FENCING FIDUCIARY DUTIES

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This comment on the work of Professor Tamar Frankel builds on her encyclopedic discussion of the various types of duties that have been classified as "fiduciary." I argue for a more precise definition and more limited application of fiduciary duties which recognizes that their usefulness depends on their being limited and separated from other duties that apply in other settings. The fiduciary duty is appropriately construed as one of unselfishness,

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as distinguished from lesser duties of care, good faith and fair dealing, and to refrain from misappropriation. The fiduciary duty of unselfishness is appropriate only for a limited class of agency relationships in which the principal delegates open-ended power to the agent, and not for those who may exercise lesser power over the property of others, including co-investors, advisers, professionals, and those in confidential relationships. More broadly applying fiduciary duties could unnecessarily constrain parties from self-protection in contractual relationships, impose excessive litigation costs, provide an unsuitable basis for contracting, and impede developing fiduciary norms of behavior. This analysis of fiduciary duties helps address current issues, including those regarding the duties of brokers, dealers, and investment and mutual fund advisers. In short, fencing fiduciary duties protects both fiduciary and non-fiduciary relationships and enables parties to contract for the precise level of protection that is appropriate to the services they are purchasing.

INTRODUCTION

Tamar Frankel's book[1] is a broad, detailed, and much-needed work. It clarifies and explains the theoretical underpinning for an expansive version of fiduciary duties, and applies fiduciary theory to such contemporary problems as those in the securities industry, the professions, as well as corporate issues such as executive compensation. The book raises many important issues and deserves close attention by a broad range of legal scholars.

Without diminishing Professor Frankel's prodigious work, I argue for a smaller role for fiduciary duties. I maintain that fiduciary duties should be fenced into a limited area rather than allowed to roam freely on the range of human relationships.[2] This narrow definition recognizes the significant costs and potential ambiguities of fiduciary duties. It also enables fiduciary duties to better perform their specific disciplinary function within the broader range of constraints on the parties defined by other types of agency and contractual relationships.

An important basis of my approach and another distinction from that of Professor Frankel concerns the importance of contract to fiduciary duties. Professor Frankel sees fiduciary duties as distinct from contracts.[3] Indeed, this distinction often seems to characterize Professor Frankel's view of the fiduciary relationship as an island separate from the workaday world of arm's-length dealings. However, given the ubiquity of contracts in a capitalist economy, the fiduciary duty is most usefully viewed as a type of contract.

My analysis complements rather than refutes Professor Frankel's work. Frankel's analysis is so broad that it necessarily encompasses several areas that

[1] TAMAR FRANKEL, FIDUCIARY LAW (2011).

[2] This paper builds on my earlier work, Larry E. Ribstein, *Are Partners Fiduciaries?*, 2005 U. ILL. L. REV. 209.

[3] *See* FRANKEL, *supra* note 1, at 212-15.

are so far from its central concerns as to seem anomalous. A narrower and more precise conception of fiduciary duties better explains these anomalies.

The discussion proceeds as follows. Part I contrasts the broad Frankel view of fiduciary duties with my narrower view. Part II discusses implications of the narrow view for some specific duties that are often erroneously classified as fiduciary. Part III illustrates the consequences of the narrow view by showing how it deals with the important current issues of mutual fund compensation and broker-dealer duties.

I. Defining Fiduciary Duties

This Part contrasts Frankel's broad definition of fiduciary duties, based on the expansive category of entrustment, with my narrower view that focuses on a particular type of entrustment.

A. *Frankel's Definition*

In Frankel's view, fiduciary duties arise from services that involve entrustment of property or power and a risk of untrustworthiness that markets, the entrustor, and the trustee cannot adequately protect against.[4] Frankel discusses a broad range of relationships that have these characteristics, including those involving trustees, corporate directors, physicians, lawyers, brokers and dealers, spouses, and friends.[5] Many other relationships arguably involve some entrustment and therefore fit within Professor Frankel's definition, including those between controlling and minority shareholders, debtors and creditors, and contracting parties who are vulnerable to opportunistic conduct, or who have disparate knowledge, sophistication or power.

B. *Narrower View*

My definition of fiduciary duties, like Professor Frankel's, arises from the concept of entrustment. However, my definition focuses on the particular type of entrustment that arises from a property owner's delegation to a manager of open-ended management power over property without corresponding economic rights. Examples include relationships between management and dispersed owners in a traditional publicly held corporation, and between the trustee and beneficiaries of a trust. As in all economic agency relationships, the separation of control and economic ownership gives the manager or fiduciary an incentive to use her control to enrich herself rather than the property owner.[6] My definition of fiduciary duty is similar to that proposed by other scholars.[7]

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[4] *Id.* at 4-6.

[5] *Id.* at 42-62.

[6] Ribstein, *supra* note 2, at 215.

[7] *See* Matthew Conaglen, *The Nature and Function of Fiduciary Loyalty*, 121 L.Q. Rev.

There are two critical differences between Frankel's and my definitions of fiduciary relationships. The most obvious concerns the open-endedness of the delegation of power my definition specifies. The basic intuition underlying this limitation is that with less extensive delegations of power, less drastic and costly constraints are sufficient to adequately constrain the power-holder. For example, the principal may be able to observe the manager's behavior and thus fire her or reduce her compensation when behavior or output is unsatisfactory. But such constraints or supervision are impractical where the principal delegates open-ended control, necessitating court review and action.

The second difference between Frankel's and my conceptions of fiduciary duties is that my view of the fiduciary relationship is necessarily contractual; one becomes a fiduciary only by contract, including by contracting for a relationship in which the law says fiduciary duties arise.[8] Under this view, the law should not impose fiduciary duties on one who has superior knowledge or expertise irrespective of the party's agreement to be a fiduciary. The general law of contract deals with knowledge or expertise disparities by invalidating or interpreting the contract rather than by imposing extra substantive duties. Other implications of the contractual approach are discussed below.

