

## [51 N.J.R. 493\(a\)](#)

VOLUME 51, ISSUE 8, APRIL 15, 2019

### RULE PROPOSAL

#### Reporter

51 N.J.R. 493(a)

***NJ - New Jersey Register > 2019 > APRIL > APRIL 15, 2019 > RULE PROPOSAL > LAW AND PUBLIC SAFETY -- DIVISION OF CONSUMER AFFAIRS***

## **Interested Persons Statement**

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### INTERESTED PERSONS

Interested persons may submit comments, information or arguments concerning any of the rule proposals in this issue until the date indicated in the proposal. Submissions and any inquiries about submissions should be addressed to the agency officer specified for a particular proposal.

The required minimum period for comment concerning a proposal is 30 days. A proposing agency may extend the 30-day comment period to accommodate public hearings or to elicit greater public response to a proposed new rule or amendment. Most notices of proposal include a 60-day comment period, in order to qualify the notice for an exception to the rulemaking calendar requirements of [N.J.S.A. 52:14B-3](#). An extended comment deadline will be noted in the heading of a proposal or appear in a subsequent notice in the Register.

At the close of the period for comments, the proposing agency may thereafter adopt a proposal, without change, or with changes not in violation of the rulemaking procedures at [N.J.A.C. 1:30-6.3](#). The adoption becomes effective upon publication in the Register of a notice of adoption, unless otherwise indicated in the adoption notice. Promulgation in the New Jersey Register establishes a new or amended rule as an official part of the New Jersey Administrative Code.

## **Agency**

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LAW AND PUBLIC SAFETY > DIVISION OF CONSUMER AFFAIRS > BUREAU OF SECURITIES

## **Administrative Code Citation**

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Proposed Amendment: [N.J.A.C. 13:47A-6.3](#)

Proposed New Rule: N.J.A.C. 13:47A-6.4

## **Text**

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Fiduciary Duty of Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives

Authorized By: Christopher W. Gerold, Bureau Chief, Bureau of Securities.

Authority: [N.J.S.A. 49:3-67\(a\)](#).

Calendar Reference: See Summary below for explanation of exception to calendar requirement.

Proposal Number: PRN 2019-044.

Submit written comments by June 14, 2019, to:

Christopher W. Gerold, Bureau Chief  
Bureau of Securities  
153 Halsey Street, 6th Floor  
PO Box 47029  
Newark, New Jersey 07101

or electronically at: <http://www.njconsumeraffairs.gov/proposals/pages/default.aspx>

The agency proposal follows:

### **Summary**

In order to better protect the public interest and, in particular, New Jersey's investing public, the New Jersey Bureau of Securities (Bureau) is proposing new N.J.A.C. 13:47A-6.4 to establish, by regulation, the common law fiduciary duty and apply it to broker-dealers and agents, and to codify it for investment advisers and investment adviser representatives. The Bureau believes that the proposed new rule is necessary to ensure that persons involved in the securities markets are uniformly held to a high standard in their dealings with the general public and is necessary to ensure the welfare of New Jersey investors. Moreover, the proposed new rule will establish a uniform standard for financial professionals and rectify investor confusion that results from the lack of uniformity.

The Bureau published a notice of pre-proposal soliciting comments regarding amendments to its rules to require that broker-dealers, agents, investment advisers, and investment adviser representatives owe a fiduciary duty to their customers. In addition, in connection with the notice of pre-proposal, the Bureau held two informal conferences to take testimony from interested parties to gather facts to inform a rulemaking and to afford ample opportunity for the receipt of public comment from the regulated communities, industry representatives, and the public at large. The notice of pre-proposal and informal conferences was published in the New Jersey Register on October 15, 2018, at 50 N.J.R. 2142(a). The Bureau received 62 comments and there were 21 speakers at the informal conferences.

It is well established that investment advisers owe their customers a fiduciary duty as a matter of law. Broker-dealers by rule are subject to a suitability standard, which means having reasonable grounds to believe that the strategy, transaction, or recommendation is suitable for the customer, based upon reasonable inquiry concerning the customers' investment objectives, financial situation, and needs, and any other relevant information known by the broker-dealer.

