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By electronic mail to rule-comments@sec.gov

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Consolidated Comments in Response to SEC Proposed Rulemakings: Regulation Best Interest (File No. S7-07-18), Form CRS Relationship Summary, Amendments to Form ADV, Required Disclosures, and Restrictions on the Use of Certain Names or Titles (File No. S7-08-18), and Standards of Conduct for Investment Advisers (File No. S7-09-18)

Dear Mr. Fields:

On behalf of the North American Securities Administrators Association, Inc. ("NASAA"),[1] I am submitting the following consolidated comments and recommendations in response to the proposed rulemakings of the U.S. Securities and Exchange Commission ("SEC" or the "Commission") announced on April 18, 2018: Regulation Best Interest,[2] Form CRS Relationship Summary, Amendments to Form ADV, Required Disclosures, and Restrictions on the Use of Certain Names or Titles,[3] and Standards of Conduct for Investment Advisers[4] (collectively, the "Proposals").

In sum, we believe the Proposals represent a good initial step but that significant improvements are needed in order to promulgate final rules that will serve the best interest of

[1] NASAA is the association of the 67 state, provincial, and territorial securities regulatory agencies of the United States, Canada, and Mexico. NASAA serves as a forum for these regulators to work with each other to protect investors at the grassroots level and promote fair and open capital markets.

[2] Regulation Best Interest, SEC Release No. 34-83062, File No. S7-07-18 (Apr. 18, 2018), *available at* https://www.sec.gov/rules/proposed/2018/34-83062.pdf.

[3] Form CRS Relationship Summary, Amendments to Form ADV, Required Disclosures in Retail Communications and Restrictions on the Use of Certain Names or Titles, SEC Release No. 34-83063, File No. S7-08-18 (Apr. 18, 2018), *available at* https://www.sec.gov/rules/proposed/2018/34-83063.pdf.

[4] Proposed Commission Interpretation of Conduct for Investment Advisers, SEC Release No. IA-4889, File No. S7-09-18 (Apr. 18, 2018), *available at* https://www.sec.gov/rules/proposed/2018/ia-4889.pdf.

investors as the Commission intends. NASAA encourages the Commission to make modifications to the text of the proposed rules and to substantially reform its guidance on the Proposals prior to their adoption. NASAA agrees that the Commission should act to address investor confusion regarding the different roles of investment advisers and broker-dealers and that the Commission should raise the current standard of care applicable to broker-dealer recommendations from suitability to a standard akin to the fiduciary duties owed by investment advisers. We believe the Commission's approach of raising the standard for broker-dealers, while not weakening the current standard applicable to investment advisers, is the correct one. NASAA supports the Proposals' effort to address conflicts of interest, improve fee transparency, restrict the use of potentially misleading professional titles, and clarify investment adviser conflict of interest obligations.

NASAA especially appreciates Chairman Clayton's leadership in advancing this important regulatory priority. We look forward to further engagement with Chairman Clayton, the Commissioners, and the SEC staff as the Commission develops the Proposals into final rulemakings. Given our members' shared responsibility with the SEC for oversight of the firms and individuals that will be impacted by the Proposals, NASAA is anxious to work closely with the Commission on further refinements to the Proposals and we hope our constructive comments are well received and considered fully.

I) Executive Summary

As set out more fully below in the body of this letter, we encourage the Commission to revise the Proposals so they will be more consistent with a standard designed to align broker-dealer conduct with the best interests of investors and investors' reasonable expectations. Our comments below are aimed at clarifying and expanding the scope of the new conduct standard for broker-dealers, specifying the types of practices that would be prohibited under the new broker-dealer standard, establishing clearer lines of demarcation between investment advisory and broker-dealer activities, preserving investor rights and remedies, improving the effectiveness of proposed Form CRS, and expanding how the Commission proposes to move forward on the use of certain professional titles.

Generally, our recommendations on proposed Regulation Best Interest include the following:

- Label the new regulation and its new eponymous duty obligation to act in customer's best interest the "Broker-Dealer Standard of Conduct" rather than "Regulation Best Interest" to avoid conflations of broker-dealer's best interest duties and investment adviser's fiduciary duties.
- Define the new broker-dealer standard of conduct as Commissioner Stein has proposed and expand the scope of this duty to encompass all investors and all securities products.

- Clarify the requirements necessary to satisfy the new broker-dealer standard of conduct by adding specific factors that must be met and by broadening broker-dealer conflict of interest mitigation and disclosure obligations.
- Prohibit certain practices by broker-dealers and their associated persons (particularly those involving financial incentives) as *per se* incompatible with the new broker-dealer standard of conduct.
- Establish through rulemaking guidance more definite borderlines between investment advisory and broker-dealer activities so as to effectuate longstanding congressional intent underlying the broker-dealer incidental practice exclusion from the Investment Advisers Act.
- Require broker-dealers and their associated persons to consider securities products beyond just those offered by the firm itself when making recommendations under the new broker-dealer standard of conduct.
- Clarify through rulemaking guidance the rights and remedies the Commission anticipates investors will have in pursuing violations of the new broker-dealer standard of conduct and expressly declare that the new standard is not intended to preempt any state laws or regulations.
- Limit the scope of impermissible broker-dealer titles beyond just "adviser" or "advisor" to address how associated persons of broker-dealers hold themselves out to the public.
- Conduct comprehensive testing of proposed Form CRS to evaluate its usefulness to investors and, at such time as the form is adopted, allow firms some flexibility in implementing the disclosures so as to tailor the content for their customers' needs.
- Defer to state securities regulators regarding registration of investment adviser representatives and any potential continuing education requirement for these persons.

We look forward to further engagement with the SEC on our comments as the Commission moves forward with these important rulemakings.

II) Regulation Best Interest

NASAA supports raising the broker-dealer standard of care for recommendations to customers about securities or investment strategies provided the end result is enhanced protection and recourse for investors subject to abusive advice and sales practices. Moving from the current investor protection floor of FINRA's suitability standards to a true heightened standard akin to an investment adviser's fiduciary duty should necessarily change the status quo by curbing abusive sales and advisory practices. Unfortunately, much of the Commission's guidance surrounding the new broker-dealer standard of care indicates it will be interpreted (at least by the SEC) to preserve

the status quo so that all existing business models, products, and practices can persist notwithstanding their known potential for investor harm.

