# "Fiduciary"? — Take a Step Back, and a Step Up

## Where Wealth, Health, Care & Legacy Intersect

"*Best interest means best interest, if you're asking a lawyer if something is over the line, maybe it's time to step back from the line."* – Gary Gensler, Chairman SEC

**A Fiduciary Relationship**

The reality is Best Interest (BI), in fact meets the definition of fiduciary, regardless of how many seed splitting lawyers dance on pin heads. A fiduciary owes their beneficiary a duty of undivided loyalty, i.e., Best Interest.

Miriam-Webster defines a fiduciary relationship is one in which one party places special trust, confidence, and reliance in and is influenced by another who has a fiduciary duty to act for the benefit of the party.

Typical fiduciary relationships exist between agents and principles, attorneys and clients, executors or administrators and legatees or heirs, trustees and beneficiaries, corporate directors or officers and stockholders, receivers or trustees in bankruptcy and creditors, guardians and wards, and confidential advisors of those advised. In other words, give the best advice possible, based on all they know or can access, just as they would a family member.

*Nowhere is the definition of a fiduciary relationship limited to a financial relationship, arrangement, portfolio, or product.*

It is worth noting that the Hippocratic oath expresses the essence of the fiduciary relationship between a physician and each of its patients. The concept of "do no harm to patients medically or personally" dates back to the 5th century CE. The concept is a broad one, not limited to medicine. Today that additional 'personal' responsibility is expressed as a commitment to elevate their conduct above that of commercial actors.[1] Doctors recognize that their specialized medical advice cannot operate independent of other medical advice, and that they have a broader personal responsibility to the patient.

*Doctors don't restrict "holistic" to their own medical silo. It includes an inextricable connection throughout the entire body (physical, behavioral, social, psychological) and onto a patient's family.*

They recognize their limitations can give rise to unintentional harm. Consequently, they are comfortable handling second opinions. They regularly refer to others within and outside their own silo of expertise – both within their practice or system, and outside of it. By doing so, they eliminate unintentional conflicts that arise from their own limitations and that give rise to harm.

*A fiduciary relationship is intended to eliminate (not mitigate) conflicts of interest*

[1] It is important to note, while doctors have a fiduciary responsibility the core of their business is not financial. The same is not true of the hospitals (provider systems) and health insurance companies (payors).

**A Fiduciary Responsibility**

*A fiduciary responsibility or duty is less than, and not equal to, a fiduciary relationship.*

The Prudent Man Rule crystallized the legal concept of a fiduciary responsibility in the context of Trust Law in 1830. It directed trustees to invest with prudence, discretion, and intelligence to meet the needs of beneficiaries, preserve the corpus of the trust, and provide regular income. The legal concept was applied to managing the asset of a Trusts in a conservative fashion.

In the face of large, global, and complex markets, increasingly sophisticated investors, and a proliferation of investment products, the Prudent Person Rule evolved to a more liberal one. It still expects rational, intelligent decisions and investment choices on behalf of the client. However, the choices are guided by the client's investment mandate or policies, which may not be conservative, generate income, or preserve a corpus. Also, the client may be an individual, corporation, or plan.

**Why the Distinction Between the Two Is Important?**

Trusts also evolved well beyond personal trusts to enable concentrated corporate ownership to exert monopoly pricing power. The pendulum swung against those Trusts from 1892 to 1933 as numerous Acts were passed to separate a variety of corporations and functions.

The Banking Act of 1933 (Glass-Steagall Act) separated commercial from investment banking. Insurance was already separate, and regulation was ultimately turned over to the States by the McCarran Ferguson act in 1945. This effectively exempted them from the Sherman Antitrust Act for purposes pooling risk rating data, while effectively restricting their size and pricing power.

*With the separation of banking, investment, and insurance the three industries redefined how fiduciary responsibility applies to each of their businesses.*

Financial services, in this country, are fragmented across the three silos, and further fragmented within each industry silo. Banking broke into Trust, Commercial, and Retail. Insurance broke into Life, Health, and Property-Casualty. Securities broke into Investment Banking, Trading, Retail Sales and Investment Advisory.

Some silos continued to assume a fiduciary duties and responsibility, others did not. Conflicts of interest are widespread.

**Commercial Bank**

- Trust investment managers are guided by the "Prudent Person Rule", while Trust Officers may have a full fiduciary relationship with a client.
- Commercial Lenders' fiduciary duty is to protect the quality bank's loan portfolio yet represents the borrower to the bank.
- Retail Bankers are salespeople, with no fiduciary responsibility. They sell loans and deposits at rates to help their bank maintain a profitable spread.

**Investment Bank**

- Investment Bank's fiduciary duty derives from its contracts with the issuers it brings to market.
- Traders have a duty to the firm to manage their trading book within the trading policies and risk limits of the firm.

