AMERICAN ASSOCIATION for JUSTICE

December 7, 2017

The Honorable Jay Clayton
Chairman
U.S Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Investment Advisor and Broker Dealer Standards of Conduct

Dear Chairman Clayton:

The American Association for Justice (AAJ), formerly the Association of Trial Lawyers of America (ATLA), hereby submits the organization's response to the Security and Exchange Commission's (SEC or the Commission) June 1, 2017 request for comment regarding the standards of conduct that should be required of investment advisers and broker-dealers.[1]

AAJ, with members in the United States, Canada, and abroad, is the world's largest trial bar. It was established in 1946 to safeguard victims' rights and strengthen the civil justice system. AAJ members represent victims of fraud. As representatives of those who have been subject to the abuses that have permeated the financial services market, we provide our input for the Commission's review of the standards of conduct applicable to broker-dealers and registered investment advisers.

We thank the Commission for beginning the long-overdue process of addressing the appropriate standard of conduct for the people and entities that control so much of American consumers' financial security. We applaud the Commission's stated goal of collaboration with the Department of Labor (DOL),[2] which recently enacted a strong, forward-looking standard of conduct rule for retirement advisers which protects the rights of consumers of financial services and promotes confidence in the market for retirement financial products (the so-called DOL Fiduciary Rule).[3] Strong conduct regulations, like the DOL's Fiduciary Rule, that protect the rights of investors promote confidence in the fundamental fairness of America's financial system.

---

[1] Securities and Exchange Commission, Public Statement: Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers (June 1, 2017) *available at* https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31
[2] *Id*.
[3] 81 Fed. Reg. 20946 (Apr. 8, 2016).

AAJ strongly supports the DOL's Fiduciary Duty Rule, and encourages the Commission to adopt a similar approach to regulating the conduct of investment advisers and broker dealers. The DOL Fiduciary Rule requires that investment advisors act in consumers' best interests by avoiding conflicts of interest and being transparent about fees and financial incentives. This is a common-sense standard that promotes the Commission's stated mission of maintaining "fair, orderly and efficient markets […] that are worthy of the public's trust."[4] For too long, American investors have received faulty investment advice that may not be in their best interest. The DOL's approach reforms the system to de-incentivize advisers from providing self-serving and imprudent recommendations without accountability, and ensures that investors have greater protections when making decisions about their retirement—including access to the courts.

For the reasons outlined below, AAJ strongly encourages the SEC to follow the DOL's approach in developing and adopting a fiduciary standard of conduct rule for investment advisers and broker-dealers.

I. A Fiduciary Standard is Necessary to Protect Investors

It is clear that the Commission's standard of conduct rules must be updated to reflect the current market. As the extensive notice and comment discussion surrounding the DOL's Fiduciary Rule shows, ordinary investors expect and demand that the people who control their financial future act in their best interest. The extremely limited (and sometimes nonexistent) standards of conduct provided by the Investment Advisers Act of 1940 (the '40 Act), the Securities Act of 1933 (the '33 Act), the Securities Exchange Act of 1934 (the '34 Act) and the regulations promulgated thereunder desperately need updating to fit the modern marketplace, which includes pressures and demands on advisers and broker-dealers that were unimaginable in 1940. Many private-sector investors do not realize that the people who control their financial destiny may not owe them a legal obligation to act in their best interests. In fact, many financial professionals who are typically not fiduciaries hold themselves out as trusted advisers and use titles such as "financial adviser" or "financial consultant." Use of these titles is deliberate and intended to falsely assure consumers that they are receiving advice designed to serve their best interests and to convince consumers that they are in a relationship of trust. According to a Rand Corporation survey of investors' beliefs about different financial service professionals, 59 percent mistakenly believed that "financial advisors or financial consultants" are required by law to serve their client's best interest.[5] The Rand study also indicated that many investors are incapable of telling whether their own adviser is a broker or an investment adviser, let alone whether he or she owes them a fiduciary duty.[6]

When consumers receive financial advice that is not in their best interest, it can cause real harm. Financial professionals who are not required to put their client's interests first are free to

[4] Securities and Exchange Commission, About the SEC: Mission Statement *available at* https://www.sec.gov/about.shtml

[5] Angela A. Hung, et al., Investor and Industry Perspectives on Investment Advisers and Broker-Dealers, Rand Corporation, Sponsored by the United States Securities and Exchange Commission (Jan. 2008) *available at* http://1.usa.gov/1nePF0L.