The guidance in the Proposals, and in particular the guidance on proposed Regulation Best Interest, appears to give broker-dealers free rein to offer advisory services beyond what the broker-dealer incidental practice exclusion from the Investment Advisers Act reasonably should be interpreted to permit.[5] The Commission characterizes the type and frequency of advice provided by broker-dealers as a regular function of the relationship between broker-dealers and their customers.[6] While we agree that access to a variety of products and services is important for investors and that broker-dealers should be able to provide very limited advice, the questionable goal of preserving an antiquated broker-dealer business model should not undermine investor protection necessities nor undercut existing registration requirements. We believe this foundational defect in proposed Regulation Best Interest can be remedied by revising proposed Rule 15*l*-1 and the Commission's guidance thereto. Separately, the Commission should also spell out the rights and remedies available to investors harmed by a broker-dealer's failure to act consistent with their obligations under the new conduct standard as any effort to elevate the broker-dealer standard of care will be in vain without clear remedies for breach of the standard.

For the most part, NASAA supports proposed Rule 15*l*-1 as well as the structure and language utilized in Regulation Best Interest. We believe the proposal should be revised in five general areas, though:

1. changing the title of the regulation and the labeling of the duty throughout from "Regulation Best Interest" to "Broker-Dealer Standard of Conduct" (to avoid conflating broker-dealer and investment adviser duties and lessen investor confusion on this issue);
2. broadening the scope of the new duty to apply to recommendations made to any broker-dealer customer, striking the "retail" qualifier throughout the text of proposed Rule 15*l*-1;[7]
3. clarifying the requirements necessary to meet the broker-dealer standard of conduct by emphasizing specific metrics that must be reviewed in assessing whether a recommendation is in the best interest of a particular customer (by adding "risks" and "costs," where currently omitted, to the factors enumerated in subparagraph (a)(2)(i));

[5] *See* 15 U.S.C. § 80b-2(a)11(C).

[6] *See* Regulation Best Interest, *supra* note 2, at 21 ("There is broad acknowledgement of the benefits of, and support for, the continuing existence of the broker-dealer model as an option for retail customers seeking investment advice . . . .") and 39 ("We also share concerns raised by commenters about retail customers losing access to advice they receive through recommendations from broker-dealers . . . ."

[7] *See id.* at 91 ("Should the Commission broaden or limit the scope of individuals to whom Regulation Best Interest applies? For example, should it apply to small business entities such as a sole proprietorship? Why or why not?").

4. broadening broker-dealers' conflict of interest obligations under subparagraph (a)(2)(iii) of the proposed rule to include policy, procedure *and practice* obligations applicable to both firms and their associated persons on a transaction-by-transaction basis; and

5. inserting a new subsection defining the standard of conduct for broker-dealers.

These revisions to Rule 15*l*-1 as proposed are reflected in the Attachment to this letter.

NASAA also has significant concerns with the guidance developed by the Commission as part of proposed Regulation Best Interest. At its core, a rule purporting to require firms and investment professionals act in the "best interest" of their clients must have a merit component that would presumptively require those professionals to recommend products and strategies that are, in the professional's informed and expert judgment, the best or most prudent fit for their clients. Where there is a plethora of suitable alternatives (as is often the case), the expectation should be that the professional will recommend the product or strategy that is best suited to achieving the client's financial goals. As the proposing release makes clear, the Commission does not interpret the phrase "best interest" along those lines. Rather, the Commission interprets "best interest" in such a manner that, with disclosure, brokers can continue recommending investments and strategies that are high cost, complex, illiquid and risky as nonetheless in a customer's "best interest" even where there are cheaper, simpler, more liquid and safer alternatives. It is difficult to square this outcome with a regulation intended to put investors' interests first.

In NASAA's view, such conduct would not satisfy the fiduciary duties of care and loyalty that investment advisers have to act in their clients' best interests. To be sure, the Commission's proposing rule release cites no controlling case law or supporting interpretive guidance that has ever found such conduct by an investment adviser to be consistent with (much less satisfy) the principles underlying a fiduciary standard of care. (And, to the extent the Commission is aware of investment advisers routinely engaging in such conduct without consequence, it should utilize its examination and enforcement authority to redirect and, if necessary, remove such actors.) In light of the foregoing, NASAA understands and shares Commissioner Stein's concern that the Commission's proposed guidance on Regulation Best Interest would result in a "best interest" standard for broker-dealers that is not meaningfully better than existing suitability standards. To guard against that, NASAA supports Commissioner Stein's recommendation that the new standard be specifically defined so that calls are made in favor of investors and, as suggested above, that the care and conflict of interest obligations be clarified to ensure that key factors are weighed in the investor's favor.

The following are specific areas responsive to the Commission's proposed rulemaking and guidance related to the overarching "best interest" obligation that NASAA believes should be reformed to effectively elevate the broker-dealer standard of care and ameliorate investor confusion regarding the comparative roles and duties owed by broker-dealers and investment

advisers. Americans increasingly rely on their own savings to secure their retirement and to fund significant expenditures such as a child's education. Research shows investors mistakenly believe they are paying broker-dealers and their agents to provide advice in their best interests and that investment professionals are obligated by law to do so.[8] Securities regulations should catch up with these reasonable expectations.

1. Scope of the new Broker-Dealer Standard of Conduct

Under the proposed broker-dealer standard of conduct outlined in Regulation Best Interest, broker-dealers and their agents would be obligated to ensure any recommendations they make to retail customers regarding securities or investment strategies are in the customers' "best interests." This duty is described as "act[ing] in the best interest of the retail customer at the time the recommendation is made without placing the financial or other interest of the broker, dealer, or a natural person who is an associated person of a broker or dealer making the recommendation ahead of the interest of the retail customer."[9] The duty would contain subsidiary disclosure, care and conflict of interest obligations.[10]

With respect to what it means for a broker-dealer to act in a customer's "best interest," we support – and encourage the Commission to adopt – the functional definition of the term offered by Commissioner Stein in her April 18, 2018, Public Statement on the Proposals, with two minor revisions.[11] We believe the term "best interest," if it is retained by the Commission to brand this rulemaking, should be described as follows:

> "To act in the best interest" means when a broker, dealer, or natural person who is an associated person of a broker or dealer, makes a recommendation, the recommendation reflects the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use taking into consideration all of the facts and circumstances, including the costs and risks of the recommendation, in light of the investment profile of the Customer to whom the recommendation is made.[12]

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[8] *E.g.*, Regulation Best Interest, *supra* note 2, at 20 n.28 (discussing research into investor expectations by the RAND Corporation and by the Consumer Federation of America and other organizations).

[9] Regulation Best Interest, *supra* note 2, at 44.