In the wake of the 2008 financial crisis, Congress recognized the need to ensure that retail investors can readily access unbiased advice from all financial professionals, regardless of whether that advice comes from an investment adviser or broker-dealer. In accordance with Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Securities and Exchange Commission (SEC) conducted a study (the 913 Study) and the SEC staff recommended that the SEC establish a uniform fiduciary duty standard for investment advisers and broker-dealers when providing investment advice about securities to retail customers that is consistent with the standard that currently applies to investment advisers.

An investment adviser is a fiduciary whose duty is to serve the best interests of its clients, including an obligation not to subordinate clients' interests to its own. Included in the fiduciary standard are the duties of loyalty and care.

An investment adviser that has a material conflict of interest must either eliminate that conflict or fully disclose to its clients all material facts relating to the conflict.

Broker-dealers that do business with the public generally must become members of the Financial Industry Regulatory Authority (FINRA), which serves as a self-regulatory organization (SRO) for broker-dealers. Under the antifraud provisions of the Federal securities laws and SRO rules, including SRO rules relating to just and equitable principles of trade and high standards of commercial honor, broker-dealers are required to deal fairly with their customers. Moreover, broker-dealers are subject to statutory, SEC, and SRO requirements that are designed to promote business conduct that protects customers from abusive practices, including practices that may be unethical but may not necessarily be fraudulent. Currently, broker-dealers and their agents are required to have a reasonable basis to believe a recommended transaction or investment strategy involving securities is suitable for the customer. The reasonable basis is based on information obtained through reasonable diligence of the broker-dealer or agent to ascertain the customer's investment profile. FINRA Rule 2111 states the customer's investment profile includes, but is not limited to, the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, and risk tolerance.

[page=494] The 913 Study reflected that retail investors do not understand the differences between investment advisers and broker-dealers or the standards of care applicable to broker-dealers and investment advisers. Many find the different standards of care confusing and are uncertain about the meaning of the various titles and designations, such as "money-manager," "wealth-manager," "financial advisor," etc., used by investment advisers and broker-dealers. Many expect that both investment advisers and broker-dealers are obligated to act in the investors' best interests. Moreover, many retail investors expect, and incorrectly believe, that financial professionals, including broker-dealers, are acting in a fiduciary type relationship of trust. In addition, because many broker-dealers are also investment advisers, this compounds the problem of investor confusion. These dual registrants "switch hats" when dealing with the same customers, thereby blurring the lines between investment advisory services and sales services.

The need for additional protection for investors is highlighted by the March, 2018 Federal appeals court decision vacating the Department of Labor's Fiduciary Rule (DOL Fiduciary Rule), and the April, 2018 SEC proposal of Regulation Best Interest, in response to the 913 Study. The Department of Labor, under its authority to promulgate rules under the Employee Retirement Income Security Act of 1974 (ERISA), [29 U.S.C. §§ 1001](#) et seq., and [26 U.S.C. § 4975](#), sought among other things, to update the definition of investment-advice fiduciary (first promulgated in 1975) to provide additional protections for employee benefit plans, and their participants and beneficiaries. The Department of Labor's initiative considered the dramatic changes in retirement plans and accounts since ERISA's enactment, notably the shift from pension plans controlled by large employers and money managers to individual retirement accounts (IRAs) and retirement plans directed by participants, such as 401(k)s. The DOL Fiduciary Rule brought under its umbrella those financial and insurance professionals who do business with ERISA plans and IRA holders, including those who did not provide advice on a "regular" basis. While the rule survived initial challenges, the United States Court of Appeals for the Fifth Circuit reversed the district court for Northern Texas and vacated the rule, holding, among other things, that the Department of Labor acted beyond its express statutory authority in crafting its rule by expanding the definition of investment-advice fiduciary.

The SEC's response to the 913 Study similarly compels the Bureau to take action to protect New Jersey investors. Several commenters to the pre-proposal requested that the Bureau not proceed with its rulemaking until the SEC adopts the "Regulation Best Interest," which requires all broker-dealers and agents to act in the best interest of retail customers when making a recommendation of any securities transaction or investment strategy involving securities to retail customers. The Bureau has been monitoring and reviewing the SEC's rulemaking process, including the comments submitted to the SEC. As several commenters to the pre-proposal noted, the proposed SEC standard is greater than that of the suitability rule but is less than that of a fiduciary duty. The Bureau believes that the SEC Regulation Best Interest does not provide sufficient protections for New Jersey investors. The Bureau believes that imposing a fiduciary duty standard for broker-dealers, investment advisers, agents, and investment adviser representatives protects investors against the abuses that can result when financial professionals place their own interests above those of their customers, will help to reduce investor confusion, and will work to foster

public confidence in the financial profession. Accordingly, the Bureau determined to proceed with this rulemaking at this time.

