsuit-filed-to-challenge-new-department-of-labor-rule-that-prevents-financial-professionals-from-best-serving-retirement-savers/> [<https://perma.cc/2KZX-EQZK>].

40. Definition of the Term "Fiduciary"; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. at 20,946.

41. SEC. & EXCH. COMM'N, STUDY ON INVESTMENT ADVISERS AND BROKER-DEALERS (2011), <https://www.sec.gov/news/studies/2011/913studyfinal.pdf> [<https://perma.cc/C645-N949>].

42. *Id.*

Second, and perhaps most importantly, our lawsuit takes issue with the rule's Best Interest Contract Exemption ("BICE"), which essentially forces firms to enter into legally binding contracts with clients in order to continue doing business on the same terms and to subject themselves to class-action lawsuits from the plaintiffs' bar that the DoL has no authority to impose.<sup>43</sup> The DoL thus abused its exemptive authority by forcing financial professionals to rely on BICE and then conditioning that exemption on their agreement to requirements and liabilities that the DoL has no power to impose or enforce. Precisely because the DoL has no enforcement authority in this area, it has delegated enforcement to private litigants.

It is truly an unprecedented, exploitative, and improper action by a federal agency. This is why we have taken legal action to stop the rule. We are hopeful that the courts will see how the DoL exceeded its authority and created a rule so complex and so costly that it will make receiving and giving financial advice more expensive for hardworking Americans saving for retirement.<sup>44</sup>

That brings me to my conclusion. I hope each of you will take away a better understanding of the origins of the call for a uniform best interest standard, SIFMA's views on how to implement it, the urgency of our call to do so now, and finally, why we were compelled to litigate with DoL to maintain the promise of a uniform fiduciary standard.

The future remains as uncertain as ever. Our DoL case goes to a hearing next week, and the SEC's direction under its Dodd-Frank authority remains murky. Who knows? Maybe seventeen years from now, the thirty-fourth Annual Sommer Lecture in 2033, when we have all converted to the fee-based advisory model, will lament the death of and call for the return of the commission-based brokerage account, while we all scratch our heads wondering, "How did we get into this mess?" Stranger things could happen. Stay tuned. This saga has many chapters still to go.

For my final *Hamilton* reference, whenever the fiduciary debate gets sorted out, all I know is "I wanna [sic] be in the room where it happens."<sup>45</sup> Thank you for listening and, again, thank you for the honor.

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43. Best Interest Contract Exemption, 81 Fed. Reg. 21,002 (Apr. 8, 2016) (to be codified at 29 C.F.R. pt. 2550).

44. Danko, *supra* note 39.

45. *The Room Where It Happens Lyrics—Lin-Manuel Miranda*, GENIUS, <https://genius.com/Lin-manuel-miranda-the-room-where-it-happens-lyrics> [<https://perma.cc/62AU-YBEZ>].

DEAN DILLER: Ira has agreed to take some questions and comments.

AUDIENCE MEMBER: Thank you. You are giving your speech at an interesting time. Should the SEC move ahead with a uniform standard now requiring broker-dealers to honor the best interests of their clients?

IRA D. HAMMERMAN: One of the themes in my talk was that we do think the SEC is the proper agency to move forward. To answer your question about doing it now, there are many complexities to them acting now.

AUDIENCE MEMBER: If I could push that, I do not expect them to act this week, but suppose that the new administration proposed that Dodd-Frank be repealed in whole; would you favor the SEC retaining its authority to adopt a uniform fiduciary standard?

IRA D. HAMMERMAN: I guess we will all have to wait and see about the first part of your question. I personally would be surprised if now President-Elect Trump, who is no longer campaigning for office, will still be pushing for the repeal of Dodd-Frank, which I think was the premise of your question. I do not think we will end up going down that path. But whether we do or not, the answer to the second part of your question is that the SEC is the expert agency; it is the right agency to deal with this issue. Whether or not this issue remains in Dodd-Frank, I believe we would still be in favor of the SEC being the proper agency to wrestle with this very complicated issue and topic.

AUDIENCE MEMBER: What is your sense of why the SEC has not acted? There were all kinds of opportunities obviously before the DoL started to move. When it became apparent the DoL was starting to move, there was even a greater incentive, and I think an encouragement, on many people's parts to get the SEC to move, and yet it seems not to have gotten off the ground. Notwithstanding all the other things it had to do, why let the issue get processed by DoL?