[10] *See id.* at 44-45.

[11] *See* Commissioner Kara Stein, Statement on Proposals Relating to Regulation Best Interest, Form CRS, Restrictions on the Use of Names or Titles, and Commission Interpretation Regarding the Standards of Conduct for Investment Advisers (Apr. 18, 2018), https://www.sec.gov/news/public-statement/stein-statement-open-meeting-041818.

[12] This definition modifies Commissioner Stein's proposal by making clear the "best interest" standard applies to all customers, not just retail customers, and that the factors to consider in evaluating compliance with the duty include costs and risks in light of the customer's investment profile.

Adopting this functional definition would accomplish several things.

First, our proposed definition would expand the scope of Regulation Best Interest, making it universally applicable for all investors. Second, our proposed definition would make clear that the best interest duty is objective, not subjective to the broker-dealer or agent, and that it must be exercised reasonably. Third, this functional definition expressly invokes the principles of care, skill, prudence, and diligence that a broker-dealer or agent's conduct will be evaluated against. Fourth, it includes a temporal component, expressly requiring that the conduct be evaluated as of the time the recommendation is made and in light of all relevant facts and circumstances including the customer's investment profile. These changes would help "level the playing field" between sophisticated and retail investors and would do so in ways that would be easy for retail investors to understand.[13]

Regulation Best Interest as proposed is principles-based; the Commission has not elected to proscribe certain specific types of activities. If the Commission maintains this principles-based approach, it should provide clearer guidance on the types of conduct that would be permissible or impermissible under the new standard. Such guidance would be necessary for firms to understand their compliance obligations and for investors to better understand the contours of the duty owed to them. As discussed below, we believe the Commission should declare certain conflicts of interest tied to compensation and practices that incentivize broker-dealers and their associated persons to put their interests ahead of their customers' as *per se* impermissible under Regulation Best Interest as proposed.

The proposal would require broker-dealers to use "reasonable diligence" in fulfilling their duty of care. The proposal describes this as "similar to the standard of conduct that has been imposed on broker-dealers found to be acting in a fiduciary capacity"[14] and states the required amount of diligence "will vary depending on, among other things, the complexity of and risks associated with the recommended security or investment strategy and the broker-dealer's familiarity with the recommended security or investment strategy."[15] Commission guidance should clarify these points further, though. We encourage the Commission to diagram in detail several hypothetical examples of sufficient or insufficient diligence in the context of fulfilling the best interest obligation.

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[13] *See* Commissioner Robert Jackson, Statement on Proposed Rulemakings Relating to Investment Adviser / Broker-Dealer (IABD) Standards of Conduct (Apr. 18, 2018), https://www.sec.gov/news/public-statement/proposed-rulemaking-retail-investor-relationships-investment-professionals.

[14] Regulation Best Interest, *supra* note 2, at 134 n.222.

[15] *Id.* at 139.

The proposal requests feedback on the scope of the "retail customer" definition.[16] A retail customer is defined as any "person, or the legal representative of such person," who receives "a recommendation of any securities transaction or investment strategy involving securities" from a broker, dealer or associated person thereof and who "uses the recommendation primarily for personal, family, or household purposes."[17] A "person" can include a natural person as well as a non-natural persons (such as a trust) that exists for the benefit of a natural person.[18] We believe Regulation Best Interest should be extended to include *all* customers, not just "retail customers," as we can think of no reason why all investors should not receive the benefit of this new standard regardless of their wealth, sophistication, or legal personhood.

Among the many questions posed in the proposal is whether a broker-dealer's "best interest" duty should apply to recommendations as to the type of account the customer opens or maintains with the firm.[19] We believe that, notwithstanding the premise underlying this request for comment, proposed Regulation Best Interest would indeed apply to such recommendations because they bear directly on the investment strategy being used for the customer. We believe that *any* recommendation from a broker-dealer or agent related to a securities transaction or investment strategy involving securities will fall under Regulation Best Interest unless it is expressly exempted from such treatment by the SEC.[20] There need only be a minimal nexus to a security or investment strategy for the "best interest" duty to attach.[21] Regulation Best Interest therefore will apply, for example, to sales of variable annuities and other nontraditional securities consistent with existing Commission guidance. It will also apply to recommendations to hold or to not engage in a particular securities transaction or strategy. In sum, we encourage the Commission to acknowledge in any final rulemaking what we believe existing law already implies, namely that Regulation Best Interest will apply to all recommendations regarding securities or investment strategies, including recommendations regarding account types and variable annuity sales.

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[16] *Id.* at 83-91.

[17] *See* Proposed Rule 15(l)-1(b)(1).

[18] Regulation Best Interest, *supra* note 2, at 85.

[19] *Id.* at 93-94 ("Should the Commission extend Regulation Best Interest to recommendations of account types even if the recommendation is not tied to a securities transaction? If so, what factors should a broker-dealer consider in making a recommendation of an account type? Should the factors differ if the account type recommended is discretionary versus nondiscretionary? Should they differ for dual-registrants versus standalone broker-dealers?").

[20] For example, FINRA Rule 2111.03 expressly exempts certain communications from treatment as recommendations as a matter of policy in order that these activities not be included within the scope of Rule 2111.

[21] Regulation Best Interest as proposed would apply well tread standards of what constitutes a "recommendation" under FINRA rules. *See* Regulation Best Interest, *supra* note 2, at 73 – 83. FINRA rules interpret this term broadly and apply it to all manner of securities contexts. *See, e.g.*, FINRA Regulatory Notice 12-25, *Suitability*, at 4 – 5 (May 2012); FINRA Rule 2111 (Suitability) FAQs, http://www.finra.org/industry/faq-finra-rule-2111-suitability-faq.

2. Scope of Products Offered By a Broker-Dealer and Comparison with Alternatives

NASAA strongly disagrees with the Commission's apparent position that a broker-dealer could satisfy its "best interest" duties by recommending securities from a very limited menu of products without any comparison whatsoever to alternatives beyond this limited menu.[22] How could a broker-dealer or an associated person of the broker-dealer ever make a good faith statement that a recommendation is in a customer's best interest without first exploring whether there are cheaper, simpler, more liquid, and less risky alternatives available to achieve the customer's investment objectives? Such an interpretation of a "best interest" conduct standard is contrary to the care obligation articulated in the text of the proposed rule, which requires broker-dealers and associated persons to "exercise reasonable diligence" and "prudence" in recommending products. There is nothing reasonable or prudent about a firm or its associated persons recommending only the product offerings at his or her firm while ignoring alternative investment opportunities and products elsewhere that may better serve the customer's overall investment needs. The Commission should revise the language in the proposing release to make clear that broker-dealers and associated persons do in fact need to look outside the firm in considering factors such as cost, complexity, liquidity, and risk of readily available products and investment strategies that meet the customer's investment profile for purposes of making a best interest recommendation. This change would not require that broker-dealers and their associated persons become knowledgeable about every investment that is offered or sold; we are not suggesting such a maximalist application of the basic principle underlying a best interest duty. Rather, broker-dealers and their associated persons should be held accountable for knowing broadly about competing asset classes and investment strategies to ensure that the products offered at the firm, whether limited or expansive in scope, are not merely suitable but are truly in their customers' best interests.