The Bureau proposes to amend the Bureau's existing suitability standard for broker-dealers and agents at [N.J.A.C. 13:47A-6.3\(a\)](#)<sup>3</sup> to add an exception for when the fiduciary duty proposed at N.J.A.C. 13:47A-6.4 applies. In addition, the Bureau proposes to amend the rule to include recommendations for the "opening of or transfer of assets to any type of account," which is commonly understood to be encompassed as part of an investment strategy.

Proposed new N.J.A.C. 13:47A-6.4 establishes as a dishonest or unethical business practice, failing to act in accordance with a fiduciary duty to a customer when providing investment advice or recommending to a customer an investment strategy, the opening of or transfer of assets to any type of account, or the purchase, sale, or exchange of any security. In accordance with the common law definition of fiduciary duty, both the duty of care and duty of loyalty must be satisfied. The rule sets forth to whom the duty is owed and the duration for which the duty is owed. In addition, the rule allows for transaction-based fees if certain conditions are met. The Bureau notes that, in accordance with the subchapter definitions as set forth at [N.J.A.C. 13:47A-6.2](#), when the Bureau refers to "adviser" at N.J.A.C. 13:47A-6.4 the term "adviser" includes both investment adviser as defined in [N.J.S.A. 49:3-49\(g\)](#) and investment adviser representative as defined in [N.J.S.A. 49:3-49\(s\)](#).

Proposed new N.J.A.C. 13:47A-6.4(a)1 specifies that for a broker-dealer, or its agent, failing to act in accordance with a fiduciary duty to a customer when making a recommendation or providing investment advice is a dishonest or unethical business practice. As set forth in subsection (a), a recommendation includes one for an investment strategy, the opening of or transfer of assets to any type of account, or the purchase, sale, or exchange of any security. Subparagraph (a)1i states that when making a recommendation, the fiduciary duty obligation extends through the execution of the recommendation and shall not be deemed an ongoing obligation. To address the concerns over dual registrants "switching hats" when dealing with the same customer and the resulting investor confusion, the Bureau proposes subparagraph (a)1ii, to state that if a broker-dealer or agent also provides, in any capacity, investment advice to the customer, the fiduciary duty obligation is an ongoing obligation to that customer. The fiduciary duty will be applicable to the entire relationship with the customer, regardless of the security account type. Paragraph (a)2 provides that it is a dishonest or unethical business practice if an adviser, or a broker-dealer or its agent who has discretionary authority over the customer's account or a contractual fiduciary duty, or who is acting as an adviser, fails to act in accordance with a fiduciary duty to a customer when providing investment advice.

Proposed new N.J.A.C. 13:47A-6.4(b) provides that, to meet the fiduciary duty, a broker-dealer, agent, or adviser shall satisfy both the duty of care and duty of loyalty. Paragraph (b)1 sets forth the common law duty of care. Subparagraph (b)1i specifies that, for purposes of the duty of care, the broker-dealer, agent, or adviser must make reasonable inquiry, including risks, costs, and conflicts of interest related to the recommendation or investment advice, and the customer's investment objectives, financial situation, and needs, and any other relevant information. Paragraph (b)2 sets forth the common law duty of loyalty, such that the recommendation or the advice is made without regard to the financial or any other interest of the broker-dealer, agent, adviser, any affiliated or related entity and its officers, directors, agents, employees, or contractors, or any other third-party. The Bureau is concerned about harmful incentives, such as sales contests, that encourage and reward conflicted advice. Accordingly, subparagraph (b)2i establishes a presumption of a breach of the duty of loyalty for offering or receiving direct or indirect compensation to or from the broker-dealer, its agent, or adviser for recommending the opening of or transfer of assets to a specific type of account, or the purchase, sale, or exchange of a specific security that is not the best of the reasonably available options. The Bureau also proposes new subparagraph (b)2ii to specify that there is no presumption that disclosing a conflict of interest in and of itself will satisfy the duty of loyalty. In its testimony before the SEC's Investor Advisory Committee meeting on the proposed Regulation Best Interest and Customer Relationship Summary Form, the AARP noted: "Recent behavioral science studies have shown that disclosures are largely ineffective because they tend to increase conflict in advisers and make the investor more likely to trust the adviser and thus follow biased advice. [(citing Sunita Sah, Gray Matter: The Paradox of Disclosure, NEW YORK TIMES, July 8, 2016; Sunita Sah and George Loewenstein, Nothing to Declare: Mandatory and