[6] *Id.*

steer investors into excessively high cost, low performing investments that drain hard-earned savings while maximizing the professional's profits. Practices like theses can cost investors a lot of money. For example, working from the various studies, the DOL estimates that retirement savers alone will lose between $210 billion and $430 billion over 10 years, and between $500 billion and $1 trillion over 20 years, because of conflicted advice just with regard to mutual fund investments in IRAs.[7] The DOL also estimated that a retirement saver who rolls money out of a 401(k) plan and into an IRA based on conflicted advice can expect to lose 12 to 24 percent of the value of his or her savings over 30 years.[8] These are examples based solely on conflicted advice with respect to retirement accounts and financial products, which the Council of Economic Advisors (CEA) found costs savers an aggregate average of $17 billion every year.[9] The full cost of conflicted advice is far higher for all American investors.

Unfortunately, everyday American investors who can least afford to have their finances diminished due to conflicted advice are at the greatest risk. According to the industry's own data,[10] moderate income savers are disproportionately served by advisers who are not required to serve their best interests and therefore are the most likely to receive and follow harmful advice. For these reasons, the SEC must move forward with a strong consumer oriented fiduciary standard similar to the DOL rule.

A. A Key Component of a Strong Fiduciary Standard is Accountability via the Court System

A major problem with the current paucity of conduct regulations on investment advisers and broker-dealers is that bad actors can rarely be held accountable for any losses to everyday investors caused by their misconduct.[11] Any SEC action must address consumer remedies and the abusive practice of forced arbitration. Forced arbitration directly prevents injured investors from being made whole in court and creates an unequal power dynamic between investors and advisors.

Consumers are regularly required to sign away their legal rights in favor of forced arbitration before a dispute even arises. Forced arbitration clauses typically are (1) offered on a take-it-or-leave-it basis, (2) binding, and (3) pervasive. More explicitly, consumers and investors not only have no choice but to enter into forced arbitration in the event of a dispute, but any results reached in the arbitration process are final and generally not reviewable by a court of law. Since forced arbitration decisions are not official court proceedings, they also hinder the development of law, as the growth of a body of law in the common law system requires the evolution of case law. Instead of contributing to the doctrine of *stare decisis*, forced arbitration decisions are akin to a

---

[7] 81 Fed. Reg. 20946, 20950 (Apr. 8, 2016).
[8] *Id*.
[9] Council of Economic Advisers, The Effects of Conflicted Advice on Retirement Saving (Feb. 23, 2015) *available at* https://obamawhitehouse.archives.gov/blog/2015/02/23/effects-conflicted-investment-advice-retirement-savings
[10] Letter from Kent Mason, Partner at Davis and Harman, citing Oliver Wyman's "Assessment of the impact of the Department of Labor's proposed 'fiduciary' definition rule on IRA consumers," April 12, 2011, http://1.usa.gov/1CyB9V2.
[11] *Id*.

"dead end" in that future judicial decisions cannot rely on arbitration outcomes regardless of the factual or policy similarities between cases.

Furthermore, arbitrators are generally not required to have any legal training and often have a stake in the forced arbitration outcome. This is because when a dispute arises, a company will often refer the case to an arbitrator who has previously decided cases in its favor. Accordingly, arbitrators are motivated by a pecuniary interest to rule for corporate entities to attract and retain their future business.

Additionally, because forced arbitration decisions are not required to be made public, consumers have little chance of uncovering an arbitrator's potential bias. Society—and the markets—benefit from an open legal process that exposes "bad actors" and lets investors price these actions into their valuations. One of the most important societal benefits of civil litigation is the discovery process, which can uncover negligent or harmful corporate practices that lead to financial or even physical injury to the public. Forced arbitration restricts the public's ability to obtain such information—and thus artificially inflates the valuation of bad actors—by keeping abusive practices hidden.

