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Regulating Best Interest: SEC Confronts the Brave New Markets

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This Note comments on how recent developments in securities regulation deal with today's securities industry challenges. As usual, the law advances much slower than technology.[1] *After decades of debate over heightened standards for broker-dealers giving investment advice, the Securities and Exchange Commission ("SEC") introduced Regulation Best Interest (Reg BI).*[2] *Our modern market demands that broker-dealers execute quick trades on behalf of their clients as well as provide broader investment advice. The popularity of online trading platforms ("OTPs") only exacerbated the need for regulatory changes. The theme of this paper surmises how Reg BI responds to the rise of the retail investor's trading app.*

Part II, the Introduction, will provide a brief history of the American brokerage business. This timeline will demonstrate how equities started out as a market only for the wealthy but eventually turned into an exchange where brokers compete for the everyday person's business.

Part III will then explore the SEC's issues with current securities providers. Part III(A) discusses the methods that OTPs use to

1 *See generally* Daniel Malan, *The law can't keep up with new tech. Here's how to close the gap*, WORLD ECON. FORUM, (June 21, 2018), https://www.weforum.org/agenda/2018/06/law-too-slow-for-new-tech-how-keep-up/_(explaining how fast technological change cannot rely only on government legislation because of redundancy at the time of implementation).

2 Kenneth E. Bentsen, Jr., *A Long Time in the Making, SEC's Regulation Best Interest Raises the Bar for Investor Protection*, SIFMA (June 30, 2020), https://www.sifma.org/resources/news/a-long-time-in-the-making-secs-regulation-best-interest-raises-the-bar-for-investor-protection/.

garner clients and bring in revenue. It will discuss how application designers use "gamification" to retain clients and encourage trading. Brokerages use a free-to-play system that encourages more trading through visual, process, and social media components. Part III(B) will explain the payment for order flow ("PFOF") model. OTPs allow clients to conduct "cost-free" trading on the OTP while still bringing in revenue for the brokerage. The practice of PFOF involves selling retail market order data to market makers.[3] After all, data is the new oil. In contrast to the expansive regulations in the oil and gas industry, however, Reg BI obligations show a more measured approach. Thus, consumers derive significant cost savings from PFOF even when retailers sell their order data to market makers who in turn sell securities to those same consumers. Part III(C) of this Note will provide insights into market interactions from a behavioral finance perspective. Behavioral finance studies show how OTPs subtly influence investor strategy, execution, and long-term goals. Studies show that the accessibility and visual appeal of online brokerage applications affects investor risk tolerance as well as trading patterns.[4] Firms want their customers to use as many of their applications as possible. The implication is that firms want customers to use their digital applications because then they can influence them to use premium features, other firm products, or engage in behavior that adds more value to the brokerage or its other lines of business.[5] These influences can lead to serious consequences for uninformed customers who cannot properly assess the firm's financial products or services.

After spending time on the technical aspects of OTPs, Part IV will review the history of stockbroker duties. Part IV(A) goes into common law fiduciary duties: stockbrokers maintained an agency relationship through contract. Thereafter, Part IV(B) discusses circumstances that turn a broker into a fiduciary. A popular analysis—the "trust and confidence test"—determines whether a stockbroker has a fiduciary duty to its customer. In addition to the trust and confidence test, courts look at other control factors to

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3 *See* Bill Alpert, *What Is Payment for Order Flow? Behind the Trading Controversy at Robinhood and Other Brokers.*, BARRON'S (Aug. 31, 2021), https://www.barrons.com/articles/payment-for-order-flow-robinhood-51623412441.

4 Julia Bayuk & Suzanne Altobello, *Can Gamification Improve Financial Behavior?*, 37 INT'L J. OF BANK MKTG. 951, 959 (2019).

5 *See id.*

determine whether to impose obligations on brokerages. In Part IV(C), this Note will also expound on the historical dichotomy between broker-dealers and financial advisers. Because brokers perform an increasingly enlarged advisory function, one must understand the different standards brokers and advisers are held to. The historical context gives an added justification for Reg BI's supplemental obligations to their customers.

Part V will opine on the new SEC rule that requires broker-dealers to only recommend financial products that are in their customers' best interests.[6] *Falling under the Securities and Exchange Act of 1934, Reg BI hopes to safeguard investors and standardize the conduct of broker-dealers who also provide financial advice.*[7] *This Note will discuss the benefits and criticisms of the new regulation.*[8] *For the most part, Reg BI adds needed reinforcement of securities laws while not overburdening broker-dealers.*

Ultimately, Part VI suggests that we should remain cautiously optimistic about such technologies. No doubt, the market should encourage fintech innovations. Consumer access to markets should remain a large priority given today's economic climate. Still, financial services remain a highly regulated industry because of the need to protect risk-bearing consumers.[9]

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6 17 C.F.R. § 240.15l-1 (2022).
7 *Id.*
8 *Id.*
9 *See* Kimberly Amadeo, *Financial Regulations Do Regulations Keep Your Money Safer?*, THE BALANCE, https://www.thebalance.com/financial-regulations-3306234#:~:text=Financial%20regulations%20protect%20consumers'%20investments,%2C%20financial%20markets%2C%20and%20consumers (Apr. 30, 2021).

I. INTRODUCTION

Gone are the days when the average man on the street must pay trading fees to buy stocks.

In an attempt to capture younger investors of more modest means, brokerages created easily accessible and intuitive OTPs. Unfortunately, these new investors jumped in with reckless abandon, unaware of the real-world consequences. Critics of such trading mediums accuse brokers of encouraging careless trading activity. The ease of access to trading applications from mobile devices contrasts starkly with how the equities markets functioned in the past. To meet changes in the markets, regulators will use Reg BI to lay the groundwork for how brokerages should treat their customers.

Historically, stock brokerages charged commissions through a fixed rate based on the share price and amount of shares purchased.[10] Investors purchased shares of stock in even lots or batches of 100 shares.[11] On May 1, 1975, commonly referred to as May Day, the SEC allowed brokerages to charge variable commission rates in contrast to the previous system where all brokerages charged the same price for trades.[12] Such deregulation decreased commissions, increasing the average retail investor's market participation.[13] While rates drastically lowered, broker-dealers gradually appeared online, resulting in further market accessibility. From there rose a new do-it-yourself investor class whose members conducted their own research while paying lower trading fees.[14] Investors trading on OTPs could now place trades in the market from the comfort of their personal devices.[15]

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10 Karl Kaufman, *How to Trade Stocks for Free*, FORBES (Feb 18, 2018), https://www.forbes.com/sites/karlkaufman/2018/02/18/how-to-trade-stocks-for-free/?sh=1b726c909680.
11 *Id.*
12 Cory Mitchell, *May Day*, INVESTOPEDIA, https://www.investopedia.com/terms/m/mayday.asp (Oct. 29, 2021).
13 *Id.*
14 *Id.*
15 Kaufman, *supra* note 10.

Today, we now have fierce competition between low-cost trading platforms and big-name brokerages for market share in the retail trading space.[16] As fees race to the bottom, an incredible amount of "small money" finds its way into the markets. Even amidst COVID-19 economic uncertainty, small money invested a record 500 billion dollars into the United States stock market by mid-2021.[17] The increase in American discretionary income has also brought more people into securities trading. As such, the SEC shows a similar uptick in regulatory enforcement actions.[18] Market misbehavior aside, the changes in consumer financial services contribute to a better customer experience overall.

II. THE SECURITIES AND EXCHANGE COMMISSION'S NEW CHALLENGES

The SEC encourages investors to trade only with registered entities. Should those registered violate federal securities law, government enforcers have avenues for penalties.[19] Despite the threat of SEC prosecution, complications still arise regarding broker-dealer or adviser behavior toward their clients. Retail investor platforms looking for new customers naturally market toward a younger audience.[20] While accumulating this customer base, the OTP encourages active trading as opposed to investing in safer options like index funds.[21] Unaware of their own inexperience in the market, these users liken their OTP purchases and sales of securities to that of a video game.[22]

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16 Kirsten Chang, *Battle for Client Assets Heats Up as Brokers cut Fees to Zero*, CNBC, (Oct. 14, 2019), https://www.cnbc.com/2019/10/13/battle-for-client-assets-heats-up-as-brokers-cut-fees-to-zero.html.

17 Emily Graffeo, *Retail Investors are on Pace to Sink a Record $1 Trillion into Stocks this Year - and the Flows Have Actually Accelerated Over the Past Month, JPMorgan says*, BUS. INSIDER (June 19, 2021), https://markets.businessinsider.com/news/stocks/stock-market-retail-investors-trillion-jpmorgan-trading-activity-levels-meme-2021-6.

18 Press Release, SEC, SEC Announces Enforcement Results for FY 2021 (Nov. 18, 2021), https://www.sec.gov/news/press-release/2021-238; *see also* Nick Stonnington, *How Democratization Is Paving A Path Of Continued Growth In The Stock Market*, FORBES (Mar. 3, 2021, 12:40 PM), https://www.forbes.com/sites/forbesbusinesscouncil/2021/03/03/how-democratization-is-paving-a-path-of-continued-growth-in-the-stock-market/?sh=4a868af497f1.

19 *Statement on Potentially Unlawful Online Platforms for Trading Digital Assets*, SEC (Mar. 7, 2018), https://www.sec.gov/news/public-statement/enforcement-tm-statement-potentially-unlawful-online-platforms-trading.

20 Derek Horstmeyer, *Robinhood Empower Young Investors not Take Advantage of Them*, YAHOO (Sept. 27, 2021), https://www.yahoo.com/now/robinhood-empower-young-investors-not-092900025.html.