Voluntary Disclosure Leads Advisors to Avoid Conflicts of Interest, 25(2) PSYCHOL. SCI. 575-584 (2014); cf. Sunita Sah, Angela Fagerlin, and Peter Ubel, Effect of physician disclosure of specialty bias on patient trust and treatment choice, <http://www.pnas.org/content/113/27/7465.full.pdf>.)] Indeed, simply disclosing conflicts does not provide adequate protection and does not shield investors from potential financial harm of conflicted advice. Disclosure may even have unintended effects, such as making a consumer more confident that a financial professional is meeting a higher standard than he or she actually may be meeting."

[page=495] Proposed N.J.A.C. 13:47A-6.4(b)3 allows, notwithstanding the presumption set forth at subparagraph (b)2i, for a broker-dealer or agent to receive a transaction-based fee provided that the fee is reasonable and is the best of the reasonably available fee options for the customer, and the duty of care is satisfied. The requirement that the fee is reasonable, is consistent with existing Bureau rule, [N.J.A.C. 13:47A-6.3\(a\)](#)12, which sets forth as a dishonest or unethical business practice, charging unreasonable and inequitable fees for services performed.

Proposed new subsection (c) sets forth the individuals and entities that are excluded from being deemed a "customer." For purposes of N.J.A.C. 13:47A-6.4 a customer would not include: a bank, savings and loan association, insurance company, or registered investment company; a broker-dealer registered with a state securities commission (or agency or office performing like function); an investment adviser registered either with the SEC under Section 203 of the Investment Advisers Act of 1940 or with a state securities commission (or agency or office performing like function); or any other person (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$ 50 million.

New N.J.A.C. 13:47A-6.4(d) provides that the provisions at N.J.A.C. 13:47A-6.4 do not apply to a person acting in the capacity of a fiduciary to an Employee Benefit Plan, its participants, or beneficiaries, as those terms are defined in ERISA, [29 U.S.C. §§ 1001](#) et seq.

New N.J.A.C. 13:47A-6.4(e) states that nothing in N.J.A.C. 13:47A-6.4 shall be construed to establish any capital, custody, margin, financial responsibility, making and keeping of records, bonding, or financial or operation reporting requirements for any broker-dealer or agent of any broker-dealer that differ from, or are in addition to, the requirements established under [15 U.S.C. § 78o](#)(i).

To allow broker-dealers, their agents, or advisers time to implement the Bureau's new rule, the Bureau is proposing at N.J.A.C. 13:47A-6.4(f) that the operative date for the new rule to be 90 days after the effective date of the rulemaking.

As the Bureau has provided a 60-day comment period on this notice of proposal, this notice is exempted from the rulemaking calendar requirement pursuant to [N.J.A.C. 1:30-3.3\(a\)](#)5.

### **Social Impact**

The Bureau believes that proposed new rule N.J.A.C. 13:47A-6.4 will have a positive social impact upon the public by increasing confidence in financial professionals and ensuring that investors are protected against the abuses that can result when financial professionals place their own interests above those of their customers, regardless if investing with a broker-dealer or an investment adviser. The Bureau also believes that the proposed amendment and new rule will have a positive effect upon members of the regulated community by clarifying their obligations and responsibilities under the State securities laws.

### **Economic Impact**

The Bureau believes that the proposed amendment to [N.J.A.C. 13:47A-6.3\(a\)](#) will not have any economic impact because it is providing further guidance concerning the existing suitability standard.

Proposed new N.J.A.C. 13:47A-6.4 may have an economic impact on broker-dealers and may indirectly impact broker dealer agents, investment advisers, and investors. The Bureau believes that any increased costs are outweighed by the interest in protecting the welfare of investors.