A fiduciary relationship differs from the broader category of agency relationships.[9] Both involve forms of entrustment.[10] In an agency relationship, as in a fiduciary relationship, a principal who owns property with residual economic rights entrusts control of the property to an agent.[11] The resulting separation of ownership and control means the agent might manage the property so as to realize benefits without incurring the full costs of her conduct.[12] Because the principal can negotiate to be paid to cover the risks resulting from separation of ownership and control, both parties have incentives to contract for monitoring and bonding mechanisms – including incentive compensation and control devices – designed to minimize these risks.[13] Fiduciary duties are just one type of device for controlling agent

452, 459-60 (2005); Robert Cooter & Bradley J. Freedman, *The Fiduciary Relationship: Its Economic Character and Legal Consequences*, 66 N.Y.U. L. REV. 1045, 1048 (1991); L.S. Sealy, *Fiduciary Relationships*, 1962 CAMBRIDGE L.J. 69, 74-79 (discussing categories of fiduciary duties but indicating that each incorporated an obligation of loyalty); J.C. Shepherd, *Towards a Unified Concept of Fiduciary Relationships*, 97 LAW Q. REV. 51, 75 (1981) (defining a fiduciary relationship as a "duty to utilise that power in the best interests of another"); D. Gordon Smith, *The Critical Resource Theory of Fiduciary Duty*, 55 VAND. L. REV. 1399, 1406 (2002) (defining fiduciary duty as a duty of loyalty or unselfishness).

[8] For a similar contractual characterization of fiduciary duties, see Frank H. Easterbrook & Daniel R. Fischel, *Contract and Fiduciary Duty*, 36 J.L. & ECON. 425, 427 (1993).

[9] *See* Ribstein, *supra* note 2, at 224.

[10] *Id.*

[11] *Id.*

[12] *See* Cooter & Freedman, *supra* note 7, at 1048.

[13] *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976).

misconduct.[14] In short, a fiduciary relationship necessarily is an agency relationship but an agency relationship is not necessarily a fiduciary relationship.[15]

C. *Reasons for the Narrow View*

One may wonder why a fiduciary duty should be limited to a relatively small part of the broader category of entrustment situations. After all, judicial supervision through fiduciary duties would seem to make sense for any long-term relationship in which one party must depend on the faithfulness of another. The following subsections show how limitations arise from judicial review, the extra-legal functions of fiduciary duties, the costs of open-ended terms, and the relationship between fiduciary duties and explicit contract terms.

1. The Nature of Fiduciary Duties

One of the most famous judicial expressions of fiduciary duties is that of Justice Cardozo in *Meinhard v. Salmon*[16]:

> Joint adventurers, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty. . . . A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior.[17]

Justice Cardozo added that "thought of self was to be renounced, however hard the abnegation,"[18] leaving no doubt that the fiduciary duty is one of selfless behavior. As Justice Cardozo emphasized, this contrasts sharply with the norm of self-interest that generally prevails in the marketplace.[19] The importance of this expression of fiduciary duty is indicated by almost four hundred U.S. cases that have quoted the sentence including "punctilio of an honor."[20]

The strictness of the fiduciary duty helps explain its limited scope. A duty of self-abnegation is only rarely appropriate in a competitive marketplace. Such a duty is usually excessively costly when applied to commercial dealings because it undermines the incentives that motivate business people to provide high-quality goods and services.

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[14] For a general review of other devices, see THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH (Reinier Kraakman et al. eds., 2d ed. 2009).

[15] Ribstein, *supra* note 2, at 224.

[16] 164 N.E. 545 (N.Y. 1928).

[17] *Id.* at 546.

[18] *Id.* at 548.

[19] *Id.*

[20] A Westlaw search on this phrase in the "allcases" database on November 28, 2010 had 382 results.

This poses another question of why the default fiduciary duty should require avoidance of all conflicts of interest. Why not instead a default rule allowing disclosed conflicts as long as the fiduciary can show she nevertheless acted in the beneficiary's best interests? The additional considerations discussed in the following subsections help answer this question.

2. Limited Judicial Capacity

An important characteristic of the strict fiduciary duty of selflessness is that it is easier for courts to apply than alternative formulations of the fiduciary duty. For example, a duty not to harm the beneficiary would require proof that the fiduciary made the beneficiary worse off and that the fiduciary caused this deterioration. Since the beneficiary likely delegated management responsibility to the fiduciary because of the latter's expertise, second-guessing the fiduciary's performance ordinarily requires at least comparable expertise. By contrast, a court applying a duty of selflessness enables the beneficiary to recover the fiduciary's benefit from the relationship without necessarily requiring the beneficiary to show harm. Therefore the court evaluates the fiduciary's exercise of judgment.

3. Interaction with Other Contractual and Market Constraints on Power-Holders

Limiting the scope of the fiduciary duty helps reconcile it with other ways to control entrustment of power to agents, including consent or voting by entrustors, rules enabling exit from the relationship, and disclosure. Combining these devices with fiduciary duties may reduce their efficiency and entail unnecessary costs. For example, imposing a fiduciary duty on a party with voting or exit power may reduce that party's ability to self-protect against potential abuse by one entrusted with managerial power. By contrast, parties in the limited category of relationships involving open-ended delegation of power cannot contract to limit the manager's power without undermining the beneficiary's objective in delegating power. This makes an additional fiduciary duty appropriate.

The fiduciary duty of selflessness must be evaluated in the context not only of contractual constraints but also of market and other extralegal constraints on fiduciaries' conduct. Parties' self-interest usually can motivate them to act reasonably carefully where they are effectively disciplined by the product and job markets. But a self-dealing fiduciary's self-interest can overwhelm these extra-legal constraints. This intuition supports defining the fiduciary duty in terms of loyalty rather than care.

The duty of selflessness may be excessively costly even in some fiduciary settings. This helps explain why, as discussed below, it is so important to enforce contractual variation of fiduciary duties. Even if the parties often contract around the fiduciary duty, it is still effective as a default rule because it requires the fiduciary to get the entrustor's consent to engage in self-dealing. Those who hold power as non-fiduciaries, by contrast, generally may engage in self-dealing without obtaining the entrustor's consent as long as they disclose conflicts.

4. Litigation Costs

Setting clear boundaries for fiduciary duties can reduce the frequency and costs of litigation. High litigation costs can be a tax on transactions and complicate planning. Where the party subject to the duty is likely to bear most of the costs of any litigation, the other party's power to force litigation could transform her into a kind of trustee. This could trigger the need for more contracting. Indeed, under Professor Frankel's approach, it could even entail a reciprocal fiduciary duty to refrain from self-interested litigation.