21 *Id.*

22 See *id.*

Ameliorating the problem would require regulator heavy-handedness against brokers who insist on taking advantage of ignorant investors. However, a captivating user experience does not necessarily call for unadvisable speculation or high risk-taking.[23] OTPs maintain that no enticement occurs; they claim to facilitate trades with neutrality.[24] Neutrality in this context has a particular meaning: the OTPs maintain an agnostic position on price movements.[25] Your OTP has no opinion on whether you buy, sell, or hold.[26] Here, they follow the general practice—brokerages do often provide consulting, advisory, or strategic services in addition to an investment platform.[27] But less obvious, OTPs use subtle nudges within the investment application, impacting the behavior of users trading on the platform itself. Such influences are not readily transparent to the client.[28] These behavioral finance techniques encourage more trading than otherwise would occur.[29] Given the circumstances, regulators drew the elusive line between the faultless influence of a trading platform and culpable active encouragement.

Why the drive to boost trading on a commission-free platform? Broker-dealers using a commission-free model derive value through selling retail investor order information to market makers.[30] Market makers profit from playing two sides of the transaction.[31] In essence, the practice of market-making involves maintaining an inventory of shares or contracts and offering them both to buyers and sellers.[32] Market makers receive compensation based on the spread between the bid and ask

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23 *See* Yun Li, *SEC says Brokers Enticed by Payment for Order Flow are Making Trading into a Game to Lure Investors*, CNBC (Oct. 18, 2021), https://www.cnbc.com/2021/10/18/sec-says-brokers-enticed-by-payment-for-order-flow-are-making-trading-into-a-game-to-lure-investors.html.

24 *See Id.*

25 Adam Hayes, *Neutral*, INVESTOPEDIA (Dec. 23, 2020), https://www.investopedia.com/terms/n/neutral.asp.

26 *Id.*

27 Adam Hayes, *What Is a Brokerage Firm? How It Makes Money, and Types*, INVESTOPEDIA (May 1, 2022), https://www.investopedia.com/terms/b/brokerage-company.asp.

28 *See* David Ingram, *Designed to Distract: Stock App Robinhood Nudges Users to Take Risks*, NBC NEWS (Sept. 12, 2019), https://www.nbcnews.com/tech/tech-news/confetti-push-notifications-stock-app-robinhood-nudges-investors-toward-risk-n1053071.

29 Matt Levine, *The SEC Is Baffled By GameStop Too*, BLOOMBERG (Oct. 19, 2021), https://www.bloomberg.com/opinion/articles/2021-10-19/matt-levine-s-money-stuff-gamestop-baffles-the-sec-too.

30 Andrew Bloomenthal, *Market Maker*, INVESTOPEDIA (Aug. 31, 2021), https://www.investopedia.com/terms/m/marketmaker.asp.

31 *Id.*

32 Theresa Carey, *Payment for Order Flow (PFOF)*, INVESTOPEDIA (Dec. 3, 2021), https://www.investopedia.com/terms/p/paymentoforderflow.asp.

prices.[33] The "payment for order flow" ("PFOF") system potentially makes spreads of securities vulnerable to manipulation, as the order information gathered by market makers induces unfair play.[34] In a game of seconds, data given to "big money" beforehand makes these "free trades" cost a little bit more at the time of execution.[35] These market makers armed with that order information act without keeping the retail investor's best interests in mind.[36] Retail investors overpaying for trades exacerbates in the options markets because options order spreads are considerably wider—an advantageous position for the market maker.[37] While all of these deals occur between the market maker and the broker-dealer, the retail investor moves forward believing their commission-free platform gives the most value when in fact the broker engages in double-dealing.[38]

Ideally, firms should adhere to FINRA Rule 5310 to promote investor protection.[39] Rule 5310 requires that FINRA members "use reasonable diligence to ascertain the best market" for executing a trade with a price as favorable as possible under market conditions.[40] FINRA members, moreover, must review execution quality by comparing the trade execution achieved against the quality their customers might receive under non-PFOF routing arrangements.[41] Trying to obtain the best execution of trade with no fees proves quite difficult, but confirming a broker's FINRA membership at least provides an avenue to hold problematic actors accountable through arbitration.

Note that PFOF is not a new phenomenon. Firms began significantly routing orders to market makers in the 1990s. As noted in SEC Commissioner Richard Robert's remarks in 1993, PFOF transactions occurred as early as 1984.[42] For the sake of transparency, firms engaging in PFOF have to disclose such relationships under Rule 10b-10 of the Securities Exchange Act and Regulation National Market System ("Reg

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33 Akhilesh Ganti, *What Is a Bid-Ask Spread, and How Does It Work in Trading?*, INVESTOPEDIA (May 31, 2022), https://www.investopedia.com/terms/b/bid-askspread.asp (a bid-ask spread is the difference between the asking price and the offering price of a security or other asset).

34 *See* Carey, *supra* note 32.

35 *Id.*

36 *Id.*

37 *Id.*

38 See *Id.*

39 FINRA, RULE 5310 (2014).

40 *Id.*

41 *FINRA Clarifies Guidance on Best Execution and Payment for Order Flow*, KATTEN (July 28, 2021), https://katten.com/finra-clarifies-guidance-on-best-execution-and-payment-for-order-flow.

42 *See generally* SEC Comm'r Richard Y. Roberts, Address on Payment for Order Flow (Apr. 29, 1993), https://www.sec.gov/news/speech/1993/042993roberts.pdf.

NMS").[43] Under Rule 10b-10, brokers must indicate on customer confirmation statements when PFOF has been received for a trade. Brokers then notify customers that they may request information about the nature of the broker's compensation.[44] Under Reg NMS, Rule 606 mandates that brokers post quarterly reports on their websites, disclose the vendors they route orders to, and explain the PFOF arrangements. Rule 607 prescribes that brokers must disclose their PFOF and order routing policies to customers upon opening the account, and annually thereafter.[45] Nevertheless, reports for display execution quality and PFOF statistics prove difficult to find on the broker's website.[46] For example, Robinhood's customers may find its disclosures buried in the "Disclosures" section of the application's menu next to other statements nobody reads such as Licenses, Privacy, and Customer Relationship Summary. In acknowledgment of the need for transparency, FINRA has issued recent regulatory notices reminding firms of their best execution obligations regarding PFOF, signaling that the SEC might consider additional best execution requirements if such outcomes remain.[47]

In concern of these issues, the SEC has reexamined the lack of regulation in the OTP space, questioning the business model entirely.[48] PFOF conflict of interest and disclosure issues have even caused SEC chairman Gary Gensler to suggest a possible ban on the PFOF model that enables OTPs to offer their no-fee trading system.[49]

A. Gamification and Social Influence

As mobile app OTPs continue their popularity, regulators continue to inquire about design. Application design essentially needs to offer a good user experience, which adds and retains clients for the broker-dealer's customer base. Part of that user experience includes "gamification" elements. Gamification applies the positive reinforcement of game-design elements in non-game contexts.[50] Financial applications, including OTPs,

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43 17 C.F.R. § 240.10b-10; 17 C.F.R. § 242.606; 17 C.F.R. § 242.607.

44 17 C.F.R. § 240.10b-10.

45 KATTEN, *supra* note 41.

46 Carey, *supra* note 32.

47 KATTEN, *supra* note 41.

48 Press Release, SEC, SEC Requests Information and Comment on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology (Aug. 27, 2021), https://www.sec.gov/news/press-release/2021-167.

49 Dmytro Spilka, *Exploring the SEC's bid to Ban Payment for Order Flow: What Could Replace PFOF?*, NASDAQ (Oct. 21, 2021), https://www.nasdaq.com/articles/exploring-the-secs-bid-to-ban-payment-for-order-flow%3A-what-could-replace-pfof-2021-10-21.

50 Bayuk & Altobello, *supra* note 4 at 959.

have significant exposure to the gamification market.[51] Consequently, stock brokerages use gamification to encourage loyalty and increase activity.[52] Online trading applications with a PFOF model must garner an active user base to create value for themselves and the market makers they give information to.[53] Accordingly, game-design elements may be divided into three main types: website or user experience, process-related mechanics, and social-related components.[54]

An intuitive user experience is the goal of app design. Market participants, especially newer entrants, will likely stick to a more intuitive application.[55] The ability to instinctually move about an application creates familiarity, deterring a user from using other competitors. Fintech innovation spurred the advent of online investment platforms, which have only increased in popularity as people now spend almost seven times longer on these apps than on broker-dealer websites.[56] Retail investor-oriented OTPs market accessibility because a large quantity of clients makes market orders more desirable to firms who will pay for that retail order information.[57] While trading platforms for beginners do *some* marketing for features such as educational resources, easy navigation, clear commission and pricing structures, portfolio construction tools, and good customer service—most marketing focuses on the more exciting and lucrative aspects of trading.[58]

Good user interfaces often contain personalized data and statistics to keep track of the user's progress.[59] These process-related components of games and apps present user data as goals for financial achievements.[60] Moreover, these badges and achievement indicators keep users engaged in the application.[61] For example, Robinhood famously used digital confetti to celebrate a user's first trade.[62] The financial services industry often

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51 *Id.* at 952-53.
52 Rajat Paharia, LOYALTY 3.0: HOW BIG DATA AND GAMIFICATION ARE REVOLUTIONIZING CUSTOMER AND EMPLOYEE ENGAGEMENT 68 (2013).
53 Carey, supra note 32.
54 Bayuk & Altobello, *supra* note 4, at 954.
55 *Id.* at 955-56.
56 Siqi Wang, *Consumers Beware: How Are Your Favorite "Free" Investment Apps Regulated?*, 19 DUKE L. & TECH. REV. 43, 44 (2021).
57 *Id.* at 50.
58 Michael Sacchitello, *Best Trading Platforms for Beginners*, INVESTOPEDIA (Dec. 6, 2021), https://www.investopedia.com/best-brokers-for-beginners-4587873.
59 Bayuk & Altobello, *supra* note 4, at 956.
60 *Id.* at 956.
61 Andrew Ramonas, *SEC 'Gamification' Study Ups Reporting Threat for Online Brokers*, BLOOMBERG L. (Sept. 7, 2021), https://news.bloomberglaw.com/securities-law/sec-gamification-study-ups-reporting-threat-for-online-brokers.
62 *Id.*

lauds gamification as the "democratization of the sector."[63] The industry argues that gaming principles keep up engagement, while the visualization of user activity data and goals motivates market participants to perform better or continue reaching their financial goals.[64] In all fairness, an OTP gathers a lot of useful data free of charge that the customer may then consider for future portfolio adjustments. At the same time, gamifying stock trading only confirms to many the assumption that the markets are little more than a gilded playground for the rich while low-information traders play "casino capitalism."[65] Further, cosmetic upgrades cause OTP user losses because the customer might not take the markets seriously.[66]