Ultimately, AAJ believes that investor choice in dispute resolution is paramount. We urge the Commission to follow its own guiding principles—that sunshine and transparency are the best remedy for bad actors in the market—and ensure that arbitration policy is transparent and fair to investors.

B. The Commission Should Ban Harmful Forced Arbitration Clauses Because It Impedes the Functioning of the Free Market

Financial institutions have long used mandatory pre-dispute arbitration clauses to limit their potential liability for wrongdoing—this is partly why so few financial institutions were held to account by harmed consumers during the recent systemic financial crisis and why institutions like Wells Fargo have managed to continue to avoid paying fair restitution to wronged consumers.[12] These mandatory, binding pre-dispute arbitration clauses represent a failure of the free market approach to regulation and require intervention to prevent future institutions from enriching themselves at everyday investor's expense. Notably, the number of primary checking accounts at Wells consistently increased as the fraud became public, suggesting that the free market did not discipline Wells for its misconduct until regulators intervened, and did so only modestly at that point."[13] This is the definition of a market failure that has created an unquestionably inefficient outcome.

Currently, as the Wells Fargo example shows, investors are required to unknowingly sign away their legal rights in favor of forced arbitration before a dispute has arisen. Investors not only have no choice but to arbitrate their disputes, but often have limited or no ability to appeal an arbitrator's decision in a court of law. Additionally, forced arbitration is costly. In most cases,

---

[12] Jeff Sovern, Free-Market Failure: The Wells Fargo Arbitration Clause Example (May 1, 2017). 70 Rutgers U.L. Rev. (Forthcoming); St. John's Legal Studies Research Paper No. 17-0004, *available at* https://ssrn.com/abstract=2961347

[13] *Id*.

investors must pay filing fees and arbitrators' costs upfront. For many, these upfront costs and ongoing fees are prohibitive and the provider is often allowed to choose the location of the forced arbitration, making it even more costly for the investor. Forced arbitration represents a clear example of a market failure—not only do consumers unwittingly sign away their rights, in doing so they force the market into an inefficient outcome, where institutions are unjustly enriched for harms suffered by investors through no fault of their own.

Additionally, as the Wells Fargo case illustrates, the failure to hold these bad actors to account can bring the entire system into disrepute. A Gallup poll from the time the Wells Fargo fraud was discovered reveals that American's confidence in the financial sector fell as more details were revealed, further diminishing an already low public opinion of the industry.[14] The Commission's goal is to promote consumer confidence in the fundamental fairness of the market for securities and investment products. Placing restrictions on mandatory pre-dispute arbitration clauses would strongly support that goal.

C. Adopting the DOL Fiduciary Standard Would Not Disrupt the Securities Market

Commission action to collaborate with the DOL and institute a similarly structured fiduciary standard would not lead to major dislocations and disruptions in the financial services market, because many investment advisors have already incorporated the fiduciary standard of care into their practice. As with any rulemaking, the DOL responded to industry representatives and consumer stakeholders, working to devise a negotiated agreement that both sides supported. Any movement further away from that compromise by the Commission would harm both investors and the institutions that negotiated in good faith with the DOL.

In addition to harming consumer pocketbooks, the Commission's failure to collaborate with the DOL would harm the financial institutions who, after negotiating in good faith with consumer representatives and the DOL, have now spent considerable time, effort, and expense preparing for—and implementing—the Department's rule, including preparing for potential implementation of a similar Commission rulemaking. If anything, the Commission's failure to adopt a similar fiduciary standard of conduct regulation would lead to more market disruption than the alternative—a strong, forward-thinking investor protection regulation.

