The Transition of Consumer Financial Protection Regulations: The Anticipated Impact of the 2016 U.S. Department of Labor Fiduciary Rule on Low and Middle Income Consumer Financial Well-Being

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Abstract

The aging of the population in the United States means that during the next 20 years, about 80 million more people will be experiencing the impact of important financial decisions they previously made about when and how they would retire. Yet according to the US Department of Labor (DOL), some of the advisors, brokers or "financial planners" responsible for guiding these people towards quality investment decisions, "actually profit from backdoor payments and hidden fees to the detriment of their clients."

Research shows that advisors that do not work in the best interest of their clients, are responsible for these effected Americans buying into bad retirement investments that result in annual losses of about $17-$20 billion per year and of particular concern is the impact on the lower or middle income individuals. A recent DOL regulatory impact analysis estimates that middle and working class families with IRAs would save more than $40 billion over ten years when new fiduciary rules and exemptions are fully implemented.

The final DOL fiduciary rule in 2016 stated that in most situations, financial planning activity involved providing advice and as such, required that all advisors and brokers be governed under a fiduciary level duty of care. A common reaction from the effected advisors in the financial services community was that the DOL fiduciary rule would hurt the very people it was intended to help, the lower and middle income (LMI) clients, because advisors could no longer financially justify providing investment advisory services for these people. This policy paper disputes that position.

Introduction

While in the past there had been some attention drawn to the issue of the various relationships that existed between clients and their financial advisors, it was the Dodd-Frank Wall Street Reform and Consumer Protection act of 2010, and the initial 2010 DOL proposed fiduciary rule that raised the attention level and led to a more thorough examination and evaluation of the role of advisors in the financial services industry.

Dodd-Frank, which had the momentum of being created as a result of the 2008 general financial meltdown, had the authority of law under Section 919C to dictate that the General Accounting Office (GAO 2011) conduct a study to research if "financial planners" needed additional oversight and regulation relating to their titles and their advisory roles with consumers.

While the DOL's 2010 proposed fiduciary rule had zeroed in on the theory that regardless of title, financial advisors that provided advice must adopt and abide by fiduciary level duties of care, it was retracted in 2011 because of cumbersome transitional issues that would ultimately be addressed in a future DOL fiduciary rule proposal.

In 2010, research showed that there were different categories of financial planners being governed under various federal and state laws, operating under varying standards of care. According to the GAO report (2011) "conflicts of interest were a concern" as was the fact that numerous titles and designations financial planners were using were creating undue confusion among consumers.

The GAO report (2011) voiced concerns regarding the fact that while some financial planners operated under an advisor "fiduciary" standard of trust, other transactional orientated financial planners may have had "an inherent conflict of interest in recommending products they ultimately stood to benefit from selling."

The end result of this lengthy study by GOA (2011) was a recommendation to the Securities and Exchange Commission (SEC) in collaboration with the states, to conduct further research on the subject, but that was met with little enthusiasm and the issue of whether “financial planners” should be specifically regulated as a distinct profession, lost much of its traction.

What the GAO (2011) study did accomplish was to add considerable clarification about the regulatory environment at the time and that the *activity* of advisors should be the primary focus of regulatory attention and not titles or designations. As such, the issue of activities became the focal point, as was initially suggested by the DOL proposed rule in 2010.

The DOL issued their next proposed fiduciary rule in 2015 which addressed the types of advice that qualify as fiduciary in nature, carved out certain categories of investment advice that were no longer subject to the rule, and amended several existing exemptions from the classes of prohibited transactions.

What that accomplished was to address many of the transitional issues associated with the original 2010 proposal that were learned from considerable stakeholder input and made the transition from the prevailing duties of care, to a fiduciary level duty of care, considerably more palatable to the financial services community.

After additional and considerable stakeholder input was addressed, subsequent to the issuance of the 2015 fiduciary rule, the DOL issued its final proposed fiduciary rule in April 2016 which:

- Clarified specifically what does and does not constitute fiduciary advice;
- Will allow firms to accept common types of compensation – i.e. commissions and revenue sharing payments involving more types of advice;
- Streamlined exemptions, contract requirements and time frames of contracts;

- Minimized contractual parties;
- Streamlined required disclosures and provided considerable grandfathering and;
- Extended the implementation time period.

According to Rick Meigs (2016) the final fiduciary rule "streamlined and simplified the rule to minimize the compliance burden and ensure ongoing access to advice, while maintaining an enforceable best interest standard that protects savers."

While the final rule, which is certainly a positive step forward for financial consumers as well as professionals, many in the financial services community still feel that it would hurt low and middle income (LMI) individuals by limiting their access to financial advisors.