5. Fiduciary Duties and Behavioral Norms

Fiduciary duties can be helpful in establishing behavioral norms that supplement the law. Consistent with this goal, Justice Cardozo used strong and colorful language in *Meinhard* to describe the intensity of fiduciary duties and therefore the shame that should result from breach.[21] Fiduciary law can help express when norm violations occur, and therefore when conduct should trigger society's informal shaming sanction for norm violation.[22] Commentators have argued that fiduciary standards frame corporate managers' roles as calling for high amounts of trust rather than self-interest.[23] Fiduciary duties also help signal when behavior crosses a moral line and deserves condemnation.[24] Fiduciary duties cannot play this norm-enforcement role if they are amorphous and traversed by ordinary market behavior or commonplace breach of contract.

Fiduciary duties' norm-creation function highlights problems with Professor Frankel's broad entrustment theory. Trust's several meanings weaken its ability to create fiduciary norms.[25] Trust in its broadest sense simply describes a person's willingness to engage in entrustment.[26] As Professor Frankel notes, this sort of "subjective" trust does not get us very far in defining duties.[27] Trust in a narrower "strong form" sense can arise even in the absence of legal enforcement where parties adhere to norms of trusting and trustworthy behavior.[28] Inappropriate legal remedies can be counterproductive by

[21] Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928).

[22] David A. Skeel, Jr., *Shaming in Corporate Law*, 149 U. PA. L. REV. 1811, 1812 (2001).

[23] *See, e.g.*, Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735, 1738 (2001).

[24] *See* FRANKEL, *supra* note 1, at 104.

[25] *See* Larry E. Ribstein, *Law v. Trust*, 81 B.U. L. REV. 553, 556-58 (2001).

[26] *See id.* at 557.

[27] FRANKEL, *supra* note 1, at 12 (recognizing that the "necessary degree of trust in a fiduciary relationship must be quite high").

[28] *See* Ribstein, *supra* note 25, at 557-58 (distinguishing these various meanings of trust).

"crowding out" strong form trust.[29] A fiduciary duty to refrain from self-dealing helps create norms where they are most needed as a basis for strong-form trust.[30] On the other hand, equating fiduciary duties with the broad concept of entrustment would not assist norm creation or create trust other than the subjective reliance that legal penalties can create.[31]

6. Facilitating Contracts

As noted above and discussed further below, fiduciary duties are essentially contractual in the sense that they arise from contractual relationships that carry with them default fiduciary duties.[32] Viewed from this perspective, fiduciary duties raise the question of when they should be the default rule. Broadly applying fiduciary duties to different types of transactions may complicate parties' ability to determine the precise duty that applies to their relationship or transaction, and therefore makes it difficult to use the default rule as a basis for contracting.

II. IMPLICATIONS OF THE NARROW VIEW

This Part discusses some specific consequences of the broad and narrow approaches to defining fiduciary duties and to determining which duties are fiduciary in nature and when fiduciary duties should be applied.

A. *Contract and Fiduciary Duties*

Perhaps the most important policy question regarding the various approaches to fiduciary duties concerns the enforceability of contracts modifying or eliminating fiduciary duties. As noted in the Introduction, my emphasis on contract importantly distinguishes my and Professor Frankel's theories.

Professor Frankel emphasizes the need to separate fiduciary and market principles.[33] In order to analyze this separation, it is important to identify what is at stake. Fiduciary duties are clearly created by contract in that one can decide whether to be a party to a relationship that includes these duties as a default term.[34] The fact that fiduciary duties are imposed by default rule rather than by explicit agreement should not take them out of the contractual realm, anymore than default rules are inconsistent with contracts in myriad other

[29] *See* BRUNO S. FREY, NOT JUST FOR THE MONEY 8-18 (1997); Iris Bohnet et al., *More Order with Less Law: On Contract Enforcement, Trust, and Crowding*, 95 AM. POL. SCI. REV. 131, 132 (2001).

[30] *See* Ribstein, *supra* note 25, at 565-66.

[31] *Id.*

[32] *See supra* Part I.C.3; *infra* Part II.A.

[33] *See* FRANKEL, *supra* note 1, at 239; *id.* at 234 (enforcing contracts would increase trustees' temptation to abuse their trust).

[34] *See* Easterbrook & Fischel, *supra* note 8, at 427 (concluding that a fiduciary relationship is also a contractual one, with the same sort of obligations as a contract).

settings. Nor should it be significant that a fiduciary's default obligations differ from those of other contracting parties. A variety of default rules designed for different types of transactions enables parties to contract cheaply for a wide range of market relationships. Fiduciary duties are suited to a contract providing for an open-ended delegation of power.

The specific question regarding the contractual nature of fiduciary duties is whether one who contracts for a relationship that has the fiduciary characteristic of open-ended delegation of power without economic rights may contract out of the fiduciary duty that accompanies this power? In other words, are fiduciary duties necessarily bundled with fiduciary powers? Mandatory bundling would not necessarily make fiduciary duties "non-contractual," since many types of contracts are limited by mandatory rules. However, bundling importantly constrains the range of contracts that parties can make regarding fiduciary duties.

Parties should be able to contractually adjust the terms of a fiduciary relationship. Frankel argues that the contractarian approach to fiduciary duties ignores the parties' unequal bargaining position.[35] To be sure, a fiduciary relationship implies disparities of information and expertise between the fiduciary and the entrustor.[36] But it does not follow that the entrustor necessarily is disadvantaged when negotiating restrictions on fiduciary duties and remedies at the beginning of the relationship. The market for fiduciary services produces information regarding fiduciaries' prior conduct and reputation for reliability.[37] Entrustors engaged in business may have special skills in evaluating potential trustees and be able to design contractual incentives and remedies that efficiently substitute for fiduciary duties. Fiduciaries have incentives to offer credible information about themselves and assurances because entrustors can choose what types of fiduciary services to buy and from whom.

Instead of forbidding fiduciary contracts, the law might impose conditions on how parties contract around fiduciary duties that take account of the special circumstances of fiduciary relationships, particularly including the inherent disparity of knowledge and sophistication between entrustor and trustee.[38] For example, courts and legislatures might require fiduciaries to make affirmative disclosures, obtain explicit consent to modifications, or specify a minimal level of duties and remedies.

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35 *See* FRANKEL, *supra* note 1, at 232.

36 *Id.*

37 *See* Benjamin Klein & Keith B. Leffler, *The Role of Market Forces in Assuring Contractual Performance*, 89 J. POL. ECON. 615, 615-17 (1981) (discussing contract enforcement through repeat performance).

38 *See* FRANKEL, *supra* note 1, at 197 (discussing how to release fiduciary duties); John H. Langbein, *Mandatory Rules in the Law of Trusts*, 98 NW. U. L. REV. 1105, 1122-23 (2004).