II. The Commission Must Guarantee Injured Investors Access to the Courts

The Commission's June 1 letter asks commenters whether the Commission should adopt private rights of action as part of any future rulemaking.[15] It unquestionably should. Access to the full protections of the Seventh Amendment and our judicial system is a staple of our constitutional democracy and a functioning market economy. When one party harms another in a transaction, the most efficient way to right that wrong without unjustly enriching one member of the transaction is through the civil justice system—a fact that the Commission has repeatedly

---

[14] Gallup, Americans' Confidence in Banks Still Languishing Below 30% (June 5, 2016) *available at* http://www.gallup.com/poll/192719/americans-confidence-banks-languishing-below.aspx?g_source=confidence+in+banks&g_medium=search&g_campaign=tiles

[15] SEC Letter, *supra* at note 1.

acknowledged in its reliance on the mechanism of the private class action in resolving disputes under the securities laws.[16]

A private cause of action is the most economically efficient and practical mechanism for allowing injured consumers to hold bad actors accountable within the framework of the market for financial services. Including a specific private cause of action to deter behavior that brings the fundamental fairness of the entire securities system into question would further the Commission's own stated aims while allowing private actors to determine the efficient solution to disputes.

a. The Commission Should Follow FINRA's Example and Prohibit Contracts that Include Bans on Consumer Class Actions

The Commission should follow the Financial Industry Regulatory Authority (FINRA)'s lead[17] and mandate the removal of class action bans from all current and future brokerage contracts. Investors' ability to join together as a class brings relief to those who suffer identical or similar harms where a singular, individualized action would be cost-prohibitive to pursue. By permitting class action bans, the Commission grants bad actors in the securities industry the ability to act with impunity. That is, when class action bans appear in forced arbitration clauses, they have the practical effect of preventing investors from pursuing any legal remedy whatsoever. When, as is often the case for small investors, the cost and expense of pursuing an individual claim in arbitration far exceeds any possible recovery, a waiver of the right to participate in any collective action effectively immunizes corporations from these smaller claims.

Class actions function as a private market solution to government regulation:[18] the securities industry is governed, then, both by a public enforcement mechanism (the Commission) and a private system that keep bad actors in check. In fact, the US Supreme Court has specifically recognized the import role of private enforcement to deter fraud and corporate misconduct, a fundamental goal of the securities laws, by supplementing criminal and civil actions brought by the various government entities.[19] Likewise, the SEC has long recognized that private litigation is an "essential supplement" to the SEC enforcement actions.[20]

Class action bans threaten this vital dual-enforcement system to its core. For as long as there has existed a system of private and public enforcement of securities law, there have been

---

[16] 15 U.S.C. § 78u-4 ("Private securities litigation"). *See also* Securities and Exchange Commission, "How can investors get money back in a fraud case involving a violation of the federal securities laws?" (referencing, in particular "private class actions") *available at* https://www.sec.gov/fast-answers/answersrecoverfundshtm.html.
[17] FINRA Rule 13204 (2012).
[18] House Liberty Caucus, Statement on H.R. 985 (Mar. 9, 2017) arguing that "class action lawsuits are a market-based solution for addressing widespread breaches of contract . . . they are a preferable alternative to government regulation because they impose damages only on bad actors."
[19] *See* Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 313 (2007) ("This Court has long recognized that meritorious private actions to enforce federal antifraud securities laws are an essential supplement to criminal prosecutions and civil enforcement actions brought respectively, by the Department of Justice and the Securities and Exchange Commission.").
[20] Brief of the United States as Amicus Curiae Supporting Respondents at 1, Merck & Co., Inc. v. Reynolds, 130 S. Ct. 1784 (2010) (No. 08-905) (recognizing the importance of private securities litigation as a supplement to criminal and civil enforcement actions); *see also* Walter Remarks, supra (it is "critical to investors, our securities markets, and our economy overall that these laws remain fully enforceable [by the public]").

managers, directors, and corporate actors seeking ways to avoid it. Attracting investment requires protecting investors, and investor protection requires both law and the effective enforcement of law. Regrettably, it is simply not possible to unambiguously define every pyramid scheme, every breach of a fiduciary duty, or every method a manager might use to misappropriate or misuse company assets.[21] Therefore, enforcement, and the ability to translate violations of codified statutes and common law principles into meaningful deterrents, regulatory sanctions, and, most importantly, the return of assets to wronged investors, is essential.