Since this author feels that the 2016 fiduciary rule is fair and reasonable for all stakeholders and that it is the LMI clients in particular that need objective advice from advisors that is *always* in *their* best interest, the purpose of this policy paper is to answer two questions:

- Will the 2016 DOL fiduciary rule change the behavior of financial advisors as it regards their *type* of clients?
- Will the 2016 DOL fiduciary rule be detrimental to the ability of LMI individuals to *access* quality investment advisors?

Significant findings of this study are:

(1) There is no evidence that advisors and broker-dealers providing investment advice will be negatively affected by the introduction of the 2016 DOL fiduciary rule.

(2) Imposition of the 2016 DOL fiduciary standard of care among financial advisers and brokers may result in a "net welfare gain to society" (Finke and Langdon, 2012) and in

particular, a gain to the LMI consumers who are ill-equipped to make complex financial decisions.

As such, the null hypothesis of this policy paper is:

> All else being equal, requiring that all investment advisors and brokers be governed under the Department of Labor 2016 fiduciary rule will not impact low and mid-income individual's (LMI) access to qualified investment advisors

The conclusion based on the research in this study of the DOL 2016 fiduciary rule is that we *do not reject* the null hypothesis. This paper proceeds to the Literature Review, Methods, Results and Conclusion sections and concludes with References.

Literature Review

A primary focus of this policy paper regards the economic and consumer protection issues associated with fiduciary investment advice and the duty of care being provided by different segments of the advisor, broker-dealer and agent community and whether regulations are adequate to assure that the best interest of the various types of clients are being protected.

According to Benjamin Cummings and Michael Finke (2010) the “inability to accurately detect quality prior to or even after purchase distinguishes professional advice from other consumer goods or services.” One premise was that a consumer that is unable to assess the difference between an advisor's recommendation and the ideal recommendation is “vulnerable to the self-serving behavior”.

Consumers will pay the price for financial advice when they feel the advisor knows more than they do, but common sense dictates that the advice must provide more net value than the cost. Cummings and Finke (2010) believe that without an “informational imbalance” between the client and advisor, there is “no reason to pay the cost of expert advice and that in the current environment, the information imbalance will not produce the optimal efficient market outcome without *additional and adequate regulation*.”

Common sense also dictates that if a client engages a financial advisor or broker who is held to a fiduciary standard of care and, because of a high level of professional integrity, makes recommendations that maximize the well-being and welfare of the client, the outcome will ultimately be in the best interest of the client.

On the other hand, if an investor retains an agent who is held to a lower standard of care and is more concerned with their own self-interest over the clients, the outcome will typically be less then optimal, at least from the client’s perspective and point of view.

In 2010, the DOL initially proposed a fiduciary rule broadening the definition of "fiduciary" to include "*any person* who provides investment advice to employee retirement plans and plan participants for a fee or other compensation." This included individuals who might give advice on a less than regular or full time basis.

The DOL received considerable comment regarding the fiduciary definition because it would expand legal liability of service providers and fiduciary plan sponsors, as well as "increase plan cost which, theoretically, would be ultimately trickle down to plan participants" (Frankel, 2011). As a result, in September 2011, the DOL announced they would re-propose its fiduciary rule definition sometime in 2013.

During a similar time frame, and as a result of the "financial meltdown" in the United States during 2008-2009, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 was passed to address various financial issues, not the least of which involved the specific issue of financial planning and the need for additional clarification as to the standards of care required of the professional "financial planner" community.

The Dodd-Frank Act addressed issues specifically relating to standards of care of brokers, dealers and advisers and to consider "the elimination of the broker exclusion from the Advisors Act of 1940 and the impact of imposing the duties of the Advisors Act on brokers" (Frankel, 2011).

Within Section 919C the Dodd-Frank Act (2010) was a directive to the Government Accountability Office (GAO) which mandated that the GAO specifically study the oversight of "financial planners" because there was some concern that as a result of the anticipated surge of individuals soon reaching retirement age, there would be a greater need for assistance with investments, insurance products, and general financial planning expertise. According to the

Bureau of Labor Statistics (2010), forty million additional workers are expected to retire by 2020.

The GAO report (2011) specifically addressed how consumers were being assisted by financial planners as it pertained to financial issues involving investments, insurance and overall financial planning and if additional protection was needed from a legal or regulatory perspective to assure a high level of consumer financial well-being.

Dodd-Frank mandated a detailed examination of "how financial planners were regulated and overseen at the federal and state levels, what was known about the effectiveness of these regulations, and the advantages and disadvantages of any alternative regulatory approaches" (GAO 2011).