To the extent broker-dealers choose to modify written policies and procedures or provide training to their employees, the proposed new rule will have an economic impact upon broker-dealers. The costs will vary depending upon a firm's existing business practices with respect to disclosure and conflict mitigation activities to comply with existing requirements. In addition, to the extent that broker-dealers are currently able to generate revenues from securities recommendations that are consistent with FINRA's suitability rule but are not consistent with the proposed fiduciary duty standard, those revenues would be impacted. The proposed new rule may require broker-dealers to engage the professional services of attorneys to ensure they comply with the proposed new rule. The costs associated with engaging professional services of attorneys are difficult to estimate, and they will vary depending upon the amount of work that each registrant will require and the rate that the professional will collect for his or her services.

To the extent the proposed new rule impacts financial incentives or bonus programs for financial professionals to recommend proprietary products and services over third-party or non-proprietary products, or the types of accounts in which they enroll their customers, may impact broker-dealer agents' financial compensation. The impact is difficult to estimate because the amount of financial professionals' compensation varies and there are different compensation models.

The Bureau notes that in April 2016, the Department of Labor adopted a fiduciary rule in connection with services for retirement accounts. Although in March 2018, the DOL Fiduciary Rule was vacated by the United States Court of Appeals for the Fifth Circuit, a July 2017 survey of broker-dealers reflected that to comply with the DOL Fiduciary Rule many of the survey participants had already implemented changes to both retirement and non-retirement accounts. Accordingly, to the extent broker-dealers have already implemented changes to comply with the now vacated DOL Fiduciary Rule, the economic impact associated with the Bureau's proposed new rule will be reduced.

The Bureau also believes that the proposed new rule may have an indirect economic impact on investment advisers to the extent the proposed new rule impacts the competitive market for the provision of investment advice.

The proposed new rule may also have an indirect economic impact on investors to the extent broker-dealers determine they no longer wish to make certain recommendations and choose to forgo some of the revenue stream associated with such recommendations. Broker-dealers, for compliance or business reasons, may determine to avoid certain products or account types, despite the fact that those products or account types may be beneficial to certain customers in certain circumstances. In addition, the proposed new rule may decrease incentives of agents to expend effort in researching products or account types and, therefore, may impose a cost on customers if there is a decline in the quality or variety of recommendations.

In at least one study published in the Journal of Financial Planning, "The Impact of the Broker-Dealer Fiduciary Standard on Financial Advice" by Michael Finke, Ph.D., CFP, and Thomas P. Langdon, J.D., LL.M., CFP, CFA, the study's authors explored the proposed application of a universal fiduciary standard and the impact on the financial adviser industry. The study surveyed registered representatives of broker-dealers in states that impose a fiduciary duty on the provision of investment advice to retail investors, and in states that do not impose such a duty. The authors concluded the following: "Empirical results provide no evidence that the broker-dealer industry is affected significantly by the imposition of a stricter legal fiduciary standard on the conduct of registered representatives. The opposition of the industry to the application of stricter regulation suggests that agency costs that exist when brokers are regulated according to suitability are significant. Imposition of a universal fiduciary standard among financial advisers may result in a net welfare gain to society, and in particular to consumers who are ill-equipped to reduce agency costs on their own by more closely monitoring an adviser with superior information, although this will likely occur at the expense of the broker-dealer industry. These results provide evidence that the industry is likely to operate after the imposition of fiduciary regulation in much the same way it did prior to the proposed change in market conduct standards that currently exist for brokers."

The Bureau believes that the proposed new rule may also have a positive economic impact on customers. According to a 2015 analysis by the United States Economic Council of Advisers, conflicted advice costs Americans about \$ 17 billion in foregone retirement earnings each year. The analysis also stated that the prevalence of conflicted payments may actually interfere with low-balance savers' ability to get advice. The analysis noted that

ongoing developments in the financial industry are sharply reducing the cost of advice, but it may be difficult for new entrants providing quality, unconflicted, low-cost advice to compete on price when other advice erroneously appears to be free. The analysis further states that, therefore the prevalence of hidden fees and conflicted payments may make it more difficult for low-cost, high-quality alternatives to compete on a level playing field, reducing moderate-income Americans' available options for inexpensive advice. In addition, as a result of the competitive [page=496] nature of the industry, to retain business, firms may lower the costs to clients. The Bureau also believes that investors may save money in terms of investment choices. Under a fiduciary duty, broker-dealers will now have to offer the lower-cost, similar investment option, which will potentially generate savings for investors.