3. Mitigation and *Per Se* Violations of the Best Interest Duty

The proposal identifies several broker-dealer practices whose validity would be questionable under Regulation Best Interest (including sales contests and preferential treatment in the allocation of investment opportunities), noting that these practices would be neither *per se* prohibited nor *per se* acceptable.[23] Rather, the Commission will evaluate such practices on a case-by-case basis to determine whether a broker-dealer's disclosures and efforts to mitigate or eliminate conflicts of interest are sufficient. The proposal concedes, though, that retail customer confusion about the obligations of broker-dealers can "exacerbate the potential for investor harm (such as through a misalignment of investor expectations regarding the level of protection received and the level of protection actually provided)."[24]

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[22] *See* Regulation Best Interest, *supra* note 2, at 69 ("Are any changes in Regulation Best Interest necessary to make it clear that broker-dealers who offered a limited scope of products nevertheless can satisfy the standard?").

[23] Regulation Best Interest, *supra* note 2, at 53-54.

[24] *Id.* at 37.

Having opened this door, we encourage the Commission to proceed further by declaring these two practices – sales contests and preferential treatment of allocations – *per se* impermissible under Regulation Best Interest. Sales contests are a pernicious feature of brokerage sales activities and necessarily require agents, consciously or not, to put their own interests ahead of customers. We can envision no circumstances under which any sales contest would ever be consistent with a broker-dealer's duties under Regulation Best Interest as proposed, even if the broker-dealer tried to mitigate and fully disclose the conflict.[25] What is more, the continued existence of sales contests and other abusive practices will undermine investors' faith in the basic principles underlying Regulation Best Interest. Sales contests therefore should be banned outright. In addition, there should be no room under Regulation Best Interest for preferential treatment of customers in the allocation of investment opportunities such as initial public offerings. It should be clear that broker-dealers have no freedom to favor their richest or best-connected customers when allocating investment opportunities. Investment allocations should instead be made based upon objective, fair criteria, immune from a broker-dealer's own business self-interest. We also encourage the Commission to provide additional guidance on when other potentially abusive sales practices would fail a best interest analysis.

The Commission requested comment on whether neutral compensation across products could constitute appropriate mitigation.[26] We believe it could. Neutral compensation coupled with full and fair disclosure of material conflicts of interest and fees would be an appropriate way for broker-dealers to satisfy their best interest obligations. This would eliminate the potential for a broker-dealer to favor one product over another based on the broker's own self-interest and, coupled with the duty recommended above to ensure recommendations cover the waterfront with respect to the type of securities in which investors could invest, the Commission would truly place customers on the pedestal to which they should be held by their brokers.

If the Commission is unwilling to take this step and retains the current approach permitting such activities, the Commission should at a minimum provide additional guidance on what types of conflict mitigation measures must be included in a firm's policies and procedures to combat harms associated with these practices. Specifically, a firm's policies and procedures must, at a minimum, require an analysis of the costs and risks of the product as well as the client's financial goals in order to satisfy the "best interest" standard. These factors are especially important given that the proposal would not prohibit selling from a limited menu of products or require an associated person to recommend a product beyond those available on her firm's platform.

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[25] These practices would also perforce violate an investment advisers' fiduciary duties. The Commission thus could extend the *per se* scope of broker-dealer prohibited practices under Regulation Best Interest to apply to investment advisers as well.

[26] Regulation Best Interest, *supra* note 2, at 196.

4. Complying with the Best Interest Duty – Account Monitoring

The Regulation Best Interest proposal states that while broker-dealers do not have an ongoing duty to monitor investments or investment recommendations, broker-dealers and their customers may contractually agree for the broker-dealer to do so. The Commission requested comment on whether such ongoing monitoring duties should be subject to a "best interest" duty or deemed to be investment advisory in nature and therefore subject to fiduciary duty standards under the Investment Advisers Act.[27]

Ongoing account monitoring is a *sine qua non* of an investment adviser's fiduciary duty to clients. Broker-dealer duties by comparison are transactional and episodic, as made clear by the Commission's characterization of the relationship and limited duties prescribed as a result.[28] The provision of ongoing monitoring services therefore should be a triggering event for the commencement of an investment advisory relationship to which the Investment Advisers Act should apply.

5. Complying with the Best Interest Duty – Compliance and Supervisory Systems

The proposal states that it would be reasonable for a broker-dealer to use a risk-based compliance system to comply with its "best interest" duties rather than conducting transaction-by-transaction assessments of every recommendation.[29] We urge the Commission to reconsider this approach. No compliance system should ever be treated as satisfying Regulation Best Interest on its own. Rather, implementation of an appropriate compliance system should be treated as a necessary, but not necessarily sufficient, step to comply with the regulation. Broker-dealers must be held to a high standard when executing their "best interest" obligations.

6. Broker-Dealer Exclusion and Discretionary Authority

Section II.F of proposed Regulation Best Interest requests comment on the broker-dealer exclusion and the extent to which broker-dealers should be exempt from the Investment Advisers Act in their exercise of discretionary authority over customer accounts. The current proposal is an excellent opportunity for the Commission finally to commit itself to treating broker-dealers that exercise discretionary trading authority as investment advisers. The Commission thus should undertake to implement its 2007 rule proposal in this regard and ensure "any account over which a broker-dealer exercises investment discretion is subject to the Advisers Act."[30] The broker-dealer

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[27] Regulation Best Interest, *supra* note 2, at 70.

[28] *Id.* at 329.

[29] *Id.* at 171.