Within the GAO report, there was considerable emphasis regarding the typical financial planning *activities* involved, versus the *titles or designations* in play, and what would be the most appropriate criteria to use when deciding when an individual is obligated to work in the best interest of the client, as opposed to when a lesser standard would be appropriate. This was also a primary focus of DOL preliminary rule proposal issued in 2010.

The GAO conducted their performance audit from June 2010 to January 2011 and one of the primary observations was that "there was actually no specific, direct regulation of 'financial planners' per se" and in fact, financial planning was an *activity* provided by various financial planning professionals. As a result of these observations, the GAO report (2011) suggested future attention should be more focused "on financial planning activities and *not* titles."

The following chart provides an overview of the pertinent governing laws (2011), services coverage by regulations and services covered according to standards of care.

Capacity	Investment Adviser	Broker-Dealer	Insurance Agent
Applicable federal and state laws	Federal: •Investment Advisers Act of 1940 and rules from SEC State: •State Securities Laws	Federal: •Securities and Exchange Act of 1934 and rules of SEC and FINRA State •State securities laws	State: •State insurance laws
Financial planning service covered by regulation	•Advice about securities, including advice given in conjunction with product recommendations and advice about non-securities	•Recommendations for specific securities products •Purchase or sale of securities products •Sale of variable insurance (annuities, life insurance)	•Recommendations for insurance products •Sale of insurance products •Sale of variable insurance (annuities, life insurance)
Standard of care	FIDUCIARY •Person has an affirmative duty to render services solely in the best interests of clients •Requires advisers to disclose material conflicts of interest to clients	SUITABILITY •Rules require standard of care that includes, among other things, rendering investment recommendations that are suitable for customers	VARIES BY PRODUCT AND BY STATE INSURANCE LAW •Requires insurance agents to follow suitability standards, when state has adopted such standards for products
Financial planning service covered by standard of care	•Advice about securities, including advice given in conjunction with product recommendations and advice about non-securities	•Recommendations for the purchase or sale of specific securities products •Recommendations for the purchase of variable insurance	•Recommendations for the purchase of insurance products •Recommendations for the purchase of variable insurance

Source: GAO

While the previous overview provides a detailed visual of the regulations and the degree of overlap and regulatory complexity involved, the more pertinent issue to this policy paper is related to the standards of care.

That this issue also appears to be the primary observation of the GAO report in 2011 and continues to be the Department of Labor's primary area of regulatory focus and intended consumer impact, only adds credibility to this discussion.

From a definitional perspective, under a "*fiduciary standard*" of care, the advisor must simply act in their client's best interest, ensure that recommended investments are appropriate for the client, and disclose to the client any material conflicts of interest.

Under a *"suitability standard"* of care, broker-dealers operate under a lesser standard of care which only requires that the broker-dealer recommend securities that they reasonably believe are in the best interest of the client. In that regard and according to FINRA (2010) and the GAO (2011), financial planners functioning as broker-dealers "may recommend a product that provides them with a higher commission than a similar product without triggering a conflict of interest."

The lowest standard of care is reserved for the insurance agents who typically earn a commission on products sold. There are *no requirements* that a product recommendation be suitable and in the best interest of the client.

As can be anticipated by reviewing these standards of care, consumer confusion is common and according to a Financial Planning Association report (2007) "it would be difficult, if not impossible, for an individual investor to discern when the adviser was acting in a fiduciary capacity or in a non-fiduciary capacity."

According to a Securities and Exchange Commission (SEC) study conducted by the RAND Corporation (2008), "consumers generally did not understand not only the distinction between a suitability and fiduciary standard of care, but also the differences between broker-dealers and investment advisers." That study also concluded that even experienced, sophisticated investors were confused about the various titles used by investment advisers and broker-dealers.

But according to various financial services firms, they believe their clients are sufficiently informed about the differing roles and standards of care and that their communications are adequate to *educate* the consumer. Some firms stated further that, if necessary, they provide “different agreements for different standard of care activities”. This approach would most likely not make the consumer experience any easier.

Much of the literature also appears to suggest that consumers *are not* the stakeholders that should be educated and that it is the financial professionals that should be further *regulated* and held to a consistently higher duty of care. One of the more relevant suggestions coming from the GAO (2011) report was “to extend coverage of the fiduciary standard of care to *all* those who provide financial planning advisory services.”

At the time of the GAO report (2011) when both the Nation Association of Insurance Commissioners (NAIC) and the SEC were informed of its conclusions, the NAIC said it would “consider GAO’s recommendations” while the SEC provided no comments. As such, it appeared that future clarification of these issues would have to be achieved via another regulatory avenue.