The Bureau believes that any increased costs to broker-dealers, agents, investment advisers, investment adviser representatives, or to investors, are outweighed by the interest in protecting the welfare of investors and instilling greater confidence in the industry.

### **Federal Standards Analysis**

With respect to investment advisers and investment adviser representatives, proposed new N.J.A.C. 13:47A-6.4 does not exceed Federal standards. The proposed new rule will exceed generally understood Federal standards with respect to broker-dealers and agents. The Bureau believes that this heightened standard is necessary to ensure the protection of New Jersey investors.

Although FINRA is not a government entity, it is subject to Federal oversight by the SEC, which reviews and approves all of FINRA's rules. As such, FINRA's suitability rules for broker-dealers and agents may be viewed as imposing a Federal standard.

In addition, the SEC is currently engaged in Regulation Best Interest rulemaking to require all broker-dealers and agents to act in the best interest of retail customers when making a recommendation of any securities transaction or investment strategy involving securities to retail customers. As several commenters have noted in their comments to the SEC's proposed Regulation Best Interest, this standard is purportedly greater than that of the suitability rule but is less than that of a fiduciary duty. Accordingly, should the SEC adopt Regulation Best Interest, the Bureau's proposed new rule will exceed this standard.

The Bureau believes that the proposed new rule is necessary to ensure that persons involved in the securities markets are held to a uniformly high standard in their dealings with the general public and are necessary to ensure the welfare of New Jersey investors.

### **Jobs Impact**

The Bureau does not believe that the proposed amendment and new rule will result in the creation or the loss of jobs in the State.

### **Agriculture Industry Impact**

The Bureau does not believe that the proposed amendment and new rule will have any impact on the agriculture industry of the State.

### **Regulatory Flexibility Analysis**

As of January 1, 2019, there were approximately 2,050 broker-dealers, 200,800 agents, 3,230 investment advisers, and 29,730 investment adviser representatives registered with the Bureau. If such registrants are considered "small businesses" within the meaning of the Regulatory Flexibility Act, [N.J.S.A. 52:14B-16](#) et seq., then the following analysis applies.

The proposed amendment at [N.J.A.C. 13:47A-6.3\(a\)3](#) does not impose any new compliance requirement as it is codifying the generally understood suitability standard. Proposed new rule N.J.A.C. 13:47A-6.4 imposes new compliance requirements, which are discussed in the Summary above. The proposed amendment and new rule do

not impose any new recordkeeping or reporting requirements. The costs associated with the proposed amendment and new rule are discussed in the Economic Impact statement. The proposed new rule may require registrants to engage the professional services of attorneys to ensure they comply with the proposed new rule. The costs associated with engaging professional services of attorneys are difficult to estimate, and they will vary depending upon the amount of work that each registrant will require and the rate that the professional will collect for his or her services.

The Bureau is proposing the amendments and new rule to protect the welfare of the investing public. The rules will apply to all members of the regulated community. Therefore, no differing compliance requirements for any registrant is provided based upon the size of the business.

### **Housing Affordability Impact Analysis**

The proposed amendment and new rule will have an insignificant impact on the affordability of housing in New Jersey and there is an extreme unlikelihood that the amendment and new rule would evoke a change in the average costs associated with housing because the rules concern the dishonest or unethical business practices of State registered securities professionals.

### **Smart Growth Development Impact Analysis**

The proposed amendment and new rule will have an insignificant impact on smart growth and there is an extreme unlikelihood that the amendment and new rule would evoke a change in housing production in Planning Areas 1 or 2, or within designated centers, under the State Development and Redevelopment Plan in New Jersey because the rules concern the dishonest or unethical business practices of State registered securities professionals.

### **Racial and Ethnic Community Criminal Justice and Public Safety Impact**

The Bureau has evaluated this rulemaking and determined that it will not have an impact on pretrial detention, sentencing, probation, or parole policies concerning adults and juveniles in the State. Accordingly, no further analysis is required.

## **Regulations**

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**Full text** of the proposal follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

### SUBCHAPTER 6. DISHONEST OR UNETHICAL BUSINESS PRACTICES

13:~~47A~~-6.3 Examples of dishonest or unethical practices for broker-dealers, agents, issuer-agents, advisers, and internet site operators

(a) "Dishonest or unethical practices" as used in [N.J.S.A. 49:3-47](#) et seq., specifically in [N.J.S.A. 49:3-53\(a\)\(3\)](#) and [49:3-58\(a\)\(2\)\(vii\)](#), shall include the following:

1.-2. (No change.)