Video games have long used user data to encourage more playtime. Likewise, OTPs display financial progress statistics because the quantification of market results induces competitiveness and comparability.[67] Athletes, students, and businesses all use personalized statistics to make changes and hopefully improve themselves. However, "gamification" differentiates itself from "games" because accumulating activity and loyalty around the application creates value for the *brokerage*, not necessarily the users.[68] In short, gamified design in an OTP *manufactures* motivation to perform better in the market.[69]

More about motivation, retail investors may have either extrinsic or intrinsic reasons for their trading behavior. Extrinsic motivation comes in the form of external rewards or outside stimulus.[70] The performer may not find the task itself rewarding; however, the consequences of completion or success cause recurrent behavior.[71] Self-determination theory acknowledges four types of extrinsic motivation: external regulation; introjected regulation; identified regulation; and integrated regulation. All play a role in retail behavior. [72]

First, external regulation comes from an incentive from another.[73] For example, an OTP advertisement encourages a young person to download

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63 Samuel Miranda, *Wolfenstein of Wall Street: the Gamification of Trading*, GAME DEVELOPER (Sept. 12, 2016), https://www.gamedeveloper.com/business/wolfenstein-of-wall-street-the-gamification-of-trading.

64 *See* Paharia, *supra* note 52, at 68-70.

65 Miranda, *supra* note 63.

66 *Id.*

67 Paharia, *supra* note 52, at 79.

68 *Id.* at 69.

69 John D. Rich Jr, *What Video Games Get Right About Motivation*, PSYCHOLOGY TODAY (Jan. 28, 2020), https://www.psychologytoday.com/us/blog/parenting-purpose/202001/what-video-games-get-right-about-motivation.

70 Amy Morin, *What is Extrinsic Motivation?*, VERYWELLMIND (Apr. 13, 2021), https://www.verywellmind.com/what-is-extrinsic-motivation-2795164.

71 *Id.*

72 *See* Paharia, *supra* note 52, at 86.

73 *Id.*

the application. Next, introjected regulation comes from one's ego, self-worth, and self-esteem.[74] As most Americans cannot save enough for retirement, applications like Robinhood or TD Ameritrade encourage them to redirect their attention and plan for financial security.[75] Identified regulation, in contrast, occurs when one consciously values a goal or regulation for personal acceptance.[76] Brokerage marketing and process-related components of gamified OTPs maneuver this behavior into playing the markets. Finally, integrated regulation creates habitual actions, such as constantly opening the application to see incremental market changes.[77]

In addition to extrinsic factors, games intrinsically motivate the players because of their freedom of choice, sense of accomplishment, and social interaction. In accomplishing a financial goal, gamified OTPs allow a lot of creativity.[78] Whether you use individual investing strategies or even a simple "gut instinct," it feels fulfilling to play the stock market. An investor's choices display every day in the form of bright red or green lines. That market experience engages participants who eagerly await the outcome no matter how uninformed the trading decision.[79] Likewise, games create a mastery motivator, enticing the player to focus on constant improvement in position.[80]

These intrinsic factors add excitement to investing, which traditionally seems like boring numbers moving on a screen. On the OTP, you directly see winners and losers, historical data, and new avenues to play the market—motivating the investor to keep trying to make money. After all, no incentive exists where the outcome of every risk-taking adventure amounts to a tie.

Equally important, users themselves encourage their following to join in on the fun. Alongside gamification strategies, brokerages market on social media to galvanize a large investor following.[81] The number of retail investors using OTPs has steadily increased to 91 million in 2020.[82] The

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74 *Id.*

75 Suzanne Woolley, *Americans Fall Further Behind on Retirement Savings as Inflation Bites*, BLOOMBERG (Oct. 24, 2022), https://www.bloomberg.com/news/articles/2022-10-24/have-i-saved-enough-for-retirement-55-say-they-re-behind-as-inflation-bites#xj4y7vzkg.

76 Paharia, *supra* note 52, at 86.

77 *See id.*

78 *See id.*

79 *See* Paharia, *supra* note 52, at 73.

80 *Id.* at 75.

81 Mark Schoeff Jr., *Finra Probes Brokerages' use of Social Media for Prospecting*, INVESTMENT NEWS (Sept. 17, 2021), https://www.investmentnews.com/finra-probes-brokerages-use-social-media-211602.

82 David Curry, *Stock Trading & Investing App Revenue and Usage Statistics (2022)*, BUS. OF APPS (Jan. 19, 2022) https://www.businessofapps.com/data/stock-trading-app-market/.

estimated increase of users on these apps for 2021 is 150 million.[83] In response, regulators have focused on the primary motivating factor—social interaction. The social components of gamification necessitate interaction between game players.[84] Investors on the same platform compare each other's gains (or losses) in the stock market.[85] No longer does anyone play stocks in private, or only reveal their portfolio to close family and friends. Users of financial apps tend to prefer these "social features," which enable sharing progress with peers.[86] Thus, the OTP adds yet another motivator for its customers to continue stock trading.

The SEC reports that these users have caused large movements that exceed broader market changes.[87] More specifically, millions of individuals trading on OTPs have caused over 100 stocks to experience large price moves.[88]

Consequently, social media greatly influences the retail market. Traders historically required access to a Bloomberg terminal for valuable market information.[89] Now CEOs and popular figures in the stock market directly broadcast their views on social media.[90] But just because there is more easily accessible information does not mean that such information is correct. Just like how the social aspects of gamification can spur market engagement, the spread of low-cost false or misleading information about stocks shared with the masses presents a problem for brokers and social media outlets.[91]

The SEC, along with FINRA, has started looking into ways that advisers and broker-dealers use "digital engagement practices" to land new customers. In addition to gamification and membership subscriptions, the SEC wants to investigate how social networking tools enable investors

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83 *Id.*

84 Bayuk & Altobello, *supra* note 4, at 957-58.

85 Kane Pepi, *Best Social Trading Platform 2022 – Cheapest Platform Revealed*, TRADING PLATFORMS, https://web.archive.org/web/20220122195238/https://tradingplatforms.com/social/ (Jan. 3, 2022),

86 Bayuk & Altobello, *supra* note 4 at 957-58.

87 Angela Mauroni, *SEC releases report on 'gamification' of trading apps*, JURIST (Oct. 19, 2021), https://www.jurist.org/news/2021/10/sec-releases-report-on-gamification-of-trading-apps/.

88 *Id.*

89 *See also* Will Kenton, *Bloomberg Terminal*, INVESTOPEDIA, https://www.investopedia.com/terms/b/bloomberg_terminal.asp (explaining that a Bloomberg Terminal provides sophisticated financial data and news to place trades at the cost of over $20,000 a year).

90 *The Dark Arts of Social Media on Wall Street*, THE ATLANTIC, https://www.theatlantic.com/sponsored/etrade-social-stocks/the-dark-arts-of-social-media-on-wall-street/330/ (last visited Dec. 25, 2021).

91 SEC, Request for Information and Comment on Digital Engagement Practices, 86 Fed. Reg. 49067, 49068-70, 5-10 (Sept. 1, 2021).

to copy the trades of other investors.[92] At the same time, FINRA is sweeping through a small number of firms to examine social media communications as well as customer data protection.[93] In fact, FINRA will assess firms' written policies and procedures for supervising social media marketing. FINRA specifically wants to review referral programs and "influencers" as both practices involve firms paying individuals to promote their brokerage through social media or word of mouth.[94]

B. *Payment for Order Flow in the Online Trading Platform*

Using the PFOF model, OTPs greatly benefitted consumers by eliminating online trading commissions.[95] As mentioned earlier, OTPs rely on market makers' payments in exchange for marketable retail customer orders.[96] Market makers profit from investors because "small money" purchases securities at a nominally higher rate than the market price. The spread between the price for the investor and the market price amounts to the market maker's profit.[97] However, because market makers do not have to consider the interests of the investors whose order information they purchased, bid-ask spreads could cost those "free trades" more than originally thought.[98]

On balance, OTPs still make investing much cheaper and more intuitive for the average person. Retail investment applications rely on scalable platforms intrinsic to app design. Startups appreciate users who provide more feedback, allowing programmers to focus on maximizing customer experience. Coupled with gamification elements and PFOF, investment apps can provide access to the market while also providing reliable revenue to shareholders of the brokerage firm.[99] Digital technology requires very little marginal cost per added customer. So long as these investment brokers have a sizeable enough client base to ensure proper revenue streams, they may allow users to bypass traditional brokerage account minimums. As a result, investment applications like

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92 *Id.*
93 Schoeff, *supra* note 81.
94 *Id.*
95 Carey, *supra* note 32.
96 *Id.*
97 Ganti, *supra* note 33.
98 Carey, *supra* note 32.
99 *Online Trading Platform Market to Reach USD 12.16 Billion in 2028; Utilization of Artificial Intelligence with Electronic Platforms to Aid Growth: Fortune Business Insights*, GLOBE NEWSWIRE (Aug 9, 2021, 4:56), https://www.globenewswire.com/news-release/2021/08/09/2276829/0/en/Online-Trading-Platform-Market-to-Reach-USD-12-16-Billionin-2028-Utilization-of-Artificial-Intelligence-with-Electronic-Platforms-to-Aid-Growth-Fortune-Business-Insights.html.