Dodd-Frank also focused on the regulation of advisors, broker-dealers and agents via Section 913 (b)(1)-(2) of the 2010 Act which required the SEC to study the standards of care required of these three categories of financial planners. Here again, the term “financial planners” overlaps considerably among this group and basically amounts to a generic term involving numerous activities.

According to Tamar Frankel (2010-2011), “the Commission was required to study the standards of care for advisors, brokers-dealers and agents and consider the elimination of the broker exclusion from the Advisers Act of 1940.” First, they needed to evaluate the impact of imposing on brokers the duties of the Advisers Act, including the duty of acting in the best interest of the client and avoiding all conflicts of interest.

Second, the SEC was also charged with establishing a fiduciary duty for brokers which, per Frankel (2010-2011), included any parts of the conglomerate of "brokers, etc." Broker, etc. was a term Frankel used in his paper to describe the various titles in play.

In essence, if any of the previously mentioned financial intermediates provided "advice," they would trigger fiduciary governance which would also require that they disclose to their clients the terms of their relationships with investors, including any conflicts of interest. Lastly, Dodd-Frank also provided guidelines for enforcement.

Frankel (2010-2011) said that "there is no doubt that brokers, etc. are fiduciaries and if brokers present themselves and act as advisers, and they present themselves as experts, they are fiduciaries". This author felt that if "brokers, etc." did have any conflict of interest, the law should require them to disclose the conflict to the client, in writing, and the client would or should be able to consent to continuing the relationship on those terms.

After reviewing the GAO 2011 study relating to regulatory oversight of financial planners and the SEC study relating to "standards of care" for advisors and broker-dealers, also mandated by Dodd-Frank, two macro conclusions can be drawn.

The first is that there is really no way to isolate and separately regulate financial planners because numerous professionals overlap and it is really an *activity* and not a title or designation. The second is that regulatory attention should be focused on eliminating the broker exclusion from the Advisors Act of 1940 and requiring all advisors and broker-dealers to be governed under a fiduciary level standard of care.

While there had not been any further federal action by 2012 regarding the elimination of the broker exclusion from the Advisors Act of 1940, which would require that brokers be subjected to common-law fiduciary standards, there was considerable comment from the financial services industry about the negative impact requiring a fiduciary duty of care for brokers would have on lower-middle income (LMI) individuals.

According to Finke and Langdon (2012) “it has been suggested that the imposition of a fiduciary standard on registered representatives and brokers would result in significant changes in how broker-dealers conduct business by limiting a representative’s ability to recommend commission investments, provide advice to low and middle income-market clients, and offer a broad range of financial products.”

As such, Finke and Langdon (2012) took advantage of the variance in state broker-dealer *common-law standards of care* to research whether a relatively stricter fiduciary standard of care would affect the ability to provide financial advisor services to LMI consumers.

The first objective was to assess perceived differences in business conduct among brokers (synonymous with registered representatives) sorted by states that apply a strict fiduciary standard (4) and states that apply no fiduciary standard (14). As shown further in this study, the resulting differences were not statistically significant.

The second test objective was to assess the market saturation (as a proportion of total households) of brokers among all 50 states. Mean rates of broker saturation were calculated as the number of brokers divided by the number of households within each state.

The Finke and Langdon (2012) study quantified that “the number of brokers doing business within a state as a percentage of total households does not vary significantly for states with stricter fiduciary standards." The results showed that the saturation rates were nearly identical among fiduciary categories.

As such, and again according to Finke and Langdon (2012) "empirical results provide no evidence that the broker-dealer industry is or would be affected significantly by the imposition of a stricter legal fiduciary standard on the conduct of registered representatives."

Empirical evidence also showed that the models and assumptions that had been used for the past fifty years of so, where the burden of truly understanding and evaluating sophisticated financial mechanics was the responsibility of the investor, needed to be re-evaluated.

By 2013 there had been no further action taken by the SEC to initiate any such standard of care changes, and the promised DOL fiduciary rule, which had been delayed in September 2011 and was expected to be issued in 2013, had not yet materialized.

In early 2015, President Obama called on the DOL to "update the rules and requirements that retirement advisors put the best interests of their clients above their own financial interests." His statement that "it's a very simple principle: You want to give financial advice, you've got to put your client's interests first," was published in the DOL Fact Sheet on February 23, 2015.

On April 20, 2015, after more than 300 written public comments, two days of open hearings and more than three dozen individual meetings with industry, advocates and academics, the DOL finally released a long awaited fiduciary rule proposal with the objective of further defining the term fiduciary standard of care. The 2015 DOL fiduciary rule proposal included these provisions:

- Required more retirement investment advisers to put their client's best interest first by expanding the types of retirement investment advice covered by fiduciary protection when making recommendations to an employee benefit plan, plan fiduciary, plan participant or beneficiary, IRA, or IRA owner.