3. [Recommending] **Except as provided at N.J.A.C. 13:47A-6.4, recommending** to a customer, an investment strategy, **the opening of, or transfer of assets to, any type of account**, or the purchase, sale, or exchange of any security or securities without reasonable grounds to believe that such strategy, transaction, or recommendation is suitable for the customer based upon reasonable inquiry concerning the customer's investment objectives, financial situation, and needs, and any other relevant information known by the broker-dealer;

4.-64. (No change.)

### **13:47A-6.4 Fiduciary duty of broker-dealers, agents, and advisers**



(a) "Dishonest or unethical business practices" as used at [N.J.S.A. 49:3-47](#) et seq., specifically at [N.J.S.A. 49:3-53\(a\)\(3\)](#) and [49:3-58\(a\)\(2\)\(vii\)](#), shall include providing investment advice or recommending to a customer, an investment strategy, the opening of, or transfer of assets to, any type of account, or the purchase, sale, or exchange of any security when:

1. A broker-dealer, or its agent, fails to act in accordance with a fiduciary duty to a customer when making a recommendation or providing investment advice.

i. When making a recommendation, the fiduciary duty required in (a)1 above shall extend through the execution of the recommendation and shall not be deemed an ongoing obligation, except as provided in (a)2 below.

ii. If a broker-dealer or agent also provides, in any capacity, investment advice to the customer, the fiduciary duty shall be deemed an ongoing obligation to that customer.

2. An adviser, or a broker-dealer or its agent who is acting as an adviser, has discretionary authority over a customer's account or a contractual fiduciary duty, fails to act in accordance with a fiduciary duty to a customer when providing investment advice.

(b) To meet the fiduciary duty, a broker-dealer, agent, or adviser shall satisfy both the duty of care and duty of loyalty.

1. When making a recommendation or providing investment advice, the duty of care requires a broker-dealer, agent, or adviser to use the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use taking into consideration all of the facts and circumstances.

[page=497] i. For purposes of this paragraph, a broker-dealer, agent, or adviser shall make reasonable inquiry, including risks, costs, and conflicts of interest related to the recommendation or investment advice, and the customer's investment objectives, financial situation, and needs, and any other relevant information.

2. When making a recommendation or providing investment advice, the duty of loyalty requires that a recommendation or the advice is made without regard to the financial or any other interest of the broker-dealer, agent, adviser, any affiliated or related entity and its officers, directors, agents, employees, or contractors, or any other third-party.

i. There shall be a presumption of a breach of the duty of loyalty for offering, or receiving, direct or indirect compensation to or from the broker-dealer, its agent, or adviser for recommending the opening of, or transfer of assets to a specific type of account, or the purchase, sale, or exchange of a specific security that is not the best of the reasonably available options.

ii. There shall not be a presumption that disclosing a conflict of interest in and of itself shall satisfy the duty of loyalty.

3. Notwithstanding the presumption set forth at (b)2i above, it shall not be deemed a breach of the fiduciary duty owed to a customer when the broker-dealer or agent receives a transaction-based fee, provided that the fee is reasonable and is the best of the reasonably available fee options and the duty of care is satisfied.

(c) For purposes of this section, a "customer" shall not include:

1. A bank, savings and loan association, insurance company, or registered investment company;

2. A broker-dealer registered with a state securities commission (or agency or office performing like function);

**3. An investment adviser registered either with the SEC under Section 203 of the Investment Advisers Act of 1940 or with a state securities commission (or agency or office performing like function); or**

**4. Any other person (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$ 50 million.**

**(d) Nothing in this section shall be construed to apply to a person acting in the capacity of a fiduciary to an employee benefit plan, its participants or beneficiaries, as those terms are defined in the Employee Retirement Income Security Act (ERISA), [29 U.S.C. §§ 1001](#) et seq.**

**(e) Nothing in this section shall be construed to establish any capital, custody, margin, financial responsibility, making and keeping of records, bonding, or financial or operation reporting requirements for any broker-dealer or agent of any broker-dealer that differ from, or are in addition to, the requirements established under [15 U.S.C. § 78o\(i\)](#).**

**(f) The provisions of this section shall take effect on (90 days from the effective date of this new rule).**

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