Robinhood, Webull, and M1 Finance allow market access to underserved investors with very little principal.[100]

Still, the economic incentives for a broker to send its order flow to market makers create potential conflicts of interest because the broker has a duty of best execution.[101] For example, Robinhood brings in significantly higher order routing revenue to average account value than its competitors; at the same time, other applications such as TD Ameritrade, E*Trade, and Charles Schwab also collect considerable order routing income.[102] Alphacution's study showed that as of the first quarter of 2020, Robinhood's order routing revenue to average account value ratio was $40,683, compared to $2,079 for TD Ameritrade, $891 for E-Trade, and $195 for Schwab.[103] Without such order flow, market makers could have possibly quoted more competitive prices per share obtained on the trade.[104] Robinhood claims it could adapt to regulatory changes but considering the amount of revenue received from PFOF, barring the practice could seriously hurt its business.[105] From a risk perspective, Robinhood's ability to charge a higher rate for order flows means nothing if it cannot improve disclosure and execution as promised in its previous settlement with the SEC.[106] Meaning, if Robinhood cannot stay compliant, the SEC has all the more reason to bar their business model for them and other OTPs.

Unsurprisingly, FINRA as a self-regulatory agency and the SEC as a federal body contrast on the PFOF issue. In May 2021, FINRA CEO Robert Cook appeared before Congress, commending fintech innovation.[107] In consideration of the January Market Events concerning Gamestop stock, he also recognized the need to assess the compliance of

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[100] *See* Riley Adams, *11 Best Commission-Free Stock Trading Apps & Platforms*, YOUNG AND THE INVESTED (Jan. 20, 2022), https://web.archive.org/web/20220125232900/https://youngandtheinvested.com/best-free-stock-trading-apps/.

[101] *See* FINRA, No. 21-23, REGULATORY NOTICE (2021).

[102] Tomio Geron, *Data Shows how Robinhood Makes More Money from its Users than Other Brokers*, PROTOCOL (July 15, 2021), https://www.protocol.com/fintech/payment-for-order-flow.

[103] *Id.*

[104] Bill Alpert, *2 Charts That Show Why Robinhood Cares So Much About Payment for Order Flow*, BARRON'S (Sept. 1, 2021), https://www.barrons.com/articles/robinhood-payment-for-order-flow-51630451893.

[105] *See* Simone Foxman, Julie Verhage, and Suzanne Woolley, *Robinhood Gets Almost Half Its Revenue in Controversial Bargain with High-Speed Traders*, BLOOMBERG (Oct. 15, 2018, 1:45 PM), https://www.bloomberg.com/news/articles/2018-10-15/robinhood-gets-almost-half-its-revenue-in-controversial-bargain-with-high-speed-traders.

[106] Alpert, *supra* note 104.

[107] Robert W. Cook, *Statement Before the Financial Services Committee U.S. House of Representatives*, FINRA (May 6, 2021), https://www.finra.org/media-center/speeches-testimony/statement-financial-services-committee-us-house-representatives.

app-based discount brokers that rely on PFOF as a source of revenue.[108] He then reiterated the SEC's guidance holding that a broker-dealer may receive market-maker payments so long as the broker-dealer performs its duty to seek the best possible prices for its customers.[109] As part of its review, FINRA issued a regulatory notice reminding members of their duty of best execution in accordance with FINRA Rule 5310.[110]

Imposition of fines for Rule 5310 violations rarely occurs, much less impacts the firm's bottom line.[111] Robinhood itself topped the fines at a modest $1.25 million for best execution violations.[112] In short, FINRA continues to support the allowance of PFOF but would recognize the SEC's imposition of additional PFOF disclosure requirements.[113]

More notably, SEC Chairman Gary Gensler emphasized concern about conflicts of interest and best execution. First, Gensler states that even though off-exchange market makers handle 38% of overall trading volume, seven market makers handle the vast majority of that segment.[114] The aggregation of data provides those market makers with competitive advantages over other open exchanges as well as market makers with less order flow.[115] OTPs commonly send orders to these large market makers such as Citadel Securities, Virtu, and G1 Execution.[116] Gensler reiterated similar concerns about the lack of transparency and pricing Cook mentioned.[117] Overall, the SEC seems to find aspects of PFOF as a barrier to "fair, orderly and efficient markets" in contrast to FINRA and probably most retail investors.[118]

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108 *Id.*

109 *Id.*

110 FINRA, No. 21-23, REGULATORY NOTICE (2021).

111 *See* Maria Nikolava, *FINRA Fines Virtu Americas for Failure to Provide Best Execution*, FINANCE FEEDS (July 22, 2020, 8:59 AM), https://financefeeds.com/finra-fines-virtu-americas-failure-provide-best-execution/.

112 Michelle Ong and Mike Rot, *FINRA Fines Robinhood Financial, LLC $1.25 Million for Best Execution Violations*, FINRA (Dec. 19, 2019), https://www.finra.org/media-center/newsreleases/2019/finra-fines-robinhood-financial-llc-125-million-best-execution.

113 Justin L. Chretien, *SEC Targets Payment for Order Flow: What Broker-Dealers and Wholesale Market Makers Should Know*, CARLTON FIELDS (Sept. 10, 2021), https://www.carltonfields.com/insights/publications/2021/sec-targets-payment-order-flow-what-broker-dealer.

114 *Id.* In addition to off-exchange market makers, public exchanges handle 53% of trade volume and alternative trading systems handle the other 9%. *Id.*

115 *Id.*

116 Jon Detrixhe, *Citadel Securities Gets Almost as Much Trading Volume as Nasdaq*, QUARTZ (Feb. 5, 2021), https://qz.com/1969196/citadel-securities-gets-almost-as-much-trading-volume-as-nasdaq/.

117 Chretein, *supra* note 113.

118 *Id.*

From a consumer standpoint, the zero-commission fee structure outweighs PFOF problems. Although Robinhood receives almost half its revenue via PFOF, these bid-ask spreads rarely cost a retail client more than a fee commission.[119] In any case, evidence shows marketable retail orders pursuant to PFOF arrangements may execute quicker than the national best bid or offer, adding more value to the consumer.[120] Moreover, many established brokers dropped fee commissions, further showing that a trader still retains more value on a zero-commission basis even taking into account potentially dubious bid-ask spreads, conflicts of interest, and application-induced trading.[121] Accordingly, regulators should steer clear of barring PFOF as some countries have done because the resulting reinstitution of broker-dealer fees would bar many retail investors from the market.[122]

C. Understanding Retail Investor Risks Through Behavioral Finance

Brokers always compete for new customers. But consider the radical demographic change in the retail investor market. In 2020, 22% of retail investors are under 30 years old, compared to the 6% prior.[123] These younger investors favor speaking to friends, family, and social media for investment information.[124] After all, they grew up on social media.[125] Further, these investors have smaller accounts of less than 500 dollars and usually enter the market with mobile apps rather than websites.[126]

Yet, many trading behaviors stay the same. Regardless of age, trading behavior still exhibits emotional action. Emotional responses such as anger and fear sabotage "correct trading behavior."[127] Emotional responses affect a trader in two ways: (1) withdrawal into behaviors that historically work regardless of merit, and (2) active search for possible

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[119] Foxman et al., *supra* note 105; Alexander Osipovich & Lisa Beilfuss, *Why 'Free Trading' on Robinhood Isn't Really Free*, WSJ (Nov. 9, 2018), https://www.wsj.com/articles/why-free-trading-on-robinhood-isnt-really-free-1541772001.

[120] *Id.*

[121] Chang, *supra* note 16.

[122] GARY SHORTER, BROKER-DEALERS AND PAYMENT FOR ORDER FLOW, CONG. RSCH. SERV., (Apr. 2, 2021).

[123] BNY MELLON, THE EVOLVING LANDSCAPE OF U.S. RETAIL INVESTING 5 (2021), https://www.bnymellon.com/content/dam/bnymellon/documents/pdf/insights/the-evolving-landscape-of-us-retail-investing.pdf.coredownload.pdf.

[124] *Id.* at 6.

[125] Brooke Auxier & Monica Anderson, *Social Media Use in 2021*, PEW RESEARCH (Apr. 7, 2021), https://www.pewresearch.org/internet/2021/04/07/social-media-use-in-2021/.

[126] *Id.*

[127] Mike Elvin, FINANCIAL RISK TAKING: AN INTRODUCTION TO THE PSYCHOLOGY OF TRADING AND BEHAVIOURAL FINANCE, 160 (1st ed. 2006).

plans.[128] We make judgments through a combination of knowledge and feelings. Although not conclusive, some evidence shows that self-awareness of mood changes helps traders assess their comfort level.[129] However, emotional reactions modify perception, direct attention, and give preferential access to certain memories, biasing thinking. Anxiety narrows attention, causing fearful traders to disregard rational choices.[130] Fear might cause portfolio liquidation or a "trader's freeze," where a trader does nothing when common sense requires action.[131] Conversely, investors may jump into the market due to fear of missing out on market gains.[132]

One's mood can be manipulated quite independently of anything else.[133] Psychologists describe moods derived in an inappropriate context as "misattributions."[134] For instance, OTPs enhance positive moods in the customer through perceived value.[135] Because OTPs do not give the trader too much time to think about their platform of choice, customers develop a natural bias towards the trading applications they currently use.[136] A trader's self-awareness refers to understanding one's strengths, limitations, beliefs, and motives.[137] Warren Buffet explains how investors should use areas of specialization to their investment advantage.[138] However, problems occur when an investor over or underestimates their strengths and limitations. Overconfidence causes perceptual biases, often coming from the brokerage's platform or the platform's community.[139]

Naturally, an OTPs design choice influences a customer. For example, a "Top Movers" list influences investor buying behavior by exploiting the

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[128] *See Id.* at 161

[129] *Id.* at 162.