[30] Interpretive Rule Under the Advisers Act Affecting Broker-Dealers, SEC Release No. IA-2652 at 8 (Sept. 24, 2007), *available at* https://www.sec.gov/rules/proposed/2007/ia-2652.pdf.

exclusion from the Advisers Act should apply only to non-discretionary brokerage accounts in which the only forms of discretion exercised by a broker-dealer is as to: (i) the time and price of execution, (ii) the management of cash, (iii) transactions to satisfy customer margin obligations, and (iv) the selection of securities (such as bonds) according to specific, narrowly defined criteria established by a customer.

7. Dual Registrants

Dually-registered broker-dealers and investment advisers present unique challenges to effective investor protection in a Regulation Best Interest paradigm. The proposal's guidance to dual registrants is that they must comply with the proposed regulation when they act as a broker-dealer but must comply with the Investment Advisers Act when they act as an investment adviser.[31] The proposal does not provide specific instructions for firms walking this tightrope, though, and consequently dually-registered firms will inevitably falter and fail to satisfy their legal duties. Managing such 'hat switching' and remaining compliant with applicable securities laws and regulations is concededly difficult, but financial services firms that voluntarily choose to undertake such business opportunities must abide by the concomitant regulatory obligations this entails.

The Commission should provide guidance in Regulation Best Interest to explain how associated persons should disclose the capacity in which they are acting and whether the information they are providing is a recommendation (subject to "best interest" duties) or advice (subject to a fiduciary duty). Alternatively, the Commission could go a long way toward resolving the problems associated with dual registration by simply stating through guidance that firms with clients that maintain both advisory accounts and brokerage accounts must be treated as advisory clients *in toto*. (This alternative is, in NASAA's view, the substantially preferable approach.)

8. Investor Rights and Remedies

As noted above, the Commission should expressly elaborate on the remedies available to investors when broker-dealers violate their conduct standard. The Commission states in the proposal, "we do not believe proposed Regulation Best Interest would create any new private right of action or right of rescission, nor do we intend such a result."[32] Private claims by investors against their brokers generally proceed through arbitration under rules established by the Financial Industry Regulatory Authority ("FINRA") (though they may in limited instances proceed in federal or state courts as well). We believe the obligations imposed on broker-dealers under the proposal will be enforceable in such arbitrations or litigation under well-established legal theories that exist today. We ask the Commission to expressly affirm its support for this basic principle through its guidance.

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[31] *See* Regulation Best Interest, *supra* note 2, at 199-205.

[32] *Id.* at 42.

In any final rulemaking, the Commission should state in guidance that the duties and obligations it is creating under the new conduct standard will be enforceable by customers through existing legal theories and venues open to them. Moreover, the Commission should emphasize the point made in the proposing release that "[s]cienter would not be required to establish a violation of Regulation Best Interest."[33] Regulation Best Interest is being proposed pursuant to the Commission's authority under Section 10 of Securities Exchange Act of 1934 (among others),[34] but it would be extremely unfortunate if a judge or arbitrator interpreted Regulation Best Interest as including a scienter component merely because the SEC included Section 10 as one of its legal authorities for issuing the regulation.

9. Disclosure Obligations

Regulation Best Interest would include an express obligation for broker-dealers to disclose the scope of the proposed customer relationship and material conflicts of interest related thereto.[35] This obligation could be complied with through a relationship summary (*i.e.*, Form CRS) and other standardized disclosures.[36]

We believe this proposed disclosure regime is insufficient. Separate and apart from a broker-dealer's standardized disclosure obligations under the separate Form CRS rulemaking, the Commission should require that broker-dealers disclose under Regulation Best Interest all material facts and conflicts associated with the specific transaction being recommended. Only a transaction-by-transaction disclosure obligation will ensure that broker-dealers are meeting their "best interest" duties and provide investors the level of protection they deserve. Any contrary standard would conflict with the underlying purpose of the proposal of leveling the playing field between investment advisers and broker-dealers, thereby holding broker-dealers to functionally inequivalent legal duties.

With respect to the types of fees that must be disclosed and the standardization of such disclosures, the SEC should consider mandating the use of a version of the Schedule of Miscellaneous Account and Service Fees (the "Model Fee Table") established by a working group

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[33] *Id.*

[34] The Commission proposes to issue Regulation Best Interest pursuant to its authority under Section 913(f) of the Dodd-Frank Act and Exchange Act sections 3, 10, 15, 17, 23 and 36. We believe the inclusion of Section 10 is unnecessary; the Commission has more than adequate authority under these other sections. The Commission should ensure that by naming Section 10 as among the proposal's stated bases of authority it is not opening the gates to a Trojan horse of scienter.

[35] Regulation Best Interest, *supra* note 2, at 97-99.

[36] *Id.* at 353.

of NASAA members and brokerage industry representatives in 2014.[37] The version adopted by the Commission should, however, include the fees the customer will pay for all of the services provided by the firm and any other remuneration paid by third parties to the broker-dealer that are related to those services. The Model Fee Table has been successful for those brokerage firms that have adopted it and it provides a clear, concise and standardized approach to the disclosure of miscellaneous broker-dealer fees.

10. No Preemption of State Law

There is no indication in proposed Regulation Best Interest that the Commission is seeking to impact broker-dealer duties under state law in any respect. This is eminently appropriate. It is well settled that federal and state securities laws co-exist and that past and present Congresses intend to maintain only limited preemption of state laws in this field. The SEC rule proposal acknowledges that the duties it proposes would align with duties imposed by state law.[38] There is thus no conflict of laws. Assuming *arguendo* that the Commission could, as a legal principle, preempt state securities laws through the adoption of Regulation Best Interest, we request that the Commission affirm in any final rulemaking that it has no intention of doing so. To the extent this issue ever is litigated, it would be useful to future triers of fact for the Commission to speak to this issue, even if merely in a footnote.

III) Form CRS Relationship Summary, Amendments to Form ADV, Required Disclosures, and Restrictions on the Use of Certain Names or Titles

1. Form CRS Relationship Summary, Amendments to Form ADV and Required Disclosures

NASAA fully supports the Commission's objective of reducing investor confusion as to the differences between broker-dealers and investment advisers. The Commission proposes Form CRS as a means to this end. We appreciate the SEC's efforts to develop Form CRS, however we believe a better approach would be to engage in a comprehensive bottom-up review and revision of the Form ADV and Form BD to incorporate investor education objectives into these existing forms, rather than bolting an entirely new form onto the existing disclosure structure. Form ADV and Form BD are long overdue for reformatting and rewriting (for many reasons). Incorporating an investor education component and updating these forms for the 21st century would be the best long-term solution to the problem of investor confusion. This would also reduce or eliminate duplication across these various forms. (In particular, investment advisers will necessarily duplicate some disclosures between Form ADV Parts 1 & 2 and proposed Form CRS.) But

[37] *See* NASAA Model Fee Disclosure Resource Center, http://www.nasaa.org/industry-resources/broker-dealers/model-fee-disclosure-resource-center/.