- Preserved access to retirement education, by carving out education from the definition of retirement investment advice and distinguished fiduciary from non-fiduciary activities, such as when a client tells a broker exactly what they want to buy without asking for advice.
- Provided for a change in the prohibited transaction exemption (PTE) approach that had been in play during the previous forty years.
- Provided a "best interest contract exemption" (BICE) which was a broader and more principal based (verses rule based) general guidelines exemption approach.

One of the strongest criticisms of the DOL 2010 proposal was that it would effectively ban commission-based and other indirect compensation. The best interest contract exemption (BICE) in 2015 was "DOL's response to that concern" (Milloy, 2015).

The BICE proposed to permit fiduciary advisors, on a limited basis, to receive compensation that varied based on their investment recommendations, as long as they acted in the best interest of the advice recipient. Broader exemptions were also introduced including a streamlined carve-out from the fiduciary status requirement for advice pertaining to low-fee products.

A new determination or definition of "fiduciary" was also introduced, based on the advice given and *not* the specific titles used. This was an easier requirement to introduce considering that the 2010 rule had proposed that anyone who was already a fiduciary under ERISA for other reasons, or who was an investment adviser under federal securities laws, would have automatically assumed the role of an investment advice fiduciary under this rule.

The re-proposed 2015 DOL fiduciary rule was still received by the financial services community with some trepidation. For example, one industry group, the Financial Services

Institute (2015) said “it was the latest attempt by DOL to replace its longstanding regulation defining the circumstances in which investment advice confers fiduciary status under ERISA” and that it “decreased LMI client access to retirement advice.”

Milloy (2015) added that “the 2015 rule sets duty of care standards for providers of financial advice, but its most likely impact would be to hurt retirement savers – especially low and middle income (LMI) retirement savers.” According to Headley (2011) “imposing a uniform fiduciary standard would negatively impact product access, product choice, and affordability of customer services for those customers who are in most need of these services.”

After the DOL conducted a comment period lasting over five months and received considerable feedback through four days of public hearings, over 3,000 comments, and more than 100 meetings, on April 6, 2016 they issued the final 2016 fiduciary rule regulations.

A regulatory impact analysis (RIA) released along with the final 2016 DOL fiduciary rule outlined the monetary harm caused to retirement investors from conflicted advice and the expected economic impacts of the rule. It estimated that middle and working class families with IRAs would save more than $40 billion over ten years when the new fiduciary rule and exemptions were fully implemented.

According to Katz and Belisle (2016) “ultimately, the final rule provides significant concessions to the financial services industry” and “while there are a number of changes between the proposed rule and this final rule, they appear to be more procedural than substantive”(Megs, 2016).

According the White House Fact Sheet (April, 2016) and the Federal Register (April, 2016) the final fiduciary rule expands the types of retirement advice included under fiduciary protection and includes any person receiving compensation for making investment recommendations specifically directed to a particular plan sponsor running a retirement plan, plan participant, or IRA owner for consideration or payment.

Communications are addressed in that certain benchmarks are established that quantify what does and does not qualify as fiduciary advice, and it further clarifies that education is still not considered investment advice or fall under the definition of fiduciary services.

While the 2016 rule requires that the fiduciary advisor must work solely in their clients best interest, cannot receive compensation that is unreasonable or creates a conflict of interest, the exemptions (BICE-PTE) will allow firms to accept common types of compensation, including commissions and revenue sharing payments.

Under DOL 2016, BICE exemptions will be available for more advice, will be available for small business' 401K plans, and will contain special provisions for use with proprietary products (PTE).

The latest rule requires that the advisor enter into contracts with clients that acknowledge their fiduciary positon, but there is more timing flexibility and the final exemption simplifies the contract requirement so that it is only between the firm and the client. The 2016 exemption also permits existing IRA clients to agree to the new contractual protections by "negative consent."

The exemptions have been considerably simplified from the 2015 proposal and for ERISA plans, so in many cases if proper fiduciary duty of care is acknowledged to the client, no additional BICE contract is required.

The 2016 rule also eliminates data retention requirements, contains a streamlined level fee provision so that advisors that receive only a level fee can rely on the exemption (BICE) without entering into a contract, as well as grandfather provisions pertaining to the treatment of existing investments.

In the final analysis, extensive stakeholder comments succeeded in carving out additional activities for consideration under the new rule, which in addition to education, communications and marketing activities, include appraising, ESOP evaluations as well as health and welfare plan advisory services.

The rule still holds that if advisers do not adhere to the fiduciary standards established in the rule, retirement investors can hold them accountable through either (1) a tort breach of contract claim or (2) the provisions of ERISA.