The contractual perspective helps solve the otherwise puzzling problem of how to deal with fiduciaries' compensation. Frankel notes that fiduciary duties do not deal with compensation.[39] My analysis makes compensation an exception to the general anti-self-dealing rule at the heart of fiduciary duties. Although a fiduciary may have disclosure and other duties regarding negotiations over compensation and other matters, a strict across-the-board application of the duty not to self-deal would leave the parties unable to adjust their relationship over time. Fiduciary duties therefore should be reconciled with, rather than completely separated from, contract.

B. *Non-fiduciary Duties*

The fiduciary duty is properly conceived as simply one to refrain from self-dealing.[40] Fiduciary duties so defined fit with other duties that have been erroneously placed in the "fiduciary" category.

1. Duty of Care

Fiduciaries commonly have a duty of care.[41] However, this is not a fiduciary duty, which as described above is a duty of unselfishness.[42] As discussed above, a fiduciary duty substitutes relinquishing gain for submitting to judicial evaluation of services rendered.[43] The duty of care is generally an implied term concerning the manner of a contract's performance for professional services or agency relationships.[44] Although these relationships involve some degree of entrustment, as discussed below they do not necessarily entail the open-ended delegation of power that characterizes a fiduciary relationship.[45] Thus, the Supreme Court has held that a doctor's duty

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[39] *See* FRANKEL, *supra* note 1, at 101-93.

[40] *See id.* at 1-6. It has been said that fiduciary "loyalty" differs from other duties in that it serves primarily as a prophylactic "which enhances the chance that . . . non-fiduciary duties will be properly performed." Conaglen, *supra* note 7, at 453. This is still a fiduciary duty limited to loyalty, albeit one that borrows its precise content from the nature of the parties' relationship in the specific case.

[41] *See* Ribstein, *supra* note 2, at 220.

[42] *See* J.C. SHEPHERD, LAW OF FIDUCIARIES 49 (1981) (arguing that a duty of care is not necessarily fiduciary in nature); Conaglen, *supra* note 7, at 456 ("The duty of care is not peculiar to fiduciaries . . . .").

[43] *See supra* Part I.B.

[44] *See* Knopick v. Connelly, Civ. 09-1287, 2010 WL 411701, at *5 (M.D. Pa. Jan. 25, 2010) (indicating that an "implied duty of care [is] owed by every attorney to their clients"); Lashure v. Felts, 197 P.3d 885, 891 (Kan. Ct. App. 2008) (finding that there is a duty of care implied in every professional services agreement with a doctor).

[45] *See* Ribstein, *supra* note 2, at 229 (examining how other confidential relationships do not necessarily involve the broad, open-ended delegation of power that creates fiduciary obligations).

of care did not make him the patient's fiduciary, observing that a contrary result would be an "erroneous corruption of fiduciary obligation."[46]

2. Misappropriation

The duty not to misappropriate information, business opportunities, or other property is not a fiduciary duty.[47] It simply reflects the limits on business owners' and agents' rights to property owned by the firm.[48] In other words, these duties are a function of the owners' joint rights in the firm rather than a fiduciary obligation to forego all gain. Thus, for example, even a minority shareholder or a joint venturer would have a duty not to misappropriate property or opportunities that belong to the firm even without being what this Article would label a fiduciary.

3. Good Faith and Fair Dealing

The general duty of good faith may be simply another way to refer to the fiduciary duty of selfless conduct. The implied covenant of good faith and fair dealing, however, has a different meaning as a duty that all contracting parties have and whose content is derived from the parties' agreement.[49] This is less a separate duty than an approach to interpreting contracts.[50] In contrast to fiduciary duties, the implied covenant enables contracting parties to act selfishly as long as this conduct is at least broadly consistent with the parties' ex ante expectations based on the contract.[51]

4. Social Responsibility

Any duty fiduciaries and other agents have to society as a whole rather than to specific entrustors would not be a fiduciary duty.[52] The fiduciary duty to avoid self-dealing is not defined with reference to the specific parties on whose behalf the fiduciary must act. Social responsibility generally relates to whether corporate managers have breached their duty of care or acted outside the

46 Pegram v. Herdrich, 530 U.S. 211, 235 (2000).

47 *See* Ribstein, *supra* note 2, at 221.

48 *Id.*

49 *Id.* at 223 (asserting that a duty of good faith is applied in a given case based on the parties' contract terms); Conaglen, *supra* note 7, at 456 (explaining that the good faith duty "is frequently recognized in circumstances not traditionally considered to be fiduciary relationships" including decisions involving exercise of discretionary powers in contracts "based on the contractual terms and factual matrices of the particular cases").

50 *See, e.g.*, Larry E. Ribstein, *Fiduciary Duties and Limited Partnership Agreements*, 37 SUFF. U. L. REV. 927, 938 (2004).

51 *See* Katz v. Oak Indus., Inc., 508 A.2d 873, 880 (Del. Ch. 1986) (reasoning that the duty depends on whether it is "clear from what was expressly agreed upon that the parties who negotiated the express terms of the contract would have agreed to proscribe the act later complained of").

52 *See* FRANKEL, supra note 1, at 166.

business judgment rule by seeking to benefit society rather than the corporation.[53] Since courts have limited ability to second-guess business decisions, they must give non-self-dealing managers wide leeway in making these decisions by refusing to impose liability except for decisions that egregiously waste corporate assets.[54] A distinct fiduciary duty to society accordingly is unnecessary to enable managers to fulfill whatever social responsibilities firms might have.[55]

C. *Non-fiduciaries*

For the reasons discussed in Part I, the fiduciary category should be confined to open-ended delegations of control in order to best serve fiduciary duties' functions.[56] This subpart distinguishes other types of relationships that some commentators, including Professor Frankel,[57] place in the fiduciary category.

1. Co-investors

Although partners, majority shareholders, and creditors may control the firms in which they invest, this control is not necessarily open-ended enough to warrant fiduciary treatment.[58] The control exercised by ownership factions often is carefully negotiated and limited to the power to approve major transactions and, in corporations, to elect directors.[59] This power is constrained by other contract terms, including those defining voting rights, dissociation, dissolution and appraisal rights, and profit shares.[60]

It follows from this analysis that partners do not have fiduciary duties merely as such unless, as in *Meinhard*, they hold fiduciary-type, open-ended control.[61] The power of even a majority is limited by the minority's power to cash out of the firm. Even a partner who contributed most of the funding may be outvoted by two service-only partners under the one-partner-one-vote partnership default rule.[62]

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[53] *See* Larry E. Ribstein, *Accountability and Responsibility in Corporate Governance*, 81 NOTRE DAME L. REV. 1431, 1468-73 (2006).