Directors and officers of corporations are fiduciaries, charged with acting in the best interests of the corporation and its stockholders. This principle is the very foundation upon which the relationship between shareholders, as the owners of a corporation, and the corporation's directors and officers, is built. Although some directors and officers appropriately fulfill their fiduciary duties to the corporation and the shareholders they serve, the long history of shareholder class action (and, relatedly, shareholder derivative litigation) serves as a poignant reminder that injured parties have an important role to play in regulating corporate behavior and enforcing shareholder rights. And, because corporate law does not directly provide for public regulation or enforcement of director and officer conduct, it is investors, through civil litigation and the shareholder ballot box, who are responsible for actively enforcing these fiduciary duties.

Private securities actions are undeniably the defrauded investor's primary mechanism for compensation. Statistics show that "private enforcement . . . dwarf[s] public enforcement," and thus private litigants are much more successful in terms of recovery than the SEC.[22] In fact, "even in major scandals where the SEC has brought its own action, the damages paid in securities class actions are usually (but not always) a multiple of those paid to the SEC."[23]

The US Supreme Court has long acknowledged the vital importance of private securities litigation as a "most effective weapon" in the federal enforcement regime.[24] Fortunately for investors, that recognition bares out in practical application, with assets being actively returned to shareholders, investors, pensioners, and retirees every year. In private litigation relating to the financial scandals at Enron, WorldCom, Tyco, Bank of America and Global Crossing, private enforcement returned over $19.4 billion to investors.[25] The SEC's enforcement actions against these same companies relating to the same wrongdoing netted penalties and fees of $1.750

---

[21] *See* Ira Millstein, Chair of the IFC/World Bank's Private Sector Advisory Group, remarks before the Lex Mundi North America Regional Conference (2003) *available at* http://www.ifc.org/wps/wcm/connect/6ab71c8048a7e7b3accfef6-060ad5911/Focus_ENFCorpGov3.pdf?MOD=AJPERES

[22] John C. Coffee, Jr., Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation, 106 Colum. L. Rev. 1534, 1542-43 tbls. 2 & 3 (2006).

[23] *Id*. at 1543.

[24] *See* Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 310 (1985).

[25] *See, e.g., In re: Tyco International, Ltd., Securities Litigation, U*.S. District Court, District of New Hampshire, 02-266 ($3.2 billion settlement); *In re: Enron Corporation Securities Litigation*, U.S. District Court, Southern District of Texas, 01-3624($7.2 billion settlement); *In re: Worldcom, Inc. Securities Litigation,* U.S. District Court, Southern District of New York, 02-3288 ($6.1 billion); *In re: Bank of America Corp. Securities, Derivative, and Employee Retirement Income Security Act (ERISA) Litigation,* U.S. District Court, Southern District of New York, 09-2058 ($2.4 billion settlement); *In re: Global Crossing Ltd. Securities Litigation,* U.S. District Court, Southern District of New York, 02-910 ($447.8 million settlement).

billion.[26] Indeed, in just a few years the SEC has recovered $3.76 billion in penalties, disgorgement and other monetary relief on litigation relating to the 2008 financial crisis.[27] In comparison, private class action litigation against just four financial institutions arising from their conduct that led to the near collapse of our economy resulted in judgments or settlements of over $16 billion.[28]

Clearly, private securities litigation generally, and private securities class action litigation in particular, perform a significant role in maintaining investor confidence in the integrity of our markets. Shareholders are assured that even if public enforcement fails to ferret out every incidence of wrongdoing, they maintain the ability to band together with similarly affected investors to find and punish corporate wrongdoing through civil litigation.