The final rule becomes applicable on April 10, 2017, however, the implementation of the Best Interest Contract Exemption (BICE) and Principal Transactions Exemption (PTE) is phased in on January 1, 2018.

Methods

The methods section address the quantification of broker *descriptive statistics* (test 1) and broker *saturation* (test 2) in various states requiring three different *common-law* standards of fiduciary duties of care.

According to the research performed by Finke and Langdon (2012), the names and addresses of 544,000 brokers (registered representatives) active in November 2011, were sorted into categories based on the application of a fiduciary standard.

There were four states that applied a strict fiduciary standard, 14 that applied no fiduciary standard, and 32 states that applied a limited fiduciary standard. Questions were based on brokerage industry statements and testimony before Congress suggesting that a stricter fiduciary standard will result in differences in ability to serve LMI clients. Broker-dealers in fiduciary and non-fiduciary states were asked the following questions:

1. Are you a registered investment adviser? (If so, survey is over.)
2. What percentage of your clients have incomes of less than $75,000?
3. What percentage has investable assets of over $750,000?
4. Are you able to serve the financial needs of low- to moderate-wealth clients?
5. Do your state's security regulations limit your ability to recommend a broad range of financial products?
6. Do you offer your clients a choice of financial products that meet their financial needs and objectives?
7. Do you provide advice tailored to the specific needs of your clients?
8. Do you feel that less-affluent clients avoid obtaining your services due to cost?
9. Are you able to recommend products that provide a commission?

10. How significant is the cost of compliance?
11. Do you feel that you make product recommendations that are in the best interest of your client?
12. Among the following options, which do you consider to be the most important single factor in pricing your investment advice to clients: competition in the marketplace, firm brand, personal qualifications, legal and compliance burden, or other?

Results

According to Finke and Langdon (2012) Descriptive statistics summarizing the responses received from a random survey of 207 registered representatives in four strict fiduciary states and 14 non-fiduciary states are presented as follows:

Table 1
Mean and Frequency Comparison of Registered Representatives

Question	Fiduciary States	Non-Fiduciary States	Difference (Fiduciary - NF)	P-Value Equal	DF
% clients income < $75,000	28.0%	27.9%	0.1%	0.982	174
% clients inv. Assets > $750,000	29.5%	34.5%	-5.0%	0.261	183
Serve needs of low/mod. wealth	78.9%	79.8%	-0.9%	0.878	202
Regulation limits product range	21.3%	17.4%	3.9%	0.486	198
Products meet clients needs	95.8%	94.3%	-1.5%	0.561	207
Advice tailored to client needs	91.7%	90.1%	1.6%	0.695	207
Less affluent avoid due to cost	23.6%	29.2%	-5.6%	0.374	195
Able to recommend commission	88.5%	88.2%	0.3%	0.936	206
Cost of compliance significant	70.9%	61.9%	9.0%	0.190	191
Act in best interest of client	97.8%	96.3%	1.5%	0.526	202

Source: Finke and Langdon (2012)

As can be seen above, the percentage of clients who have an income of less than $75,000 is, from a percentage perspective, about equal between fiduciary and non-fiduciary states. There is no statistically significant difference in either the percentage of high-wealth clients or in the percentage of brokers who believe they serve the needs of LMI clients.

The majority of survey participants believe they are able to provide products and advice that meet their customer’s needs. An important statistic regards the percentage of respondents who said they are able to recommend commission products. That results is 88.5 percent in strict fiduciary states and 88.2 percent in non-fiduciary states or de minimis variance.

The largest percentage variance among any of the questions posed is whether the cost of compliance is considered significant. Almost 71 percent of respondents in fiduciary states felt the costs were significant compared to about 62 percent in non-fiduciary states. The P-values confirm that the variance of all questions in the survey were not statistically significant.

Table 2 which follows shows the average degree of broker saturation, calculated as the number of brokers in the state divided by the number of households within the state.