[54] *See* Daniel R. Fischel & Michael Bradley, *The Role of Liability Rules and the Derivative Suit in Corporate Law: A Theoretical and Empirical Analysis*, 71 CORNELL L. REV. 261, 283-84 (1986) (describing the rationale behind the business judgment rule).

[55] *See* Ribstein, *supra* note 53, at 1473.

[56] *See supra* Part I.B.

[57] *See* FRANKEL, *supra* note 1, at 43.

[58] *See* Ribstein, *supra* note 2, at 224-27.

[59] *Id.* at 224-25.

[60] *Id.* at 224-27.

[61] *See* Ribstein, *supra* note 2, at 237.

[62] *See* Uniform Partnership Act § 18(e) (1914) ("All partners have equal rights in the management and conduct of the partnership business."); *see also* Revised Uniform Partnership Act § 401(f) (1997) (providing similarly for equal voting among partners).

Majority shareholders in corporations may exercise more power than partners because in corporations voting rights usually follow financial investments. However, even these shareholders are often constrained by other corporate mechanisms, including shareholder appraisal rights and supermajority and class voting. Corporate voting rights are designed to balance the potential for abuse of power with majority shareholders' need to use voting rights to protect their interests. The constraints on majority shareholders' power and the recognition that majority shareholders vote in their self-interest are inconsistent with fiduciary duties.[63] Majority shareholders have only a duty not to engage in self-dealing that harms minority shareholders.[64]

Shareholders' relationship with creditors illustrates the classic agency problem of separation of ownership and control because shareholders fully control a solvent firm's assets while contributing only part of the capital.[65] Yet, as Professor Frankel observes, shareholders do not owe fiduciary duties to creditors.[66] This is one of the puzzles that the narrow view of fiduciary duties explains better than Professor Frankel's broad approach. Shareholders are not fiduciaries as to creditors because they lack fiduciary-like, open-ended power to control funds contributed by creditors.[67] Creditors are entitled to scheduled principal and interest payments and, unlike shareholders, do not trust corporate managers with discretion over the open-ended residual that remains after payment of loan charges and other expenses.[68] Managers' and directors' wide discretion to control this residual justifies their strong fiduciary duty of unselfishness to shareholders qualified by the corporation's agreement to compensate managers for their services.

Investors lack fiduciary duties even if they might be said to have special powers over co-investors' funds attributable to the "asset-specificity" of these other investments.[69] Investments of labor, credit, and capital in enterprises often are effectively tied to other resources of the specific enterprise, and therefore are vulnerable to hold-up by other investors.[70] For example, much of a firm's value may depart with an investor or worker who has or controls

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63 Ribstein, *supra* note 2, at 225.

64 *See, e.g.*, Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) ("Self-dealing occurs when the parent, by virtue of its domination of the subsidiary, causes the subsidiary to act in such a way that the parent receives something from the subsidiary to the exclusion of, and detriment to, the minority stockholders of the subsidiary.").

65 *See* Jensen & Meckling, *supra* note 13, at 312.

66 *See* FRANKEL, *supra* note 1, at 39-41.

67 Ribstein, *supra* note 2, at 225.

68 *Id.* at 226 (citing Katz v. Oak Indus., Inc., 508 A.2d 873, 879 (Del. Ch. 1986)).

69 *See* Benjamin Klein, Robert G. Crawford & Armen A. Alchian, *Vertical Integration, Appropriable Rents, and the Competitive Contracting Process*, 21 J.L. & ECON. 297, 300-01 (1978).

70 *See id.*

access to critical assets or skills.[71] It follows that the investor or worker may be able to extract some of the value she adds to the business by threatening to leave. This leverage might seem to endow the manager with fiduciary-like power. However, the power can be constrained by specific contractual provisions that make fiduciary duties unnecessary. Imposing fiduciary duties also could interfere with the power-holder's ability to self-protect by exercising her contractual rights. Accordingly, contracting parties who use their contractual powers and leverage to extract benefits from the other parties are subject only to their contract interpreted in light of the implied covenant of good faith and fair dealing.[72]

2. Advisers and Professionals

Professor Frankel sees professionals like physicians, lawyers, brokers and dealers as fiduciaries.[73] For example, Frankel's fiduciary duty would apply to the physician's misappropriation of a patient's cell tissue[74] or a lawyer's stretching her billable hours.[75] However, under my approach, an adviser or professional does not have, by virtue of that status alone, the sort of open-ended power that requires the strong fiduciary duty against self-dealing. Rather, any adviser or professional fiduciary duties would depend on how the parties structured their deal. The advice seeker can decide precisely what to buy from the professional or adviser, from advice on a specific transaction to entrustment of broad responsibility of the client's assets. For example, in *Burdett v. Miller*, the court found that a financial adviser was a fiduciary when he "knew that [his client] took his advice uncritically and unquestioningly and that she sought no 'second opinion' or even . . . any documentary confirmation of the investments to which he steered her."[76]

The absence of a fiduciary duty based solely on an adviser or client relationship reflects the sharp distinction between fiduciary relationships and general market transactions. Market participants are expected to act self-interestedly.[77] A similar expectation does not apply to fiduciaries because the open-ended nature of the fiduciary's power over the entrustor's property

[71] *See id.*

[72] *See supra* Part II.B.3.

[73] *See* FRANKEL, *supra* note, 1 at 43; *see also* RESTATEMENT (SECOND) OF TORTS § 874 cmt. a (1979) ("A fiduciary relation exists between two persons when one of them is under a duty to act for or to give advice for the benefit of another upon matters within the scope of the relation.").

[74] *See* FRANKEL, *supra* note 1, at 109-11 (discussing Moore v. Regents of Univ. of Cal., 793 P.2d 479, 488-91 (Cal. 1990), *cert. denied*, 499 U.S. 901 (1991)).

[75] *Id.* at 112-13.

[76] Burdett v. Miller, 957 F.2d 1375, 1381 (7th Cir. 1992).