[130] *Id.*

[131] *Id.*

[132] Steve Goldstein, *Fear of Missing Out is Driving the Stock Market — and Having This Surprising Effect as well, Research Finds*, MARKETWATCH (Nov. 10, 2021, 9:02 AM), https://www.marketwatch.com/story/fear-of-missing-out-is-driving-the-stock-market-and-having-this-surprising-effect-as-well-research-finds-11636545386.

[133] Elvin, *supra* note 127, at 164.

[134] *Id.* at 160.

[135] *Id.* at 164.

[136] *Id.* at 164.

[137] *Id.* at 166.

[138] *See Understanding your Circle of Competence: How Warren Buffett Avoids Problems*, FS BLOG, https://fs.blog/circle-of-competence/ (last visited Jan. 13, 2022).

[139] *See* Bob Pisani, *Attention Robinhood Power Users: Most Day Traders Lose Money*, CNBC (Nov. 20, 2020), https://www.cnbc.com/2020/11/20/attention-robinhood-power-users-most-day-traders-lose-money.html.

appearance on the front pages of the application or website.[140] Trading communities have even formed "herding events" where Robinhood traders crowd into high-traffic stocks.[141] Unsurprisingly, social media platforms and media attention may generate discussion that leads to additional herding.[142] This herd mentality, assisted by the OTP, unduly influences the informed and self-aware trader to make more aggressive trading decisions.

Consumers rarely recognize a financial institution's influence. A bank's smartphone application can facilitate the installation of other applications.[143] While integration within one company's environment helps ease of function, that firm now has another pathway to sell a customer its products or services.[144] To illustrate, Robinhood's primary purpose as a trading platform also encourages customers to deposit money into their accounts because of a competitive Cash Management Annual Percentage Yield.[145] As such, Robinhood can now dually function as a savings account as well as an OTP for a client.

Ironically, experience with money-saving or financial apps makes someone *think* they know more about finances than actually the case. Bayuk and Altobello's findings on gamification and financial behavior tested participants in both objective knowledge and subjective knowledge.[146] The experiment assessed objective knowledge from the participant's socioeconomic status, financial questions, ability to handle a financial emergency, etc.[147] Subjective knowledge consisted of their own perception of financial expertise.[148] Interestingly, those experienced with financial applications had lower objective financial knowledge than those who had no experience.[149] Furthermore, individuals fluent with finance apps tended to prefer more "social features," perceiving the application as more useful, whereas individuals with no experience preferred more "economic features" that helped them learn and progress.[150]

With limited resources and competition, there is no surprise that an OTP promotes community features over user education about stock

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140 Brad M. Barber, Xing Huang, Terrance Odean, Christopher Schwarz, *Attention-Induced Trading and Returns: Evidence from Robinhood Users*, 77 J. OF FIN. 3141, 3143-44 (2022).
141 *See* Pisani, *supra* note 139.
142 Barber et al., *supra* note 140, at 3156.
143 *See* Bayuk & Altobello, *supra* note 4, at 966-67.
144 *Id.*
145 Robinhood, *Interest (APY)*, ROBINHOOD, https://robinhood.com/us/en/support/articles/earning-interest/ (last visited Jan. 4, 2022).
146 Bayuk & Altobello, *supra* note 4, at 965-66.
147 *Id.*
148 *Id.*
149 *Id.*
150 *Id.* at 951, 966.

markets to gain more customers. OTP community features distort investor self-management and trading strategies to the benefit of the investment platform. Self-management here refers to the ongoing mental clarity and concentration required in trading.[151] The investor's ability to openly admit mistakes or faults is key. Honesty allows flexibility in changing market situations. However, such social features can create detrimental emotions like fear of missing out.[152] Outside of the investor's own ability, market makers with order flow knowledge could place trades against the users they received the order from.[153] As such, brokers still profit from their client's trade executions even if those trades result in clients' bag-holding bad stocks because of social media-induced herding.

Fear of missing out usually comes from a perceived punishment; specifically, the opportunity of missing gains in the market. Operant conditioning holds that punishment does not encourage behavior, but only seeks to avoid the consequences of not doing that behavior.[154] Conversely, positive reinforcement will give rise to repetitive behavior.[155] In this way, OTPs encourage the proclivity of young investors to actively play the stock market. The lack of rules makes investing inherently attractive to young market entrants.[156] Generally, money-making strategies require rigid rules and discipline, but many retail investors have no strategy and may still perform just as well in the market or better.[157] So if these retail investors have no strategy, how do these customers decide when and how to trade?

Unbeknownst to investors, trading platforms play a large part in their behavior. For example, front-page trends influence whether investors choose to buy or sell in the market.[158] In addition, OTP users often view community activities, especially popular trading movements. For easy viewing, most OTPs have categories of equities grouped together through similar qualities such as industry, volatility, popularity, etc.[159] Similarly,

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[151] Elvin, *supra* note 127, at 168.

[152] *See* Goldstein, *supra* note 132.

[153] *See* Carey, *supra* note 32 (noting potential conflicts of interest occur between the broker's profit incentive and the client's best interest).

[154] *B.F. Skinner and Operant Conditioning: A Primer for Traders, Investors, and Economic Policymakers*, PHILOSOPHICAL ECON. (Oct. 3, 2015), https://www.philosophicaleconomics.com/2015/10/bfskinner/.

[155] *Id.*

[156] *Id.*

[157] *Id.*

[158] Anastassia Fedyk, *The Effect of News Positioning on Financial Markets*, HARV. U. (Oct. 10, 2018), https://scholar.harvard.edu/fedyk/publications/front-page-news-effect-news-positioning-financial-markets.

[159] *See generally* YAHOO, *Trending* Tickers, https://finance.yahoo.com/trending-tickers/ (last visited Jan. 4, 2022).

application designers have complete control of the stock market news seen on their platform. Such media does not necessarily attract the most important segments of the day, rather the news may show the most exciting or interesting stocks that could generate trading activity. Ultimately, seeing a front-page news story about a hot stock will likely induce interest in any reader.[160]

OTPs have many other ways to encourage trading through design choices. Robinhood famously used a burst of confetti to celebrate a transaction, bitcoin prices appear in neon pink, and the browse section often lists the more popular stocks to trade.[161] Rather than directing users to adopt a coherent strategy, retail brokers push riskier plays such as trading individual stocks, cryptocurrency investing, margin trading, and options trading. It might be retail investors themselves chasing risky or trendy strategies. Considering that 90% of new retail investors trade about three times a month, one might disregard an OTP's influence.[162] But examine more closely how technology and design nudge investors.[163] Even small designer choices affect behavior: the color red reduces risk-taking, showing gains encourages the sale of winning investments, and management fees discourage day trading.[164] More problematic, the combination of young people who do not properly understand the risks of margin and options trading along with low barriers to those highly complex strategies can prove quite costly.[165] Indeed, the user interface leads people to invest in individual stocks and cryptocurrencies instead of safer options.[166] No doubt, investment firms like Robinhood and Betterment acknowledge these design choices; however, the incentive to generate trading among clients leads these OTPs to provide certain types of information over others.[167]

The market's volatility can cause drastic emotional pressure upon young investors as they have the least ability to self-manage. The excitement of stock market trading without the proper education causes an overreliance on outside influences. Even worse, trendy, get-rich-quick schemes that sour often have little recourse against the influencer, causing investor anxiety, depression, and even suicide.[168] In one case, a 20-year-

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160 *See* Brian Beers, *How the News Affects Stock Prices*, INVESTOPEDIA (Sept. 30, 2021), https://www.investopedia.com/ask/answers/155.asp.
161 Ingram, *supra* note 28.
162 BNY Mellon, *supra* note 123, at 5.
163 Ingram, *supra* note 28.
164 *Id.*
165 *See id.*
166 *Id.*
167 *Id.*
168 Sheryl Nance-Nash, *New Kids On The Block: Young Investors Are Battling Anxiety And Inexperience In The Stock Market*, MONEY UNDER 30 (June 1, 2022), https://

old student took his own life upon the mistaken belief that his account balance was negative $730,000.[169] In fact, his account would correct once the stocks would credit to his account.[170] Such tragedy exemplifies the regulatory need in today's market dynamics.

The legal implications of behavioral finance reflect the bifurcation of investor treatment in the court system. On one side, investor-sympathetic courts extend broad obligations to brokers to act as favorably as possible for the customer.[171] Those courts describe brokers as the customer's fiduciary even when the broker only facilitates the transaction and nothing else.[172] In contrast, other courts reject fiduciary obligations for "simple stockbroker-customer relationships."[173] In denying that brokers are custodians of their customers, these courts mostly let the responsibility of punishing brokers for problematic behavior fall onto the regulators or markets.[174] Generally, the SEC's sanctioning decision holds so long as it is reasonably explained and not "arbitrary, capricious, or an abuse of discretion."[175] One can draw this same bifurcated attitude from SEC and FINRA statements regarding PFOF. The SEC notes a more aggressive approach, and that banning PFOF is "on the table."[176] In contrast, FINRA has issued more moderate communications like regulatory reminders and prefers routine enforcement of existing rules.[177] As we will later see, the resulting Reg BI obligations offer a reconciliation between the two opposing views.

III. OVERVIEW OF STOCKBROKER STANDARD OF CARE

The fundamental developments in statutory regulations for brokers began with the Securities Exchange Act ("SEA") and the Advisers Act.[178]

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www.moneyunder30.com/new-kids-on-the-block-young-investors-are-battling-anxiety-and-inexperience-in-the-stock-market.

169 Sergei Klebnikov, *20-Year-Old Robinhood Customer Dies By Suicide After Seeing A $730,000 Negative Balance*, FORBES (June 17, 2020), https://www.forbes.com/sites/sergeiklebnikov/2020/06/17/20-year-old-robinhood-customer-dies-by-suicide-after-seeing-a-730000-negative-balance/?sh=54dc085a1638.