- Retail Securities Sales had operated under a “suitability” standard, avoiding fiduciary duty. Now they are required to operate under a “Best Interest” standard.

**Insurance Company**

- Insurance Agents sell and manage policies on behalf of the insurance company. Any fiduciary liability falls to the company
- Insurance Brokers are agents, who have a fiduciary duty to uphold an agreed standard of care, (specifically if agreed in contractual form).
- Insurance (Benefits) Consultants are contracted and hired (usually by employers) and have a fiduciary duty to those employers, despite the possibility of compensation by the insurance company.
- Life Insurance Producers are agents of the company(s) yet owes “allegiance” to and represents the insured to the company(s).
- Variable Annuity salespeople and subject to the same “Best Interest” duty as Retail Securities Representatives
- Fixed Annuity salespeople are bound only by a Suitability Standard.

Medicare and other Public Health Insurance is generally not subject to a fiduciary standard. Instead, they are regulated and standardized, eliminating the potential for conflict of interest.[2] The private sector sponsored Medicare supplements are sold by agents, who do not have fiduciary liability.[3]

*The financial services industry successfully used siloed fragmentation within all three core silos (banking securities and insurance) to limit the application of a fiduciary duty and proscribe fiduciary relationships.*

Tailoring the scope of fiduciary responsibility to the product and distributor was successful for decades because there was a simple, clear definition of roles for public facing personnel — and the public understood it.

Insurance agents were salespeople who sold insurance. Brokers were traders and salespeople who bought and sold securities. Retail banks took deposits and made mortgage loans.

Trust banks and Investment Advisors were fiduciaries who provided estate planning and investment advice to wealthy, generally sophisticated, families. Commercial and Investment banks catered to corporations and didn’t talk to the public. Tellers took deposits and branch managers (often Presidents) made loans to neighbors.

Financial planning in the current sense did not exist. There was no expectation of unconflicted advice other than the specialized advice of investment advisors and trust officers — neither of whom dealt with the public at large.

[2] A Medicare Advantage plan’s salespeople typically avoid potential conflicts by limiting their discussion to only their employers plan. Instead, they refer all other questions to Medicare.gov.

[3] Fiduciary responsibility is less important for standardized Medicare Supplement insurance than agents’ ability to access and represent all potential carriers.

**The Pendulum Swings Back!**

From the Glass-Steagall Act in 1932 up through the deregulation of brokerage commissions on May 1, 1975, that clarity held. It was a regulatory construct that took years to build. It is also taking years to break down.

Commission deregulation put pressure on the securities industry. Gradually one barrier after another came down as siloed industries started "playing in each other's sandboxes". Inflation and the advent of money market funds put pressure on the banking industry. The banking industry began selling securities, mutual fund, fixed annuity and insurance products in their formidable branch networks. Insurance companies bought brokerage firms to gain distribution. All faced pressure to consolidate, gain scale, and increase volume.

*Scale is a voracious beast. It requires an ever-increasing share of the less sophisticated, less wealthy public.*

Then the Gramm-Leach-Bliley Act removed the remnants of the Glass-Steagall Act in 1999, and silos could not just play in other sandboxes, all could also acquire substantial players in other silos.

One year later, in 2000 and independent of the GLB Act, the Financial Planning Association was created[4] That event was a tipping point[5]. The model was a successful one. It evolved past portfolio management or cash flow and allocation analytics to justify a product sale.

Now it spans all financial industry silos, products, and services. It weaves together assets, liabilities, income, expenses, cash flow, and tax planning. Its goals are to fund education, capital acquisitions, business interests, health, care, and legacies. It adjusts over lifetimes and generations. Then a CRM, with all its personal information, was tied like a bow around the entire package.

*Comprehensive financial planning[6] as a sophisticated profession was the model, a fiduciary relationship its differentiating proposition, and it succeeded because of the value it adds.*

It added the value necessary to support RIAs fee-based revenue stream when faced with passive investments, indexing, and robo-advice. The concurrent spread of 12b-1 fees in the mutual fund industry also generated fees based on assets under management rather than sales commissions alone. Those ongoing fees require demonstrable service to justify them, and a financial planning service met that requirement.

This created a situation where large swaths of the financial services industry wished to be seen as "providing financial planning". The service had numerous monikers, Retirement Specialist, Retirement Planners, Retirement Experts, Annuity Specialist, and simply Financial Advisor, Financial Planner, or

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[4] The FPA was the result of merging the of Institute of certified financial planners (ICFP) in the international Association of financial planners (IAFP). The role of financial planning was a central distinction between them.
[5] The seminal moment occurred December 12, 1969, at a meeting in Chicago that outlined the idea that people could benefit from a profession which integrated knowledge and practices across the various areas of the financial services industry.
[6] George Kinder is widely viewed as the father of the life-planning movement, heralding an era in which financial advisers intertwine ideas of human emotion with financial decision-making

Financial Advisor. (Investment and Portfolio Manager receded into the background, and "salesperson" never mentioned!)