[38] *See* Regulation Best Interest, *supra* note 2, at 202, 277.

because we recognize a holistic redesign of Forms ADV and BD is unlikely in the near term, we provide specific comments on the proposed Form CRS below.

The Commission staff included three mock-up Form CRS's in Appendices C through E of the proposal. These examples were drafted for a hypothetical broker-dealer, an investment adviser, and a dually-registered firm. These examples should be withdrawn from the proposal. For while they are avowedly not intended as safe harbors or schoolbook solutions to preparing a Form CRS, their mere existence as an approved expression of the Commission would tend to cabin the stylistic freedom of broker-dealers and investment advisers to craft their own Form CRS disclosures in ways that best speak to their customers. (For instance, we find the comments of Susan Kleiman during the SEC Investor Advisory Committee's June 14, 2018, meeting in Atlanta, Georgia, to be compelling with regard to the need for flexibility and clarity in these disclosures.)[39] Because of the criticality of setting proper standards for the structure and content of Form CRS, we reiterate a request we and numerous other organizations made in a May 21, 2018, letter to Chairman Clayton that the Commission delay implementation of Form CRS until thorough analysis of the form can be completed.[40] Form CRS is unlikely to become palatable to retail investors without thorough pre-release product testing.

This testing should consist, at a minimum, of professionally managed focus groups of retail investors being presented with examples of CRS-like disclosures and queried for their assessments of the form's format, content, and utility. Participants in the focus group should be given various model disclosures and asked to evaluate the clarity of the forms and information. Participants should be further queried as to their comprehension of the content in the disclosure documents. Expending resources in retaining experts to assist the Commission in the design and testing of such disclosures would, in our opinion, be a prudent step to take given the importance of these potential new disclosure documents.

Furthermore, we see no benefit in a "one size fits all" enterprise-wide disclosure document summarizing all the services and fees offered by the firm, as it is likely customers will simply disregard the disclosures. Instead, firms should have some level of flexibility in crafting their own Form CRS so that it is tailored for the different types of customers they service. This would make the forms much more useful to retail investors. Also, while we are not opposed to the SEC setting out required language and placement of certain aspects of the form, as this approach will make it easier for clients to locate this information and make side-by-side comparisons, meaningful Form CRS disclosures cannot be 'cookie cutter' and thus necessarily will have to differ from one firm to the next.

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[39] *See* Investor Advisory Committee Meeting Webcast (Part 2), June 14, 2018, Statement of Susan Kleiman (beginning at 21:00 mins.), *available at* https://www.sec.gov/video/webcast-archive-player.shtml?document_id=061418iac-2.

[40] *See* Letter to Hon. Jay Clayton (May 21, 2018), *available at* https://consumerfed.org/wp-content/uploads/2018/05/groups-ask-SEC-to-delay-comment-deadline-for-best-interest-proposal.pdf.

In the event the SEC nonetheless moves forward to adopt Form CRS as proposed, we recommend the following revisions to make it more digestible for consumers. First, Form CRS should specify minimum account size and include information on miscellaneous fees different categories of investors can expect to pay. Firms should also have the flexibility to use Form CRS for disclosure of state law requirements that they may be subject to.

Second, the elements of Form CRS should be revised. Currently, Form CRS contemplates disclosure in Item 7, "Additional Information," of where retail investors can find more information about a firm's disciplinary events, services, fees, and conflicts. The descriptor "Additional Information" is too vague to describe the important information in this section. Item 7 should be recast as "Disciplinary History and Customer Rights and Remedies" and this section should include three things: (a) an overview of the firm's disciplinary history (including embedded hyperlinks to the firm's most recent disclosure report on FINRA BrokerCheck or the Investment Adviser Registration Depository ("IARD") when the form is delivered electronically so these reports are just a mouse-click away); (b) a discussion of customer's legal rights and the remedies available to customers in the event of breach (including whether the customer will be subject to mandatory arbitration); and (c) contact information for regulators where investors may file complaints or ask questions about disciplinary history.[41]

Finally, the SEC should amend certain delivery and procedural aspects of Form CRS as proposed. The proposal would require investment advisers to deliver Form CRS to each retail investor at or before entering into an investment advisory agreement and require broker-dealers to deliver the form at or before providing any services.[42] To be effective, Form CRS must be delivered to customers in a timely fashion. Delivery should always precede the provision of any advisory or brokerage services with sufficient time for the customer to review the form and ask questions. Thus, the SEC should not permit Form CRS delivery "at" the time of service but rather should always require delivery "before" the provision of services. As to updates to Form CRS, we would urge the Commission to amend proposed Rule 204-5(b)(4) and proposed Rule 17a-14(c)(4) to require that firms deliver updated Form CRS's whenever there is a change, rather than permitting firms to potentially communicate the information to investors in other ways as has been proposed.[43] In addition, broker-dealers should not use the SEC's Electronic Data Gathering, Analysis and Retrieval System ("EDGAR") to file Form CRS as has been proposed. Rather, broker-dealers should file Form CRS on the WebCRD platform maintained by FINRA for its BrokerCheck reports (and which is related to IARD).

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[41] Investors could be directed to www.nasaa.org, where they can find contact information for state regulators.

[42] Form CRS Relationship Summary, *supra* note 3, at 138.

[43] *See id.* at 146 – 47.

2. Restrictions on the Use of Certain Names or Titles

The proposal would prohibit broker-dealers and their associated persons from labeling themselves as an "adviser" (or "advisor") to a retail customer unless they were also licensed as an investment adviser or investment adviser representative. This is appropriate and should be adopted. This rule change will help forestall retail investors' confusion about the different roles and duties owed by broker-dealers/agents and investment advisers/investment adviser representatives.

The Commission requested comment, though, on whether additional terms should be restricted as well or whether other limitations on practice by broker-dealers should be adopted.[44] As a threshold matter, we believe restricting just two words – "adviser" and "advisor" – is insufficient. There are many more terms broker-dealer agents can use to clothe themselves in a fiduciary guise. But rather than creating a lengthy list of additional restricted terms, we believe an approach that combines both an explicit prohibition on the use of "advisor" and "adviser" with enumerated factors aimed at limiting the use of other potentially misleading titles is the better approach.