170 *Id.*

171 Donald C. Langevoort, *Selling Hope, Selling Risk: Some Lessons for Law from Behavioral Economics About Stockbrokers and Sophisticated Customers*, 84 CALIF. L. REV. 627, 669 (1996).

172 *See* SEC v. Hasho, 784 F. Supp. 1059, 1107-08 (S.D.N.Y. 1992).

173 Lefkowitz v. Smith Barney, Harris Upham & Co., Inc., 804 F.2d 154, 155 (1st Cir. 1986).

174 Saad v. SEC, 873 F.3d 297, 302-03 (D.C. Cir. 2017)

175 *Id.*

176 *See* Chretien, *supra* note 113.

177 *Id.*

178 *See generally* 17 C.F.R. § 240; 17 C.F.R. § 275.

The SEA of 1934 governs securities transactions on the secondary market, creating reporting and financial disclosure requirements for public companies.[179] Such requirements protect investors and ensure access to information necessary to make investment decisions.[180] Further, the SEA birthed the SEC, the federal enforcers for securities regulation.[181] The Advisers Act states that advisers have a fiduciary duty to their clients, must pass a qualifying exam, and should register with the SEC if the adviser has at least $100 million in assets under management.[182] As such, brokers can have a variety of client arrangements that may give rise to duties to the customer. Some accounts provide full-service consulting while others only act in a limited agency relationship with the fiduciary during transaction executions.[183] Consistent with fiduciary duties, brokers must observe a high standard of care when acting within that agency relationship.[184]

The nature of the securities industry requires a broker's heightened standard of care. Originally, the idea of suitability was derived from the "know your customer" rule. The know your customer rule required broker-dealers to conduct an inquiry to assure that customers could pay for securities purchases.[185] Accordingly, the regulation attempted to protect broker-dealers from holding the losses of their clients.[186] Later, the SEC advocated for the "shingle theory," positing that the public relies on these professional broker-dealers.[187] The shingle theory itself extends from the common law doctrine of "holding out." Meaning, an individual holding himself out as a certified expert manifests a higher standard of care in their recommendations.[188] Accordingly, a broker must base recommendations on client needs rather than self-interested markups or commissions.[189] Following this tradition, the SEC prohibited broker-dealers from making

179 Will Kenton, *What Is the Securities Exchange Act of 1934? Reach and History*, INVESTOPEDIA (Feb. 24, 2023), https://www.investopedia.com/terms/s/seact1934.asp.
180 *Id.*
181 *Id.*
182 Julia Kagan, *Investment Advisers Act of 1940 Definition, Overview*, INVESTOPEDIA (Oct. 28, 2021), https://www.investopedia.com/terms/i/investadvact.asp.
183 *See* Caravan Mobile Home Sales, Inc. v. Lehman Bros. Kuhn Loeb, Inc., 769 F. 2d 561, 567 (9th Cir. 1985).
184 *See* Carol R. Goforth, *Stockbrokers' Duties to Their Customers*, 33 ST. LOUIS U. L.J. 407, 410-11 (1989).
185 23A Jerry W. Markham & Thomas Lee Hazen, *Broker-Dealer Operations Sec. & Comm. L.* § 10:1 (rev. ed. 2021).
186 *Id.*
187 *Id.*
188 *Id.*
189 *Id.*

recommendations for securities transactions unless they believe the transaction looked suitable for the customer.[190]

Another factor that guides stockbroker fiduciary duties is the concept of discretionary and nondiscretionary accounts. In a discretionary account, the client authorizes the broker to make trades on the client's account without express approval from the client as to each transaction.[191] In contrast, where all investment decisions come from the client and the broker only facilitates the transaction in an administrative capacity, courts do not hold that account as discretionary.[192]

A. Common Law Fiduciary Duties

From the inception of the SEC, common law already held brokers to a fiduciary standard in many circumstances.[193] A few states have a *per se* imposition of broker fiduciary duty based on a broker-client agency relationship.[194] Many courts have held that fiduciary duties hinge on whether the broker managed a discretionary account.[195] Otherwise, courts impose a more limited set of duties in a non-discretionary account.[196] Fiduciary duties in a non-discretionary account generally limit themselves to the time of transaction execution unless exceptional circumstances exist.[197] These exceptions include factors such as the broker's usurpation of control on a non-discretionary account, proof of reliance on the broker, the customer's heed of the broker's advice, frequent communication between the parties, the customer's investment experience, and personal ties.[198] However, discretionary or non-discretionary status is not always conclusive. The customer's trust and confidence, as well as the stockbroker's control of the account, can signify whether to impose fiduciary duties.

B. The Trust and Confidence Test

Two tests are commonly used to measure whether the broker has a fiduciary relationship with the client. The first test holds that fiduciary

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190 Suitability Requirements for Transactions in Certain Securities, 54 Fed. Reg. 6693-01 (proposed Feb. 14, 1989) (to be codified at 17 C.F.R. pt. 240).
191 Goforth, *supra* note 184, at 422-23.
192 Shearson Hayden Stone, Inc. v. Leach, 583 F. 2d 367, 371-72 (7th Cir. 1978).
193 Carney v. Hanson Oil Co., Inc., 690 S.W.2d 404, 406 (Mo. 1985).
194 French v. First Union Sec., Inc., 209 F. Supp. 2d 818, 825 (M.D. Tenn. 2002).
195 *See, e.g.*, Est. of Bogue v. Adams, 405 F. Supp. 3d 929, 946 (D. Colo. 2019).
196 Vestax Securities Corp. v. Desmond, 919 F. Supp. 1061, 1072 (E.D. Mich. 1995).
197 In re Enron Corp. Securities, Derivative & "ERISA" Litig., 238 F. Supp. 3d 799, 851 (S.D. Tex. 2017), aff'd sub nom. *See* Lampkin v. UBS Painewebber, Inc. (In re Enron Corp. Sec., Derivative & "ERISA" Litig.), 238 F. Supp. 3d 799, 851 (S.D. Tex. 2017).
198 Patsos v. First Albany Corp., 433 Mass. 323, 335-37 (2001).

obligations arise upon the client's trust and confidence in a broker. The second test holds that if the client entrusts their affairs to a broker within a broker-client agency relationship, where the broker is on notice of that trust and confidence, such a relationship establishes fiduciary duties.[199] While some courts find the trust and confidence test dispositive, others find a client's trust and confidence in a broker only indicative of fiduciary obligations.

In the *Estate of Bogue v. Adams* case, the decedent's estate brought an action against investment industry professionals.[200] In Colorado, a fact-specific inquiry producing evidence that the customer placed trust and confidence in a stockbroker who knowingly managed the customer's account for the customer's benefit indicated a fiduciary relationship.[201] Here, the defendants solicited the decedent, gained his trust, and sought to have him invest in high-risk investments, exploiting the decedent's lack of financial sophistication.[202] Additionally, the defendants used their qualifications and licensure for added legitimacy.[203] The District Court of Colorado held that the decedent's estate properly alleged a breach of fiduciary duty because the decedent placed his investments under the defendant's discretionary control.[204]

More commonly in OTPs, customers do not usually give formal delegation of control to the broker. Instead, the broker *exhibits effective control* over a customer's account when following the broker's advice.[205] Courts have great difficulty finding the necessary amount of control to find a fiduciary relationship between brokers and their clients. Some courts utilize a "control test" to determine whether a fiduciary relationship exists between a broker and a customer.[206] Put another way, an agency relationship in a non-discretionary account may give rise to fiduciary duties when the broker exercised *de facto* control.[207] More in detail, a

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[199] Merrill Lynch, Pierce, Fenner & Smith v. Perelle, 356 Pa. Super. 165, 182-83 (1986) (citing Rst. 2d of Agency § 381 (1958)).
[200] Est. of Bogue v. Adams, 405 F. Supp. 3d 929, 934-36 (D. Colo. 2019).
[201] *Id.* at 945-46.
[202] *Id.* at 934-35.
[203] *Id.*
[204] *Id.* at 946.
[205] *See* in re Refco Sec. Litig., 759 F. Supp. 2d 301, 325-26 (S.D.N.Y. 2010) (explaining that lack of sophistication, extraordinary broker-dealer services, and distinguished customer' relationships with a broker may result in the imposition of fiduciary duty on a broker of a nondiscretionary account).
[206] *See* Cruse v. Equitable Securities of New York, Inc., 678 F. Supp. 1023, 1031-32 (S.D.N.Y. 1987).
[207] *Id.*

broker may still effectively exercise control where a client places his trust and faith in a broker, and routinely follows the broker's advice.[208]

In *Cruse v. Equitable Securities of New York, Inc.*, the plaintiff alleged that the defendant exercised control of his non-discretionary account since he had no concept of any trading strategies and their risks, but the defendant handled the account as if he had discretionary authority.[209] The relevant factors for control include discretion to the broker-dealer, age, education, intelligence, the client's business experience, the relationship between the client and broker, and the client's reliance placed on the broker.[210]

Relating back to OTPs, their use and advertisement on popular media platforms has created familiarity with younger investors. Such name recognition causes over-reliance on the broker who does not necessarily have its customer's best interests in mind. Coupled with the fact that younger investors rarely have financial sophistication, the story ends in retail investor losses due, at least in part, to the broker's behavior.