Consequently, eliminating penalties for committing securities fraud, breaches of fiduciary duties, or other corporate misconduct by allowing contracts with consumer class action bans (under the pretext of reducing frivolous claims or curtailing legal expenses for investors and shareholders) creates negative externalities.[29] When corporate actors aren't penalized for the harms and costs they impose on investors, they tend to do more bad acts. Thus, a failure to adequately penalize and enforce securities law violations undermines the trust and confidence in the securities markets, increasing the cost of capital for all US listed firms.[30] Professor John Coffee astutely observes that:

> [T]he cumulative effect impact of Enron, WorldCom and a host of other scandals in the 2000 to 2002 era made stockholders wary, chilled the initial public offering market, and caused investors to demand a higher return based on the perceived higher risks – in short, the cost of capital rose…[w]hen the cost of capital rises, the economy as a whole suffers, Gross National Product declines or stagnates, and unemployment may increase. As a result, not only investors, but also citizens throughout society experience a loss.[31]

From this, the ramifications not only to shareholders, but to capital markets generally, are clear: if companies are permitted to stymie or eliminate the ability of investors to join together to hold corporate actors accountable for their misdeeds, investor confidence in the integrity of our market suffers, investor participation diminishes, and American's prosperity is put at risk.

---

[26] *See* Tyco SEC Settlement Fair Fund: http://www.tycosecsettlement.com/ ($55.8 million settlement); Enron SEC Settlement Fair Fund: http://enronvictimtrust.com/ ($570 million); Worldcom SEC Settlement Press Release: http://www.sec.gov/news/press/2003-81.htm ($750 million); Bank of America SEC Fair Fund: http://bankofamericafairfund.com/ ($375 million); Global Crossing SEC Settlement Press Release: http://www.sec.gov/litigation/litreleases/lr19179.htm ($300,000).

[27] SEC Enforcement Actions, Addressing Misconduct That Led To or Arose From the Financial Crisis, Key Statistics (through October 7, 2016), *available at* http://www.sec.gov/spotlight/enf-actions-fc.shtml.

[28] Sam Carr, SNL Financial, Largest US banks have built a $60B settlement tab, so far (Mar. 5, 2013), *available at* http://www.snl.com/InteractiveX/Article.aspx?cdid=A-17047074-12337.

[29] Torchio, F., "The Circularity of Life in Securities Class Actions", University of Rochester (2008) *available at* http://www.forensiceconomics.com/assets/the_circularity_of_life_in_securities_class_actions.pdf

[30] *Id*,

[31] John C. Coffee, Jr., Reforming the Securities Class Action: An Essay on Deterrence and its Implementation, 106 Colum. L. Rev. 1534-1586 (2006).

For the reasons stated above, AAJ strongly encourages the Commission to follow FINRA's lead and prohibit class action waivers from financial contracts as part of its fiduciary standard of conduct.

III. The Fiduciary Duty Standard Would Not Result in Increased Litigation

A fiduciary standard would not result in increased litigation. We encourage the Commission to follow the Department's reasoning in adopting the Fiduciary Rule and conclude that the institutional hurdles associated with the commencement of a class action have proven to be sufficient deterrents to litigation in the past. There is ample support of this conclusion, as other restrictions on class action waivers have been in effect for years, without litigation surges: for example, overall workplace class action activity has actually decreased since the National Labor Relations Board (NLRB) found class action bans unenforceable in 2012,[32] and, as mentioned above, FINRA[33] has prohibited the inclusion of class action waivers in forced arbitration agreements since 1992, and has not seen abuses of the system or drastic changes in price. Instead, the class action provision achieves the President's stated goal of "American empowerment" by preventing financial advisors from taking advantage of retirees while enabling the latter to save more money.