The Commission thus should adopt a rule along the following lines: broker-dealers and their agents that are not dually-registered as investment advisers or investment adviser representatives cannot use the words "adviser" or "advisor" in their titles or otherwise hold themselves out in a way that could reasonably be expected to convey inaccurate information to any person as to: (i) the nature of the person's registration status; (ii) the person's proficiency, experience or qualifications; (iii) the nature of the person's relationship, or potential relationship, with a registrant; or (iv) the products or services that are provided or that may be provided by the person. (As an example of such a holding out rule, see Rule 13.18, "Misleading Communications," recently proposed by the Canadian Securities Administrators ("CSA") for potential use by provincial securities regulators in that country.)[45]

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[44] *Id.* at 186.

[45] *See* Reforms to Enhance the Client-Registrant Relationship, CSA Notice and Request For Comment, June 21, 2018 (Annex A, page 9), *available at* https://docs.mbsecurities.ca/msc/registration/en/312021/1/document.do:

> *13.18 Misleading communications*
> *(1) A registered individual must not hold himself or herself out, and a registered firm must not hold itself or its registered individuals out, in a manner that could reasonably be expected to deceive or mislead a person as to any of the following matters:*
> *(a) the proficiency, experience, or qualifications of the registrant;*
> *(b) the nature of the person's relationship, or potential relationship, with the registrant;*
> *(c) the products or services provided, or to be provided, by the registrant.*
> *(2) Without limiting subsection (1), a registered individual must not use any of the following:*

IV) Standards of Conduct for Investment Advisers

We appreciate the SEC's encapsulation of investment adviser duties in the Standards of Conduct for Investment Advisers release.[46] The release is a useful resource. More importantly, though, it should become an enforceable expression of investment adviser law once it is adopted by the Commission pursuant to the Administrative Procedures Act ("APA").[47] The proposal would thereafter stand on its own as a legal expression of the duties owed by investment advisers.

1. Duty to Mitigate Conflicts of Interest

We agree with the proposal that mere disclosure of actual or potential conflicts of interest may not always satisfy an investment adviser's duties under federal or state securities laws.[48] An investment adviser cannot, for example, cure fraudulent conduct through disclosure.[49] The scope of an investment adviser's duty to mitigate conflicts is not well developed in the law and this has not been a source of litigation. We would accordingly encourage the SEC to develop this issue more thoroughly in the investment adviser conduct proposal. In particular, the proposal should incorporate other sources of law to clarify that an investment adviser's duty to mitigate conflicts is an affirmative obligation[50] which must be performed in an objectively reasonable manner.[51] In addition, we encourage the Commission to make the following change to the text of the proposed rulemaking (at footnote 30):

> *"For example, if an adviser advises its clients to invest in a mutual fund share class that is more expensive than other available options when the adviser is receiving compensation that creates a potential conflict and that may reduce the client's*

> *(a) a title, designation, award, or recognition that is based partly or entirely on that registered individual's sales activity or revenue generation;*
> *(b) a corporate officer title unless their sponsoring firm has appointed that registered individual to that corporate office pursuant to applicable corporate law;*
> *(c) a title or designation, unless the individual's sponsoring firm has approved the use by that registered individual of that title or designation.*

[46] Proposed Commission Interpretation of Conduct for Investment Advisers, *supra* note 4.

[47] *Cf. NRDC v. EPA*, 643 F.3d 311 (D.C. Cir. 2011) (vacating regulatory guidance regarding compliance with the federal Clean Air Act by the Environmental Protection Agency because it had not been issued pursuant to public notice and comment as required by the APA).

[48] *See* Proposed Commission Interpretation of Conduct for Investment Advisers, *supra* note 4, at 23.

[49] *SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 190 (1963) (discussing congressional intent underlying the Investment Advisers Act of 1940 to "mitigate and, so far as is presently practicable to eliminate" fraudulent practices by requiring disclosure of all actual or potential conflicts of interest).

[50] *United States v. Brookridge Farm*, 111 F.2d 461, 466 (10th Cir. 1940).

[51] *Austin Hill County Realty v. Palisades Plaza*, 948 S.W.2d 293, 299 (Tex. 1997).

> *return, the adviser ~~may violate~~ would violate its fiduciary duty and the antifraud provisions of the Advisers Act if it does not, at a minimum, provide full and fair disclosure of the conflict and its impact on the client and obtain informed client consent to the conflict."*[52]

2. Minimum Financial Requirements for SEC-Registered Advisers

The investment adviser proposal requests comment on whether SEC-registered investment advisers should be subject to a financial responsibility obligation (such as broker-dealers are under the net capital rule).[53] The proposal posits NASAA's own Model Rule 202(d)-1 (the "NASAA Model Rule") as a potential guidepost.[54]

The NASAA Model Rule was designed for smaller investment advisers registered and regulated by state securities administrators. It is not geared for larger investment advisers overseen by the SEC. Accordingly, to the extent the SEC seeks to implement financial responsibility standards for investment advisers, the broker-dealer net capital rule is likely a more appropriate guidepost than the NASAA Model Rule.

3. Investment Adviser Representative Registration and Continuing Education

The proposal requests comment on whether investment adviser representatives should be "subject to federal continuing education and licensing requirements" by the SEC.[55] Today there are approximately 350,000 investment adviser representatives associated with SEC-registered or state-registered investment advisers. State securities administrators license these individuals; the SEC does not. (Many of these individuals are also dually-registered broker-dealer agents registered with FINRA.) This apportioning of regulatory responsibilities is entirely appropriate.

The SEC already regulates thousands of broker-dealers and investment advisers. It should not stretch its limited resources even further by taking on direct regulatory responsibility for hundreds of thousands of investment adviser representatives. Rather, state securities regulators should continue performing this function. NASAA and its members have developed robust rules and processes (including a testing regime) to oversee investment adviser representatives. As the Commission is aware, NASAA is also studying a potential continuing education requirement for

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[52] *See* Proposed Commission Interpretation of Conduct for Investment Advisers, *supra* note 4, at 12.

[53] *Id.* at 35 – 37.

[54] Minimum Financial Requirements for Investment Advisers, NASAA Model Rule 202(d)-1 (as amended Sept. 11, 2011), *available at* http://www.nasaa.org/wp-content/uploads/2011/07/IA-Model-Rule-Minimum-Financial-Requirements.pdf.

[55] Proposed Commission Interpretation of Conduct for Investment Advisers, *supra* note 4, at 28 – 31.

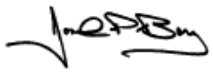
these investment adviser representatives. NASAA welcomes continued dialogue with the SEC staff as NASAA develops this issue, but SEC rulemaking on this front is wholly unnecessary.