[77] *See* ADAM SMITH, THE WEALTH OF NATIONS 572 (Edwin Cannan ed., Bantam Dell 2003).

demands a special level of behavior.[78] One who is only an adviser or professional sells advice, not management. The client purchases the advice and then, like the purchaser of any product, can decide what to do with it. Applying fiduciary duties to all advisers and professionals therefore would be unrealistic and would dilute the concept of fiduciary duties.

The non-fiduciary characterization of advisers and professionals might seem suspect because conflicts of interest matter to them as they do to fiduciaries.[79] The advice's value depends on whether it is tainted by self-interest.[80] Investment advice, for example, may be a "credence good" whose value is not apparent at the time of sale.[81] Indicia of soundness, such as the absence of conflicts, enable clients to evaluate the advice. An advice seller accordingly may have to disclose material conflicts that significantly affect the value of the advice, just as the seller of any product may be required to disclose important features of the product. If the adviser breaches a duty of disclosure, the client can sue for what amounts to fraud, recovering damages attributable to reliance on the absence of a material conflict.[82]

Contrast this situation with the fiduciary context. One who decides not only to obtain advice from an expert but to entrust her property to the expert's management ceases to make her own decisions concerning whether and how much to rely on each of the fiduciary's judgments.[83] This open-ended delegation of control to the fiduciary calls for more than mere disclosure of material facts.[84] The conflicted fiduciary who has not obtained the entrustor's explicit consent to conflicts accordingly is liable for gains from her self-dealing.[85]

Commentators who argue for fiduciary duties of brokers and other investment advisers emphasize conflicts inherent in these advisers' commission-based compensation.[86] These conflicts are, indeed, in tension with the customer's assumption that the adviser's advice is unbiased. The

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[78] Ribstein, *supra* note 2, at 216-17.

[79] *See* Benjamin Cummings & Michael S. Finke, The Economics of Fiduciary Investment Advice 2-4 (Sept. 1, 2010) (unpublished manuscript), *available at* http://ssrn.com/abstract=1701181.

[80] *Id.* at 2.

[81] *See id.*; *see also* Michael R. Darby & Edi Karni, *Free Competition and the Optimal Amount of Fraud*, 16 J.L. & ECON. 67, 68-72 (1973) (discussing the general nature of credence goods).

[82] *See, e.g.*, *In re* Atl. Fin. Mgmt., Inc. Sec. Litig., 658 F. Supp. 380, 382 (D. Mass. 1986) (describing a suit for fraud caused by a failure to disclose extant conflicts of interest).

[83] Ribstein, *supra* note 2, at 215.

[84] *See id.*

[85] *Id.* at 216.

[86] *See* James J. Angel & Douglas McCabe, Ethical Standards for Stockbrokers: Fiduciary or Suitability? 6 (Sept. 30, 2010) (unpublished manuscript), *available at* http://ssrn.com/abstract=1686756; Cummings & Finke, *supra* note 79, at 3.

solution is better designed compensation, or explicit disclosure of the risk.[87] Because compensation is an exception to rather than an inherent aspect of a fiduciary relationship, it is not an appropriate basis for creating a fiduciary relationship. Nor should sale of securities or other products accompanied by advice be deemed to create a fiduciary relationship. The adviser-seller's self-interest should be obvious to the buyer even without explicit disclosure.

3. Confidential Relationships

Fiduciary duties do not necessarily arise from "confidential" relationships such as those between spouses, parents and friends.[88] These relationships in themselves do not involve the open-ended delegation of power that characterizes a fiduciary relationship. The only duty that necessarily arises from a confidential relationship is associated with the parties' expectation that they will keep information confidential.[89] Family members and others in a confidential relationship are otherwise legally free to act in their self-interest unless they contract for a fiduciary relationship.[90] Indeed, fiduciary duties may even interfere with the intimacy that is essential to the relationship by "crowding out" trust.

III. APPLICATIONS OF THE THEORY

This Part discusses two recent and important issues that highlight the distinctions between the narrow and broad views of fiduciary duties discussed above. Mutual fund compensation and broker-dealer duties illustrate the problems of extending fiduciary duties beyond their appropriate bounds, as well as those of importing this distinctly common law concept into federal statutes.

A. *Mutual Fund Compensation*

The application of fiduciary duties in the mutual fund context recently reached the Supreme Court in *Jones v. Harris Associates*.[91] This case involved the so-called "fiduciary duty" Congress applied in section 36(b) of the Investment Company Act of 1940 to mutual fund advisers.[92] Professor Frankel notes the case throughout her book, but does not fully grapple with the

[87] *See* Angel & McCabe, *supra* note 86, at 17-18.

[88] *See* Margaret Brinig, *Parents, Trusted but not Trustees or (Foster) Parents as Fiduciaries*, 91 B.U. L. REV. 1231, 1246-47 (2011) (concluding that parents are not fiduciaries).

[89] *See* United States v. Chestman, 947 F.2d 551, 567-71 (2d Cir. 1991) (holding that there was no fiduciary duty regarding information related to a family corporation).

[90] Ribstein, *supra* note 2, at 228-29.

[91] 130 S. Ct. 1418, 1422 (2010). The following discussion is based on the analysis of that case in Larry E. Ribstein, *Federal Misgovernance of Mutual Funds*, 2009-2010 CATO SUP. CT. REV. 301 (2010).

[92] *Jones*, 130 S. Ct. at 1422-23.

problems of placing this case in the fiduciary category, which are characteristic of the broad approach to fiduciary duties.[93]

In this situation, the adviser arguably should not have a default fiduciary duty because it nominally only advises the fund's board of directors, which technically holds the open-ended, fiduciary-like management power. However, this conclusion is muddied by the odd structure of the mutual fund industry that federal law has created. A mutual fund firm establishes various funds which are essentially products sold to investing consumers. The products are designed by the investment advisers, with boards existing mainly for compliance purposes consistent with the corporate-type structure the act mandates. The advisers' power is constrained by investors' ability to get the current value of their investments back from the fund at any time.[94] More importantly for present purposes, even if mutual fund advisers might be considered fiduciaries under state common law, the section 36(b) "fiduciary duty" applies only to compensation, which as discussed above is a contractual opt-out from the fiduciary duty.