C. Federal Law Distinguishes Advisers and Brokers

Accounting for exceptional circumstances, most non-discretionary accounts limit broker fiduciary duties to administrative trade executions. However, one must understand the dichotomy between investment advisers and broker-dealers. Since an investment adviser's activity extends beyond a particular trade, fiduciary duties arise in a different set of circumstances.[211] Under the Advisers Act, such advisers have an ongoing duty to their clients to monitor and act in the client's best interests.[212] The added duty comes from the character of the financial consulting business, where advisers provide financial plans and recommendations in whole, or for particular types of investments or sectors.[213] It then follows that a federally registered adviser's obligations consist of providing ongoing, continuous services, even for a non-discretionary account.[214] Such a duty requires no actual stock sale unlike the event-driven duties of brokers under the SEA. Further, an adviser has a higher standard of disclosure under Section 206 of the Advisers Act than a broker for failure to disclose a conflict of interest under Section 10(b) of

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208 *Id.* at 1030-31.
209 *Id.*
210 *Id.* (citing Zaretsky v. E.F. Hutton & Co. Inc., 509 F.Supp. 68, 74 (S.D.N.Y.1981)).
211 Arthur B. Laby, *Fiduciary Obligations of Broker-Dealers and Investment Advisers*, 55 VILL. L. REV. 701, 727 (2010).
212 *See Id.* at 719, 728.
213 *See Id.* at 727.
214 *See Id.* at 727-28.

the Exchange Act and Rule 10b-5.[215] In contrast to Section 10(b) and Rule 10b-5, Section 206(2) lacks an intent requirement.[216]

OTPs functioning as the broker changes the dynamic because the client has little trouble executing a transaction.[217] The current issues revolve around OTPs combining an advisory function with their broker function while claiming no advisory function exists.[218] Under Reg BI, the SEC attempts to create a proper broker-dealer standard of care.[219]

IV. REGULATION BEST INTEREST

Brokers have historically always advised their clients. But now, technology has enlarged the advice component of the brokerage business and reduced executing transactions to a small matter.[220] Gamification and sophisticated behavioral finance knowledge clearly influence clients, blurring the line between adviser and broker.[221] Following these changes in financial services, the SEC's new standard resembles a compromise between stringent fiduciary duties and lukewarm FINRA obligations.

Many stockbrokers adamantly claim an inability to function in an advisor capacity and do not offer financial advice.[222] Yet, OTPs like Robinhood increasingly hire FINRA-registered financial professionals as part of customer support and brokerage-related issues.[223] Robinhood hired licensed financial counselors for more than just their technical support capacities. Clearly, the "qualifications and licensure" of these representatives bring credence to Robinhood as a premier brokerage.[224] These OTPs market towards younger adults who display little financial literacy, leaving an impressionable client base to more sophisticated

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215 Laby, *supra* note 211, at 728-30

216 *Id.* at 729; *see also* SEC v. Cap. Gains Rsch. Bureau, Inc., 375 U.S. 180, 185-86, 192 (1963).

217 *See* Laby, *supra* note 211, at 734-735.

218 *Id.*

219 *See* Kelly Anne Smith, *What Regulation Best Interest Means For Your Financial Advisor*, FORBES (Mar. 5, 2021), https://www.forbes.com/advisor/investing/regulation-best-interest/.

220 *See* Cory Mitchell, *Automatic Execution*, INVESTOPEDIA, https://www.investopedia.com/terms/a/automatic-execution.asp#:~:text=What%20Is%20Automatic%20Execution%3F,the%20need%20for%20human%20interaction (Nov. 27, 2020).

221 Ingram, *supra* note 28.

222 *See* Nicole Casperson, *Robinhood is Snapping up Financial Advisers. Here's why.*, INVESTMENTNEWS (Apr. 27, 2021), https://www.investmentnews.com/robinhood-is-snapping-up-financial-advisers-heres-why-205794.

223 *Id.*

224 Est. of Bogue v. Adams, 405 F. Supp. 3d 929, 934-36 (D. Colo. 2019).

brokerages.[225] Young people already display a proclivity towards high-cost borrowing in the form of credit cards, student loans, and expensive car notes.[226] All these factors combined show that these OTP customers would likely overleverage themselves.[227]

Furthermore, OTPs' encouragement of risky behavior leaves the investor with losses while the platform creates a profit from PFOF. Although applications like Webull, M1 Finance, and Betterment maintain that they only function as brokers, they continue to provide advisory-like services. Webull has gone so far as to partner with Benzinga, a financial news vendor, to streamline news and data for its clients.[228] Some applications have instituted algorithmic recommendations for beginner investors. These "robo-advisors" analyze many metrics including account minimums, overall costs, financial planning options, customer experience, etc.[229] In short, the client answers a small questionnaire and stock recommendations follow. Certainly, one could find this analogous to a stockbroker giving financial advice to its clients. Considering that, should the recommendations of these algorithmic counselors have a different standard of care to human financial advisors?[230]

All things considered, continual inundation of information and influence on the part of OTPs should have some duty to monitor even if the human element no longer exists.[231] Although investors may not meet with real account managers, the applications instill an increased confidence through application design and customer support.[232] OTPs still conduct an inquiry of the investor-client through questionnaires and

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225 Carlo de Bassa Scheresberg, *Financial Literacy and Financial Behavior among Young Adults: Evidence and Implications*. 6 NUMERACY 2, 1, 16 (2013).
226 *Id.*
227 *See generally* Nathaniel Popper, *Robinhood Has Lured Young Traders, Sometimes with Devastating Results*, N. Y. TIMES (Sept. 25, 2021), https://www.nytimes.com/2020/07/08/technology/robinhood-risky-trading.html.
228 PR NEWSWIRE, *Benzinga, Webull Announce Partnership to Streamline News and Data*, WEBULL (June 30, 2019), https://www.webull.com/blog/6-Benzinga-Webull-Announce-Partnership-To-Streamline-News-and-Data.
229 Alicia Adamczyk, *This is the Best Robo-Advisor for New Investors*, CNBC (Feb. 13, 2020, 11:43 AM), https://www.cnbc.com/2020/02/13/why-betterment-is-the-best-robo advisor-for-beginning-investors.html.
230 *Cf.* Lowe v. SEC, 472 U.S. 181, 191-92 (1985) (noting that investment counselors render to clients unbiased continuous advice on a personal basis).
231 *Compare* de Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293, 1302 (2d Cir. 2002) (explaining that brokers do not owe a duty to monitor a non-discretionary account because its duties and after each transaction) *with* Anwar v. Fairfield Greenwich Ltd., 891 F. Supp. 2d 548, 555-56 (S.D.N.Y. 2012) (distinguishing a passive broker from a broker who undertakes a substantial and comprehensive advisory role with respect to nondiscretionary accounts).
232 *See Anwar*, 891 F. Supp. 2d at 556.

analysis of client trading patterns for future news, stocks, and other relevant information.[233] These ancillary services may amount to a *per se* discretionary account when considering the age of the client base, lack of investor experience, and reliance placed on the broker. As such, a clear case for SEC regulatory intervention emerges. Nonetheless, the regulators and the law should take care that these investment firms may still flourish and innovate.

Considering the lack of clarity for consumers, potential conflicts of interest in compensation, and technological developments in the financial services industry, the SEC aimed to hold brokers to a higher standard called "Regulation Best Interest." In June 2018, the SEC released its new rule: broker-dealers must recommend securities that are in the best interests of their clients.[234] The SEC imposes four obligations upon OTPs: (1) to disclose information about their recommendations; (2) to apply diligence, care, skill, and prudence in recommendations; (3) to abide by policies that address conflict of interest; and (4) to comply fully with policies and procedures designed to implement the regulation.[235]

The disclosure requirement expands to a more general duty separate from federal anti-fraud provisions, and various SEC and FINRA rules.[236] Now, brokers must disclose whether the recommendation to the client comes from an investment adviser's perspective or only a broker-dealer's.[237] The care requirement obliges a broker to put their customers first, complementing the existing suitability requirements. Whether a broker uses reasonable care, diligence, skill, and prudence is determined by the following factors: (1) an understanding of risks associated with the recommendation and a reasonable basis that those risks are in the customer's best interests; (2) reasonable belief that the recommendation is in the customer's best interest based on the customer's investment portfolio; (3) reasonable belief that the recommended transactions are in the customer's best interest when viewed in aggregate, as well as individually.[238] As for the last two conflict of interest obligations, brokers must establish, maintain, and enforce written conflict of interest policies reasonably designed to disclose or eliminate material conflicts arising from financial incentives *associated with a recommendation*.[239]

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233 *See generally* Anam Bhatia, *Designing a Stock Market Research Tool*, UX PLANET (July 7, 2020), https://uxplanet.org/designing-a-stock-market-research-tool-74d6050d8296.

234 Ian Hunley, *Regulation Best Interest*, 38 REV. BANKING & FIN. L. 610, 610-11 (2019).

235 17 C.F.R. § 240.15l-1 (2019).

236 *See* Hunley, *supra* note 234, at 615.

237 *Id.*

238 *Id.* at 615-16.

239 *Id.* at 616-17

PFOF platforms needed a more transparent disclosure policy to ameliorate conflicts of interest. Still, retail investors prefer commission free trading because most OTPs have eliminated commissions altogether.[240] Lower costs of entering the market and faster execution of trades add immense value to investors who previously had no access. While PFOF opponents accurately point out the conflicts of interests between the broker, market maker, and investor, added disclosures would ensure that investors receive accurate information about order flow sales and trade execution quality.[241]

One area of additional concern is the accessibility of the disclosure reports. They admittedly contain a wealth of information. But retail investors rarely possess the sophistication required to digest the information provided.[242] It is far from clear that retail investors effectively understand the facts and terms described and their implications. An efficient solution might be to provide a simple two-page disclosure on the OTPs website or application, providing only key statistics and information. Mandating an easily digestible disclosure would bridge the communication gap between the broker-dealer and the client.

The care obligation fleshes out what brokers need to do for their customers. The circumstance-driven, best-interest inquiry likely comes from a reasonable broker's and customer's viewpoint—an objective standard. The care requirement here is higher than suitability because a recommendation may still violate care duties if the recommendation is less suitable than another similar security.[243] Fundamentally, the best interest requirement obligates a broker to present a *more suitable* recommendation.[244] In the context of OTPs, perhaps regulators will require brokers to perform additional inquiries into their customers before advertising trading in speculative markets. Perhaps instead of advertising about rare market gains, they will market towards a long-term investor class that seeks self-sufficiency. At the very least, OTPs will consider the implications of subtly encouraging excessive trading on their applications.