Table 2

Broker Saturation Rates by States

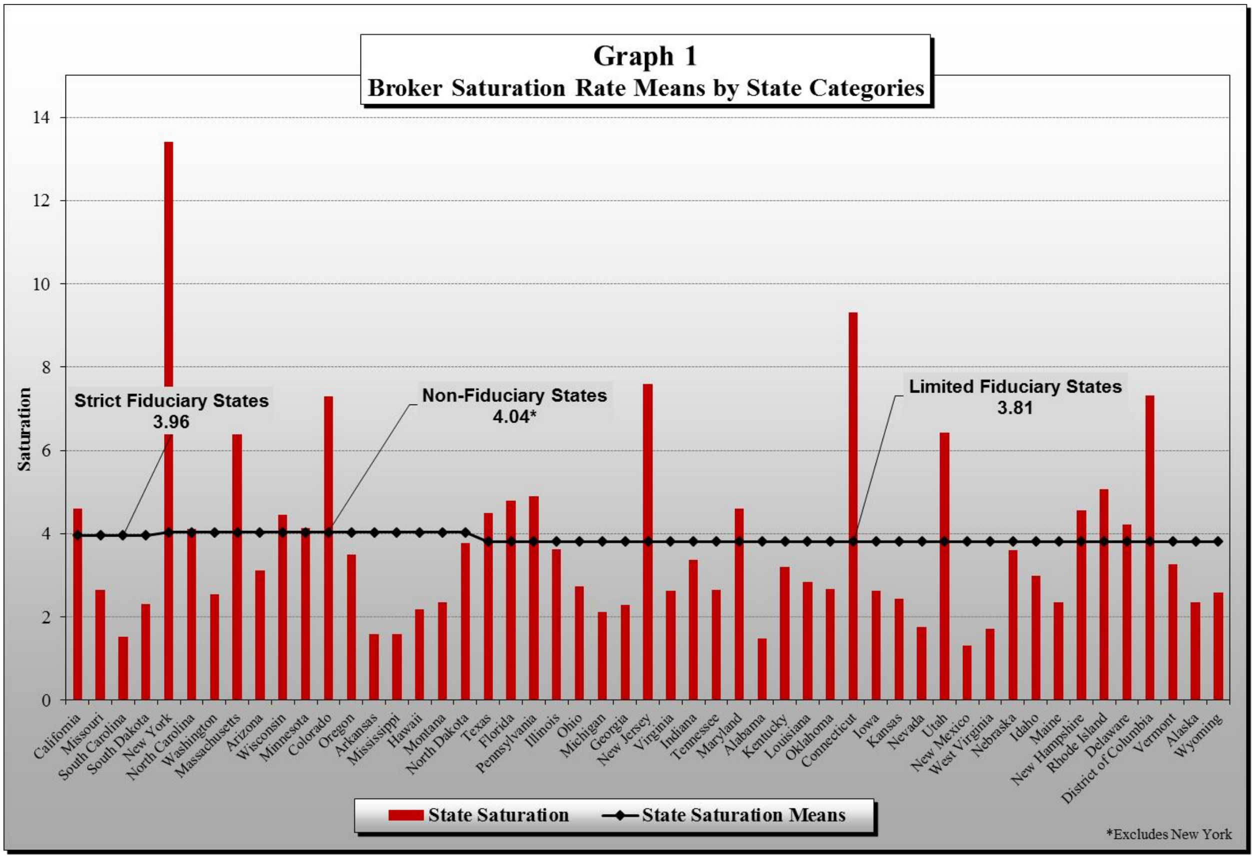
Strict Fiduciary States	**Registered Reps**	**Households (000s)**	**Saturation**
California	56,945	12,392	4.60
Missouri	6,244	2,355	2.65
South Carolina	2,667	1,753	1.52
South Dakota	737	317	2.32
Total Fiduciary	**69,120**	**16,817**	**3.96**
Non-Fiduciary States	**Registered Reps**	**Households (000s)**	**Saturation**
New York	96,862	7,221	13.41
North Carolina	15,094	3,666	4.12
Washington	6,605	2,601	2.54
Massachusetts	16,207	2,521	6.43
Arizona	7,280	2,333	3.12
Wisconsin	10,164	2,282	4.45
Minnesota	8,644	2,093	4.13
Colorado	14,168	1,942	7.30
Oregon	5,291	1,506	3.51
Arkansas	1,787	1,120	1.60
Mississippi	1,728	1,085	1.59
Hawaii	974	443	2.19
Montana	949	404	2.35
North Dakota	1,049	278	3.77
Total Non-Fiduciary	**186,802**	**29,501**	**6.33**
Total w/o New York	**89,940**	**22,279**	**4.04**
Limited Fiduciary States	**Registered Reps**	**Households (000s)**	**Saturation**
Texas	39,005	8,666	4.50
Florida	33,968	7,087	4.79
Pennsylvania	24,223	4,952	4.89
Illinois	17,258	4,768	3.62
Ohio	12,385	4,544	2.73
Michigan	8,130	3,815	2.13
Georgia	7,973	3,488	2.29
New Jersey	24,146	3,176	7.60
Virginia	7,836	2,986	2.62
Indiana	8,339	2,471	3.37
Tennessee	6,539	2,454	2.66
Maryland	9,781	2,122	4.61
Alabama	2,701	1,823	1.48
Kentucky	5,404	1,684	3.21
Louisiana	4,789	1,678	2.85
Oklahoma	3,837	1,429	2.68
Connecticut	12,682	1,361	9.32
Iowa	3,190	1,219	2.62
Kansas	2,691	1,106	2.43
Nevada	1,723	984	1.75
Utah	5,611	873	6.42
New Mexico	996	759	1.31
West Virginia	1,275	742	1.72
Nebraska	2,583	715	3.61
Idaho	1,727	574	3.00
Maine	1,291	550	2.35
New Hampshire	2,818	515	4.57
Rhode Island	2,074	408	5.08
Delaware	1,402	331	4.23
District of Columbia	1,872	256	7.31
Vermont	836	256	3.27
Alaska	593	251	2.36
Wyoming	568	219	2.58
Total Limited Fiduciary States	**260,246**	**68,278**	**3.81**