*However, there were differences: RIA's have a fiduciary duty (at a minimum), mutual fund retailers may or may not have some duty, and fixed annuity salespeople had no duty at all.*

The public did not appreciate the distinction, but the Department of Labor did. ERISA stipulates a plan sponsor has a fiduciary duty. It recognizes the money belongs to the participants, not the plan. That duty flows through to the participants in the plan. Participants in the plan were employees – aka the Public.

**Where are we now?**

The past two decades ended the longest expansion in US history with a succession of crises: a dot-com bubble, a mortgage crisis, and a health crisis. The financial crises teach us about volatility, and how little we know about markets. What we do know is that speculation permeates it.[7]

The health crisis taught us a great deal about the fragility of our health system and our population. Despite Medicare expansions, the ACA, Medicaid expansions, and strong Covid response, individuals are more concerned about the cost of health and care than ever. It looms large, it is unpredictable, and it is extremely complex.

The community-based nonprofit hospitals and health systems (providers) of the last century have been absorbed into large regional and national for-profit health systems. Those systems in turn, are dependent on large, national, private sector health insurance companies (payors). Both have a fiduciary duty to shareholders, and conflicting incentives which put patients (clients) in the middle.

The cadence of baby boomers crossing age 65 changed the mantra of retirement planning from accumulation to income and distribution. The financial services industry saw the death of the corporate pension plan and the rise of individually funded defined contribution plans. As more employees became investors, the DOL pointed out to all, that anyone touching that money had a fiduciary duty.

The industry may well see a decline and disappearance of employer-sponsored health plans. The process is already underway as employers offer higher deductible plans coupled with HSA's, MSAs, and access to the ACA. ERISA already establishes a fiduciary responsibility for employers that covers benefit plans.

*ERISA does not distinguish between types of benefits when it comes to employee's money.*

To the extent benefit plans funding and decisions devolve to employees, the DOL is likely to point out the same fiduciary relationship does as well.

**Where to go from here, A Middle Road?**

The fiduciary relationship is not determined by the amount of money involved. It is determined by what that money means to the individual whose money it is.  As firms create scale, it drives them to seek more *clients at different wealth strata who also merit a fiduciary relationship*, and one that they can deliver if they choose to.

[7] The Robin Hood business model is the primary example of both high levels of speculation and inherent conflict with its revenue model that relies on selling clients order flow.

As employer-provided benefits devolve to employees, advisors (of any type) who advise on choosing or funding any or all benefits *assume the employer's fiduciary duties at the same time*.

The SEC is clearly telling the part of the financial services industry it regulates: Best Interest is at a minimum a fiduciary duty, *that it goes beyond the Prudent Person Rule*, and that they are responsible.

Some Financial Planners and RIAs hold themselves out broadly as fiduciaries, either in fact, or in effect. The more comprehensive the plan they offer, the broader the fiduciary relationship is. If a financial plan includes costs and family members[8], it needs to provide the same level of attention to those details as it does to the AUM which determine how much they get paid. Recipients will expect it. They should not have to ask: *Is your advice based on all you know or can access*?

No advisor, regardless silo, can be unaware of the role health, care, employer benefits, and family security all play in every financial plan. They have already lived through too much.

Rather than exert effort to limit fiduciary liability to fit an advisor or firm's convenience, it is time look at the medical model – "Do no harm, medically or personally". It isn't difficult with a capable and competent team, a willingness to refer, and comfort with second opinions.[9]

The GP quarterbacks medical care, and guides patients through the health system with an eye to their personal situation. *There is no reason a financial advisor can't – Do no harm financially or personally.*

It requires addressing conflicts of interest – frontally and simply,

1. Full Fiduciary Relationship – eliminate all conflicts of interest (even unintentional ones) which is what everyone wants.
2. Limited Fiduciary Duty – mitigate conflicts of interest for a specific service, which many people may settle for.
3. (Insert Product Name) Salesperson – explicitly declare "caveat emptor" for a specific product. Only self-directed people who do research and want to buy based on price quote need apply.

Any Firm or Advisor can succeed with one of the three approaches. They can even differentiate themselves. What they should not do, is continue to muddy the distinctions between them. Switching hats, cards, titles never worked – for any client – ever.

Rather than find ways to limit fiduciary roles of "facilitators" in every silo, for every product, in every state:

- Step Back: Make the distinctions crystal clear, as they once were.
- Step Up: Define a broad fiduciary that genuinely embraces a "holistic" financial plan.

It is what clients want, and what scale can enable.

*J. Heywood E. Sloane*

[8] The most risk-fraught and significant personal cost people face is the cost of maintaining or reclaiming health for themselves or their families.
[9] The unfortunate fact is historically a commission driven culture is highly competitive. Referring even within teams can impact compensation. Referring externally can impact compensation, and also risk losing an account.