In the same self-regulating tradition as FINRA, the SEC should provide a minimum framework so brokers themselves create their own

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240 Matt Frankel, *Zero-Commission Trading: What You Need to Know*, THE MOTLEY FOOL (July 21, 2021), https://www.fool.com/the-ascent/buying-stocks/articles/zero-commission-trading-what-you-need-to-know/.

241 Tara Bernard, *Yes, You Can Get Free Trading. But There's Often a Catch.*, NEW YORK TIMES (Nov. 29, 2019), https://www.nytimes.com/2019/11/29/your-money/free-stock-trading.html.

242 *See* Steven M. Davidoff & Claire A. Hill, *Limits of Disclosure*, 36 SEATTLE U. L. REV. 599, 600 (2013).

243 *See* FINRA, RULE 2111 (2020).

244 *Id.*

additional policies for full compliance. Note that in contrast to the disclosure requirement, the conflict-of-interest requirements are specific to broker recommendations.[245] Some might critique this rule as too narrow, but the average investor's sophistication mandates the targeted disclosure systems. The broker should not have to disclose every single conflict in connection with its products nor will the average investor care about conflicts detached from their purchases.[246]

For the most part, Reg BI adequately considers both customer and broker needs. For decades, commentators have complained about the shortcomings of previous standards. The broker-dealer suitability standard proves too low to properly protect investors. At the same time, the imposition of fiduciary duties has either been struck down by courts or has only been implemented in limited capacities.[247] Most courts still hold that if an investor controls a non-discretionary account and retains the ability to make investment decisions no fiduciary duty exists.[248] Reg BI would give courts and FINRA clear codified principles and standards. While OTPs supposedly limit themselves to executing trades on behalf of their investors, their user base evidently trades differently from even the average retail investor.[249] Given the education and age demographic these investment applications serve, the SEC adds an important increased, but measured, protection for OTP clients.

Even in discount trading platforms, customers should expect that brokers have a reasonable basis to believe their recommendation is in the customer's best interests rather than what is exciting or trendy.[250] In 2021, the SEC has pursued a compliance inquiry against Charles Schwab for disclosure issues related to its robo-advisors.[251] Such inquiries into the increasingly popular technology reflect positively on Reg BI as a compliance and enforcement measure.

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245 *See* 17 C.F.R. § 240.15l-1(a)(2)(iii) (2019).

246 *See* Davidoff & Hill, *supra* note 242, at 599-601.

247 *See e.g.,* Hunley, *supra* note 234, at 613-14 (noting that executive agencies and legislation have unsuccessfully attempted to hold broker-dealers to a fiduciary standard).

248 In re Enron Corp. Sec., Derivative & "ERISA" Litig., 238 F. Supp. 3d 799, 849 (S.D. Tex. 2017), aff'd sub nom. Lampkin v. UBS Fin. Services, Inc., 925 F.3d 727 (5th Cir. 2019). Lampkin v. UBS Fin. Services, Inc., 925 F.3d 727 (5th Cir. 2019).

249 Liz Knueven, *Investing Apps Use 2 Tactics to Get People to Make Frequent and Potentially Risky Trades, According to a Behavioral Finance Expert*, BUS. INSIDER (Sept. 4, 2020), https://www.businessinsider.com/personal-finance/investing-apps-encourage-trade-more-often-2020-9.

250 *See* Smith, *supra* note 219.

251 Brian Chappatta & Benjamin Bain, *Schwab Taking $200 Million Charge for SEC Robo-Adviser Probe*, BLOOMBERG (July 2, 2021), https://www.bloomberg.com/news/articles/2021-07-02/schwab-to-take-200-million-charge-on-sec-investigation.

Furthering Reg BI objectives, FINRA could require an option to opt out of PFOF for these platforms in exchange for trading fees. The ability to opt out of PFOF orders would increase the democratization of market access.[252] At the same time, investors who prefer cost savings may still have the option to do so. The broker-dealer can always increase commissions for clients who opt out or take a loss to preserve clients who may try other product offerings.[253]

Reg BI obligations provide an incremental regulatory process for innovative financial services, which is preferable to overburdening these firms.[254] The conflict-of-interest disclosure obligation will make firms strengthen risk management and perform the necessary due diligence.[255] Likewise, the Client Relationship Summary Form seems effective despite grumblings from both brokers and investor advocates.[256]

Unsurprisingly, the SEC remains hesitant to touch the standard fee commission brokerage business. Reg BI only applies at the time the recommendation is given and does not impose any perpetual duty to monitor.[257] On balance, just because a broker-dealer gives a recommendation at one point shouldn't mean it has an ongoing duty hinged on that past recommendation. But since many OTPs claim they are "Execution-Only Businesses" and regularly state they do not give investment advice they can further argue that they do not have to abide by the Reg BI standard.[258] Ironically, although the inception of Reg BI accelerated because of modern OTPs, the SEC may have provided these market disrupting, commission free OTPs an exit from Reg BI scrutiny.

Despite their previous aggressive language, the Commission might find it preferable to wait and see if commission free OTPs really require additional duties. In short, this middle ground of a higher standard of care, but not quite reaching fiduciary duties allows for industry innovation while still protecting consumers. Maybe Reg BI is not meant to overhaul the securities business; rather, it only seeks to balance customer protection and customer choice—a fair principle.[259]

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252 GARY SHORTER, CONG. RSCH. SERV., IF11800, BROKER-DEALERS AND PAYMENT FOR ORDER FLOW (Apr. 2, 2021).
253 *See id.*
254 *See* Smith, *supra* note 219.
255 Ed McCarthy, *How Thoughts About the SEC's Regulation Best Interest Have Evolved*, PLAN ADVISOR (Apr. 8, 2022), https://www.planadviser.com/exclusives/thoughts-secs-regulation-best-interest-evolved/.
256 *Id.*
257 Kerr et al., *SEC Adopts a New Best Interest Standard of Conduct*, KL GATES (June 19, 2019), https://www.klgates.com/SEC-Adopts-A-New-Best-Interest-Standard-of-Conduct-06-19-2019.
258 *See id.*
259 *Id.*

V. CONCLUSION

Everyone enjoys cheaper access to products and services. OTPs empower investors because they give more access to the market where previously it was cost prohibitive. At the same time, these great innovations can come with some risks to the unwary investor.

Nonetheless, earlier experience in the market will create financial knowledge that most young adults have never possessed. This is an important benefit. Markets thrive on entrepreneurship and the individual's ability to properly manage resources. The Kauffman Index has indicated that entrepreneurial growth continues to rebound since the Great Recession.[260] Risk-taking behavior post-economic downturn itself does not raise any eyebrows; however, high-growth companies seem to create fewer jobs because of leverageable and cost-efficient technology.[261]

More and more Americans will need to take responsibility for their own financial futures as corporations offer fewer retirement benefits.[262] As more recognize this, the United States reports a boom in entrepreneurship even under the global pandemic.[263] Likewise, the average American's wealth has increased over time since the 2008 financial crisis, resulting in more money for people to invest compared to just a few decades ago.[264] As small money continues to expand in the stock market, regulators should adjust laws to protect these retail investors while still promoting risk-taking. As of mid-June 2021, retail investors now comprise about 10% of daily trading in stocks on the Russell 3000.[265]

We shall see whether Reg BI has constructed a proper framework for FINRA members to self-regulate or if more laws are needed to protect the public. Technological change tends to render old compliance standards

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[260] *See Entrepreneurial Growth Continues Rebound from Great Recession*, KAUFFMAN (Oct. 18, 2017), slumphttps://www.kauffman.org/currents/entrepreneurial-growth-continues-rebound-from-great-recession-slump-annual-kauffman-index-reports/.

[261] *Id.*

[262] Nathan Bomey, *'It's really over': Corporate pensions head for extinction as nature of retirement plans changes*, USA TODAY (Dec. 10, 2019), https://www.usatoday.com/story/money/2019/12/10/corporate-pensions-defined-benefit-mercer-report/2618501001/.

[263] Yusuf Berkan Altun, *Pandemic Fuels Global Growth Of Entrepreneurship And Startup Frenzy*, FORBES (Apr. 9, 2021, 8:20 AM), https://www.forbes.com/sites/forbestechcouncil/2021/04/09/pandemic-fuels-global-growth-of-entrepreneurship-and-startup-frenzy/?sh=6c5b02c07308.

[264] Nick Stonnington, *How Democratization Is Paving A Path Of Continued Growth In The Stock Market*, FORBES (Mar. 3, 2021, 12:40 PM), https://www.forbes.com/sites/forbesbusinesscouncil/2021/03/03/how-democratization-is-paving-a-path-of-continued-growth-in-the-stock-market/?sh=4a868af497f1.

[265] *Retail Investors Comprise 10 Pct Of US Daily Market Trading*, PYMNTS (June 30, 2021), https://www.pymnts.com/markets/2021/retail-investors-comprise-10-pct-of-us-daily-market-trading/ (the Russell 3000 includes 3,000 of the biggest stocks traded in the U.S., which account for some 98 percent of all equity securities in the country).

obsolete. Therefore, regulatory agencies must do more research into the market consequences of gamification for retail investors. Such agencies should inquire about the behavioral finance aspects of the brokerage business. As enforcers, it is their duty to maintain confidence in the markets and it would benefit the investing community at large to prevent further negative perceptions of brokerages.[266]

The markets should encourage broad participation. Underneath the news about outrageous stock market trades are actual businesses with employees, customers, and future value-adding projects. Players in the stock market invest not only in a corporation but in a broad system of mutual trust that sustains the economy.[267] If regulations suffice, fintech will continue to meet the demand for stock market democratization as well as create a path to financial freedom.

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266 STAFF OF SEC, SEC, STAFF REP. ON EQUITY OPTIONS MKT. STRUCTURE CONDITIONS IN EARLY 2021, at 43-44 (2021).

267 *Id.*