"There is a considerable range in saturation rates among states. The low being 1.31 per 1,000 households in New Mexico, while the high is of 13.41 in New York. Mean saturation rates are lower in states that have a limited fiduciary standard (3.81) and highest in states that currently have no fiduciary standard (6.33)."(Finke and Langdon 2012)

But the data appears to have an outlier, New York, which has a disproportionate amount of broker-dealer firms. When New York is excluded from non-fiduciary states, the saturation rates were much closer among fiduciary categories and all saturation rates were very close.

The saturation rates ended up at 3.96 for strict fiduciary states, 3.81 for limited fiduciary, and 4.04 for non-fiduciary states, so it appears clear that whether or not a state did or did not have fiduciary required duties of care, the ratios are very similar.

"Even when a regression model was run to account for differences in income, there was no statistical variance in saturation rates and ultimately there is no irrefutable evidence that the amount of assets managed by brokers in fiduciary or non-fiduciary states are greater or less," said Finke and Langdon (2012). A visual of these results helps show the continuity among the states and that the associated trend line, representing mean broker saturation, is relatively flat.


Graph 1
Broker Saturation Rate Means by State Categories
Saturation
0
2
4
6
8
10
12
14
Strict Fiduciary States
3.96
Non-Fiduciary States
4.04*
Limited Fiduciary States
3.81
California
Missouri
South Carolina
South Dakota
New York
North Carolina
Washington
Massachusetts
Arizona
Wisconsin
Minnesota
Colorado
Oregon
Arkansas
Mississippi
Hawaii
Montana
North Dakota
Texas
Florida
Pennsylvania
Illinois
Ohio
Michigan
Georgia
New Jersey
Virginia
Indiana
Tennessee
Maryland
Alabama
Kentucky
Louisiana
Oklahoma
Connecticut
Iowa
Kansas
Nevada
Utah
New Mexico
West Virginia
Nebraska
Idaho
Maine
New Hampshire
Rhode Island
Delaware
District of Columbia
Vermont
Alaska
Wyoming
State Saturation
State Saturation Means
*Excludes New York

Conclusions

This study reviewed the regulation of advisors, broker-dealers, and agents and the research appears to confirm that financial markets are more likely to operate at optimal levels when consumers understand how financial providers and products work and know how to choose among them, especially when they may not always know when a financial planner is required to serve their best interest.

When Dodd-Frank (2010) mandated the GAO study (2011) review the regulatory structure of the financial services industry, it became clear that the focus of the regulatory bodies should be on the activities provided by the financial services professional and not on the title or designation used.

The DOL fiduciary rule proposals also focused on advisor activity verses titles or designations when arriving at a determination of whether an advisor or broker was required to be governed under a fiduciary duty of care. They arrived at the conclusion that it is the actual activity provided that is the determining criteria and as a general rule, if advice is provided to individuals, the fiduciary rules will govern.

The initial DOL fiduciary rules focused more on applying the prevailing fiduciary rules and did not thoroughly address the impact of making such changes without also introducing some type of transitionary accommodations. This led to the DOL rule retraction in 2011 and the more industry friendly versions of the rule in 2015 and 2016, which clearly provided various degrees of transitional relief moving forward.

The resistance from the financial services industry regarding the fiduciary rule requirements centered on how the fiduciary requirement would substantially limit access of the lower and middle income individuals to qualified advisors.

While more research is certainly warranted as the fiduciary rule matures, current research shows that with a high degree of statistical significance, advisors and brokers act similar regardless of whether they are governed under strict fiduciary standards or no fiduciary standards.

While historical results to date provide no evidence that the broker-dealer industry is affected significantly by the imposition of a stricter legal fiduciary standard on the conduct of advisors or brokers, future research will certainly add to that body of knowledge.

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