IRA D. HAMMERMAN: Great question. We have been asking that same question for six-plus years now. We have heard everything, including "it's complicated"—but life is complicated. We still have enough support and belief that the SEC could figure it out. So, yes, it is complicated; yes, Congress may not have given them the most artful language in Section 913 to resolve the best interests of the client with preserving a commission-based model.<sup>46</sup> We totally respect and understand that it is a complicated issue, but we are also a bit disappointed

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46. See generally 15 U.S.C. § 78o (2012).

that now, six and seven years on, they really have not moved the ball forward, at least publicly. We would hear lots of discussion internally that investment management and trading and markets were working together on it, but we certainly have not seen anything. Hopefully, new day, new administration, that can change.

AUDIENCE MEMBER: This may be the other side of the same question, which is: do you have any sense as to what prompted the DoL to step into this, the SEC not having acted?

IRA D. HAMMERMAN: My only observation—and you and your colleagues have seen a lot over the years as well—is that this was politically motivated rule-making from day one. In my career, I do not remember a sitting president having a press conference over a proposal that some agency was thinking about, and this was just very politically charged from the get go. It is like it was preordained in terms of what the DoL would do here. It has been disappointing that the SEC has not taken the lead. I am a “glass half-full” kind of guy, so I am hoping now—we are going to have a change in administrations, there will be new folks leading the SEC, and who knows what happens on the DoL side of the equation? There will be a new Secretary of Labor. President-Elect Trump will have many things to work through, and hopefully the DoL piece is on that list as well.

AUDIENCE MEMBER: I was curious what you thought was a bigger inspiration for the SEC to act now: that potentially other agencies like the DoL would be intruding on its space to govern, or if it was because individual investors were being harmed by not having this uniform fiduciary standard?

IRA D. HAMMERMAN: As I tried to address in the talk, the securities business is an intensely and heavily regulated industry—at the federal level, state level, and also by the self-regulatory organizations. We can certainly debate that if you are a broker-dealer or an investment adviser, at the federal level you are heavily regulated.

The challenge has been—as in many things in life—business goes faster than regulation. So, the business over the last twenty and thirty years has converged—the broker-dealer model, the investment adviser model; everyone is in the advice business now. That is what customers need, want, and are willing to pay for. But we want to preserve the customer experience and the customers’ choices over how they pay for their services. Some people want commissions—they do not trade all that much. Others need a lot more hand holding and constant monitoring of their accounts, and maybe asset-based pricing works for them. But, regardless of which side of the fence you are on, brokers or advisers, what

we think at SIFMA is, the time has come to now have that same uniform fiduciary standard of care so when the customer is receiving advice they should know that standard is the same.

AUDIENCE MEMBER: Our system of securities laws does have different tiers of protection for investors of different levels of sophistication. So why is it that there could not be this unified standard and then the additional standard set forth by the DoL when it comes to retirement accounts where, in many cases, we are dealing with the least sophisticated investors?

IRA D. HAMMERMAN: The challenge is if you are in the financial services industry today, you have many different regulators, and if you are going to have the DoL with its standard of care and the SEC with multiple standards of care—because you have the fiduciary standard if you are under the Advisers Act, you have the suitability standard if you are a broker-dealer—firms, particularly the larger firms with 10,000, 15,000 financial advisers and millions of households as customers, need to come up with a system that is going to work so that they can educate their employees. To have one agency that is not as much of an expert in the securities market and securities laws dictate how an IRA account should be held, as I say in the talk, is the tail wagging the dog.

At many of the brokerage firms, the largest percentage of retail customer securities are in the IRA account—that is kind of the bread-and-butter business of the financial services industry—and many of those customers are buy-and-hold investors who are comfortable paying a commission when they buy a security and know that they are going to hold Apple, just to use an example, for ten years and twenty years. So, they pay once, and it is in their account. That is a choice that they like, and we want to preserve their ability.

For the DoL—again, not an expert in what is going on in terms of the securities markets—to come up and say, “You know what? We do not like commissions, and we are going to make it very, very difficult to do a commission business” kind of forces people into asset-based pricing, and that is taking away choice from the customers.

To really simplify it, the DoL is saying, “Index funds—good; active funds—bad,” and they are saying, “Fee-based accounts—good; commissions—bad.” What we are saying on behalf of our members is, “Customers want choice.” The industry has longstanding relationships with its customers, and it knows what its customers want; it is in a service business, and it wants to preserve choice for its customers.

DEAN DILLER: Well, thank you for making a complex subject so clear that even I can understand it, and thank you for your thoughtful remarks.

IRA D. HAMMERMAN: Thank you.