Section 36(b) probably does not create a fiduciary duty in the sense discussed in this Article despite its use of fiduciary terminology. Notably, the duty is imposed on the adviser, which is contracting for compensation, rather than the fund's board which actually decides the compensation.[95] As discussed above, a corporate board's function is to mitigate any problems resulting from a fiduciary's negotiating its own compensation.[96] This eliminates the need for a broad fiduciary duty of selflessness, which would be inconsistent with the obviously selfish nature of the compensation negotiation. Section 36(b) also removes the moral gloss normally associated with fiduciary duties by providing that breach of the duty is not a basis for remedies under other sections of the securities laws.[97] The section's allocation of the burden of proof to the plaintiff is inconsistent with the supposed disparity of information and sophistication that normally exists between fiduciaries and their entrustors. These characteristics of the section 36(b) duty support Judge Easterbrook's conclusion that section 36(b) should entail no more than a duty to disclose and to refrain from any "tricks."[98]

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[93] FRANKEL, *supra* note 1, *passim*.

[94] *See* D. Bruce Johnsen, *Myths About Mutual Fund Fees: Economic Insights on* Jones v. Harris, 35 J. CORP. L. 561, 592 (2010).

[95] *See Jones*, 130 S. Ct. at 1422.

[96] *See supra* Part II.C.2.

[97] Investment Advisers Act of 1940 § 36(b), 15 U.S.C. § 80a-35(b) (2006).

[98] Jones v. Harris Assocs. L.P., 527 F.3d 627, 632 (7th Cir. 2008), *rev'd* 130 S.Ct. 1418 (2010). A similar approach arguably should apply to the Delaware Supreme Court's newly imposed fiduciary duty in the corporate officer context in *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009). *See* Randall S. Thomas & Harwell Wells, *Executive Compensation in the Courts: Board Capture, Optimal Contracting, and Officer Fiduciary Duties*, 95 MINN. L. REV. 846, 896, n.318 (2011).

This case illustrates the dangers of over-applying fiduciary duties. The "fiduciary" label set up a dissonance between the duty that was appropriate to the situation – that is, the one Judge Easterbrook found – and an actual fiduciary duty of unselfishness.[99] The courts' efforts to give meaning to Congress's language resulted in the proliferation of wasteful litigation in which the courts never found a breach of duty but plaintiffs continued to pursue the settlement value conferred by the "fiduciary" label.

B. *Brokers, Dealers, and Advisers*

Professor Frankel's broad conception of fiduciary duties is likely to play a central role in determining the scope of broker-dealer duties in the wake of Dodd-Frank.[100] That Act includes a subsection, titled "Authority to Establish a Fiduciary Duty for Brokers and Dealers," which authorizes the SEC to create a standard of conduct that requires brokers, dealers and investment advisers:

> [W]hen providing personalized investment advice about securities to a retail customer . . . to act in the best interest of the customer without regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice. In accordance with such rules, any material conflicts of interest shall be disclosed and may be consented to by the customer. Such rules shall provide that such standard of conduct shall be no less stringent than the standard applicable to investment advisers under section 206(1) and (2) of this Act when providing personalized investment advice about securities . . . . The receipt of compensation based on commission or fees shall not, in and of itself, be considered a violation of such standard applied to a broker, dealer, or investment adviser.[101]

The SEC staff completed a study of broker, dealer and investment adviser duties in January 2011.[102] The study recommends a "uniform fiduciary standard" for broker-dealers and investment advisors who provide investment advice to retail customers.[103] The staff recommends the adoption of rules providing that:

> [T]he standard of conduct for all brokers, dealers, and investment advisers, when providing personalized investment advice about securities to retail customers (and such other customers as the Commission may by rule provide), shall be to act in the best interest of the customer without

[99] *Jones*, 527 F.3d at 633-34.

[100] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (to be codified in scattered sections of U.S.C.).

[101] *Id.* § 913(g).

[102] *See* SEC, STUDY ON INVESTMENT ADVISERS AND BROKER-DEALERS AS REQUIRED BY SECTION 913 OF THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT 1 (2011), *available at* http://www.sec.gov/news/studies/2011/913studyfinal.pdf.

[103] *Id.* at 109-10.

regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice.[104]

Contrary to the title of the Dodd-Frank section and the SEC staff's description of its standard, neither the Act nor the staff study provides for a fiduciary duty under my analysis. The provision refers to the "best interest" standard under section 206 of the Investment Advisers Act of 1940,[105] and its main function appears to be to align the duties of brokers-dealers with those of investment advisers. Although the section 206 duty has been held to be a fiduciary duty,[106] this characterization is questionable. It traces back to *SEC v. Capital Gains Research Bureau, Inc.*,[107] which held that an adviser's "scalping," or purchasing shares before recommending them and then selling on the rise in market price, "operates as a fraud or deceit upon any client."[108] While the Court referred to investment advisers as fiduciaries, its holding was based on an interpretation of the common law of fraud, and amounts only to a duty to disclose the material fact of an adviser's self-interest rather than a fiduciary duty of unselfishness.[109] This is consistent with this paper's analysis of the non-fiduciary nature of the duty of professionals and advisers.[110]

Fiduciary duties are even less appropriate for brokers and dealers than they are for professionals and advisers. Customers generally do not delegate fiduciary-type open-ended power that would justify fiduciary-type selflessness consistent with this article's analysis. Brokers, dealers, and advisers usually lack authority to commit the customer's property without further instructions. Nor should customers expect unselfish conduct from people who are selling securities for a commission or profit. Thus, application of fiduciary duties to brokers, dealers, and advisers would not be consistent with customers' expectations and would create a potential for confusion similar to that in the mutual fund situation discussed above.[111] As Arthur Laby has recognized: "When acting as a dealer, the firm seeks to buy low and sell high – precisely what the customer seeks. It is hard to see how any dealer can act in the '"best interest' of his customer when trading with her."[112]

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[104] *Id.* at 109.

[105] *See* Investment Advisers Act of 1940 § 206, 15 U.S.C. § 80b-6 (2006).

[106] *See, e.g.*, SEC v. Tambone, 550 F.3d 106, 146 (1st Cir. 2008) ("Section 206 imposes a fiduciary duty on investment advisers to act at all times in the best interest of the fund and its investors . . . ."), *reh'g granted and opinion withdrawn*, 573 F.3d 54 (1st Cir. 2009).

[107] 375 U.S. 180 (1963).

[108] *Id.* at 181.

[109] *See* Arthur B. Laby, SEC v. Capital Gains Research Bureau *and the Investment Advisers Act of 1940*, 91 B.U. L. REV. 1051, 1072 (2011).

[110] *See supra* Part II.C.2.

[111] *See supra* Part III.A.