The Department's Fiduciary Duty Rule closes loopholes created when investment advisors use forced arbitration clauses to shield themselves from class action claims. Now, investment advisors seeking to benefit from the rule's safe harbor provisions are prohibited from blocking their clients from participating in class actions against them. The rule acts as a deterrent while ensuring that financial advisors that do not act in their client's best interest are responsible for their own behavior, rather than passing that burden on to retirement savers. These transgressions cost working and middle class Americans an estimated 17 billion dollars a year in retirement savings alone.[34]

Class action plaintiffs must already satisfy stringent requirements to be certified as a class under Federal Rule of Civil Procedure 23, including demonstrating commonality and typicality of facts and law across the entire class, a large enough size, and adequate representation. Similarly, Rule 23 requires that the injury incurred by all members of the class is comparable in size and scope, and that the application of the relevant law to each plaintiff be substantially the same. The class must also be large enough to warrant a court certifying it as a class action—rather than simply deciding to join multiple, individual cases. Finally, the prospective class must include adequate representatives that accurately reflect the interests of all putative class members.

These requirements are exceptionally difficult to meet and become nearly impossible the smaller the scope of a business. Thus, large corporations tend to be more affected by class actions than small businesses because the smaller entities simply don't have enough clients impacted by

---

[32] Seyfarth & Shaw LLP, Workplace Class Action Report (2017) *available at* http://www.workplaceclassaction.com/2017/02/the-story-behind-workplace-class-action-filings-in-2016-trend-4/. *See also* In Re D. R. Horton, Inc., 357 NLRB 2277 (2012).
[33] FINRA Rule 13204 (2012).
[34] Counsel of Economic Advisors, The Effects of Conflicted Investment Advice on Retirement Savings (Feb. 2015) *available at* https://obamawhitehouse.archives.gov/sites/default/files/docs/cea_coi_report_final.pdf

the same illegal activity to warrant class relief. Clients of an investment advisor offering individual advice to investors on a case-by-case basis, for example, likely could not form a class, because the numerosity requirement of Rule 23 designed to encourage judicial economy would never be met. This system ensures that the class action cases that would go forward will only be cases where the harm in question is systemic, widespread, and a clear violation of the exemption under the Fiduciary Duty Rule.

For cases that do not meet the onerous requirements proscribed in Rule 23, they simply would not be joined as a class, and the individuals would be permitted to pursue their claims individually.

Investment advisors are not the first to be banned from including class action waivers in contracts—and the markets that have banned class action waivers have not experienced an explosion of litigation. As noted above, FINRA[35] has prohibited the inclusion of class action waivers in forced arbitration agreements since 1992, and has not seen abuses of the system or drastic changes in price. Furthermore, the Fiduciary Duty Rule is based on common law developed in state courts, where there are also no skyrocketing costs for investment advisors or state-wide surges in class action litigation—which is in part due to the onerous complexity of bringing class action claims under the current rules.[36]

IV. Conclusion: The Commission Should Adopt a Fiduciary Standard of Conduct

The Commission's stated goal, of protecting investors and ensuring confidence in the fundamental fairness of the market for securities and investment products, requires strong, forward-looking standard of conduct regulations for investment advisors and broker-dealers. At a time when confidence in the financial markets remains at record lows, the Commission has the tools to boost everyday investor confidence in the market while encouraging economically efficient free-market solutions to dispute resolution. By developing a fiduciary standard of conduct rule while ensuring investor's access to their 7th Amendment rights, the Commission would simultaneously encourage efficient and market-based solutions to disputes while promoting the fundamental fairness of the financial system.

AAJ encourages the Commission to adopt a fiduciary standard of conduct rule that is substantially similar to the forward-looking regulation already in effect at the Department of Labor. If you have any questions or comments, please contact Gabe Lezra, AAJ's Regulatory and Federal Relations Counsel, at [redacted].

Sincerely,

---

[35] FINRA Rule 13204 (2012).

[36] *See, e.g.*, Multnomah Group, Class Action Litigation Against Fiduciaries: How Current Litigation Impacts You and Your Plan (Sept. 2016) *available at* http://www.multnomahgroup.com/hubfs/PDF_Files/Webinar_Presentation_Slides/Class_Action_Litigation_Against_Fiduciaries.pdf (showing that class action activity has not increased); *see also* Pershing, Investment News Compensation and Staffing Study (2016) (showing increased profits for small and solo-practitioner RIAs).

Kathleen Nastri
President
American Association for Justice