[112] Arthur B. Laby, *Reforming the Regulation of Broker-Dealers and Investment Advisers*, 65 BUS. LAW. 395, 425 (2010).

Consider, for example, the SEC's recent lawsuit against Goldman, Sachs & Co. alleging that Goldman, which "structured and marketed" a security to the IKB bank, failed to disclose a famous market speculator's (John Paulson) role in selecting the derivative security's reference portfolio.[113] Although a proposal in Congress at the time of the suit would impose fiduciary duties on parties in Goldman's position,[114] such a duty would be inconsistent with Goldman's position as a seller. The only possible fiduciary in this transaction would have been the collateral manager which had responsibility for designing the security, but was not involved in the suit.[115] Goldman should be liable at most for conventional securities fraud if Paulson's involvement is deemed to be a material fact that Goldman had to disclose under existing disclosure rules.[116]

The legislative history of the Securities Exchange Act of 1934 indicates that existing law does not impose a fiduciary duty on brokers and dealers.[117] Laby shows that a proposal to prohibit a broker from acting as a dealer or underwriter ultimately was squelched in favor of recognizing the "shingle theory," which imposes a duty to buy and sell at reasonable prices.[118] Laby observes that:

> The SEC's compromise . . . is a non-fiduciary compromise. The gap between prohibiting an unreasonable price and helping the customer obtain the best price is vast, and it represents the difference between the duty of fair dealing and the fiduciary obligation.[119]

These observations are consistent with this Article's analysis.

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[113] Complaint at 1-2, SEC v. Goldman Sachs & Co. (S.D.N.Y. Apr. 16, 2010) (No. 10 Civ. 3229), *available at* http://www.sec.gov/litigation/complaints/2010/comp21489.pdf.

[114] *See* 156 CONG. REC. S3109 (daily ed. May 4, 2010) (documenting Amendment No. 3806 to Dodd-Frank offered by Senators Kaufman and Specter).

[115] *See Wall Street and Fiduciary Duties: Can Jail Time Serve as an Adequate Deterrent for Willful Violations?: Hearing Before the Subcomm. on Crime and Drugs of the S. Comm. on the Judiciary*, 111th Cong. 7 (2010) (statement of Larry E. Ribstein) (arguing that "to the extent there was any fiduciary-type delegation of discretion, it was to the collateral manager").

[116] One paper suggests a fiduciary duty might be appropriate in a transaction like the one involved in the Goldman case if there are well-established standards enabling an arbiter to judge whether there has been a breach, a party lacks the sophistication or resources necessary to identify violations of these norms, and one party lacks the necessary market voice or credibility to impose reputational sanctions on the other. *See* Steven M. Davidoff, Alan D. Morrison & William J. Wilhelm, Computerization and the ABACUS: Reputation, Trust, and Fiduciary Duties in Investment Banking 17-20 (Jan. 24, 2011) (unpublished manuscript), *available at* http://ssrn.com/abstract=1747647. Under my analysis, because Goldman would remain a seller, a fiduciary duty would be inappropriate even if these factors were present.

[117] *See* Laby, *supra* note 112, at 403.

[118] *See id.* at 427.

[119] *Id*. (footnote omitted).

A broker-dealer fiduciary duty also would be inconsistent with Dodd-Frank's legislative history. Treasury initially recommended a broker-dealer and investment adviser duty to "act solely in the interest of the customer or client without regard to the financial or other interest of the broker, dealer or investment adviser providing the advice."[120] This is clearly a fiduciary standard of unselfishness, consistent with this Article's characterization.[121] The change from the initial proposal to the final version represents a clear rejection of the fiduciary approach.

The SEC should go no further than spelling out the disclosure duties that are appropriate to advisers, dealers, and brokers. It should not confuse the duties of securities professionals by applying the fiduciary label to non-fiduciary relationships. This would help investors buy only the level of service and commitment to their interest that is appropriate to the relationship they are contracting for. Investors would not have to pay a higher price for securities professionals' unselfishness when they are also planning to exercise their own judgment and control. They would still get enough disclosure to prudently use the services they are buying, while having the flexibility to contract for a higher level of protection when they want it.

CONCLUSION

The fiduciary duty is a useful tool for controlling agency costs. It makes sense to utilize it in the context of a particular type of agency relationship involving broad delegation of power to manage another's property. In this situation, a default duty of unselfish conduct is appropriate because lesser constraints on the agent often are ineffective.

The usefulness of the fiduciary duty depends on its being kept in a corral rather than set loose to roam broadly among commercial relationships where it does not belong. The fiduciary duty of unselfishness should be distinguished from duties that can exist outside the fiduciary setting, including the duties of care, good faith and fair dealing, and to refrain from misappropriation.

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[120] U.S. DEP'T OF THE TREASURY, TITLE IX – ADDITIONAL IMPROVEMENTS TO FINANCIAL MARKETS REGULATION § 913(a) (2009), *available at* http://www.treasury.gov/press-center/press-releases/Documents/tg205071009.pdf (recommending SEC rules "to provide, in substance, that the standards of conduct for all brokers, dealers, and investment advisers, in providing investment advice about securities to retail customers or clients (and such other customers or clients as the Commission may by rule provide), shall be to act solely in the interest of the customer or client without regard to the financial or other interest of the broker, dealer or investment adviser providing the advice").

[121] *See* Laby, *supra* note 112, at 426. The confusion between the sole and best interest tests might be explained by the fact that courts often apply the best interest test to fiduciaries where the sole interest test has been qualified by contract or other circumstances. *See generally,* John H. Langbein, *Questioning the Trust Law Duty of Loyalty: Sole Interest or Best Interest?* 114 YALE L. J. 929 (2005). This characterization of fiduciary duties as default rules subject to contrary agreement is consistent with my analysis. *See supra* text accompanying notes 35-39.

Applying a fiduciary duty of unselfishness to relationships that do not involve broad delegation of discretion could unnecessarily constrain parties to conventional contracts, impose excessive litigation costs, provide an unsuitable basis for contracting, and interfere with the establishment of fiduciary norms of behavior. Fiduciaries should be distinguished from those who exercise lesser power over the property of others, including co-investors, advisers and professionals, and those in confidential relationships.

This analysis of fiduciary duties helps address current problems regarding the duties of brokers, dealers, and investment and mutual fund advisers. Fencing fiduciaries clarifies the lesser duties of these actors and enables investors to contract for the precise level of protection that is appropriate to the services they are purchasing.