* * *

The Commission seeks through the Proposals to raise the duties of care owed by broker-dealers, address the confusion among investors regarding the differing conduct standards, and make clearer the various aspects of the fiduciary duty standard applicable to investment advisers. The Commission is seeking to do all of this without favoring or disfavoring the broker-dealer or investment advisory business models. We recognize that threading this needle is not easy. As the SEC staff and Commissioners work to review stakeholder comment letters and consider potential revisions for what ultimately may become a final rule, we want to emphasize that it is more important that the Proposals be implemented appropriately than that this be done quickly. Investor protection should be the first priority and industry objections to cost or the impacts on business should be taken with the proverbial "grain of salt," as regulators have heard similar complaints in the face of new regulatory requirements in the past. The financial services industry is adaptive and can modify operations to account for new regulatory requirements as demonstrated by their work to comply with the Department of Labor's now defunct 2016 fiduciary duty rule.[56]

In conclusion, for the reasons discussed herein, we generally support the Proposals, however we recommend the Commission undertake certain revisions to the Proposals to improve them prior to adoption. If you have any questions about this letter or would like to discuss these issues, please contact me (joseph.borg@asc.alabama.gov or 334-242-2984) or NASAA Executive Director Joseph Brady (jb@nasaa.org or 202-737-0900).

Sincerely,



Joseph P. Borg
NASAA President
Director, Alabama Securities Commission

[56] *See* Deloitte, The DOL Fiduciary Rule: A Study on How Financial Institutions Have Responded and the Resulting Impacts on Retirement Investors, (Aug. 9, 2017), https://www.sifma.org/wp-content/uploads/2017/08/Deloitte-White-Paper-on-the-DOL-Fiduciary-Rule-August-2017.pdf (finding that, among the 21 financial services firms surveyed, implementation of the DOL rule resulted at most in only temporary business disruptions).

ATTACHMENT

17 CFR Part 240

Brokers, Reporting and recordkeeping requirements, Securities.

Text of the Proposed Rules

In accordance with the foregoing, Title 17, Chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 240 – GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for part 240 is revised by adding sectional authorities for section 240.15*l*-1 to read as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78c-3, 78c-5, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78n-1, 78o, 78o-4, 78o-10, 78p, 78q, 78q-1, 78s, 78u-5, 78w, 78x, 78dd, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, 7201 *et seq.*, and 8302; 7 U.S.C. 2(c)(2)(E); 12 U.S.C. 5221(e)(3); 18 U.S.C. 1350; Pub. L. 111-203, 939A, 124 Stat. 1887 (2010); and secs. 503 and 602, Pub. L. 112-106, 126 Stat. 326 (2012), unless otherwise noted.

* * * * *

Section 240.15*l*-1 is also issued under Pub. L. 111-203, sec. 913, 124 Stat. 1376, 1827 (2010).

* * * * *

2. Add § 240.15l-1 to read as follows:

§ 240.15*l*-1 ~~Regulation Best Interest~~Broker-Dealer Standard of Conduct.

(a) Best Interest Obligation.

(1) A broker, dealer, or a natural person who is an associated person of a broker or dealer, when making a recommendation of any securities transaction or investment strategy involving securities to a ~~retail~~ customer, shall act in the best

interest of the ~~retail~~ customer at the time the recommendation is made, without placing the financial or other interest of the broker, dealer, or natural person who is an associated person of a broker or dealer making the recommendation ahead of the interest of the ~~retail~~ customer.

(2) The best interest obligation in paragraph (a)(1) shall be satisfied if:

(i) Disclosure Obligation. The broker, dealer, or natural person who is an associated person of a broker or dealer, prior to or at the time of such recommendation, reasonably discloses to the ~~retail~~ customer, in writing, the material facts relating to the scope and terms of the relationship with the ~~retail~~ customer~~, including~~ and all material facts, including risks, costs, and conflicts of interest, that are associated with the recommendation.

(ii) Care Obligation. The broker, dealer, or natural person who is an associated person of a broker or dealer, in making the recommendation exercises reasonable diligence, care, skill, and prudence to:

(A) Understand the potential risks and rewards associated with the recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some ~~retail~~ customers;

(B) Have a reasonable basis to believe that the recommendation is in the best interest of a particular ~~retail~~ customer based on that ~~retail~~ customer's investment profile and the potential risks, costs, and rewards associated with the recommendation; and

(C) Have a reasonable basis to believe that a series of recommended transactions, even if in the ~~retail~~ customer's best interest when viewed in isolation, is not excessive and is in the ~~retail~~ customer's best interest when taken together in light of the ~~retail~~ customer's investment profile.

(iii) Conflict of Interest Obligations.

(A) The broker, ~~or~~ dealer, or natural person who is an associated person of a broker or dealer ~~establishes, maintains, and enforces written~~

~~policies and procedures reasonably designed to~~ identifies~~y~~ and at a minimum discloses, or eliminates, all material conflicts of interest that are associated with such recommendations in accordance with policies and procedures established, maintained, and enforced by the broker or dealer.

(B) The broker, ~~or~~ dealer, or natural person who is an associated person of a broker or dealer ~~establishes, maintains, and enforces written policies and procedures reasonably designed to~~ identifies~~y~~ and discloses and mitigates, or eliminates, material conflicts of interest arising from financial incentives associated with such recommendations in accordance with policies and procedures established, maintained, and enforced by the broker or dealer.

(b) *Definitions*. Unless otherwise provided, all terms used in this rule shall have the same meaning as in the [Securities Exchange Act of 1934]. In addition, the following definitions shall apply:

(1) *Act in the Best Interest* means making recommendations that reflect the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use taking into consideration all of the facts and circumstances, including costs, in light of the investment profile of the customer to whom the recommendation is made.~~-~~

(2) ~~*Retail*~~ *Customer* means any person, or the legal representative of such person, who~~:~~

~~(A) R~~ receives a recommendation of any securities transaction or investment strategy involving securities from a broker, dealer, or a natural person who is an associated person of a broker or dealer~~; and~~

~~(B) Uses the recommendation primarily for personal, family, or household purposes~~.

(3~~2~~) ~~*Retail*~~ *Customer Investment Profile* includes, but is not limited to, the ~~retail~~ customer's age, where applicable, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose to the broker, dealer, or a natural person who is an associated person of a broker or dealer in connection with a recommendation.

3. Amend § 240.17a-3 by adding new paragraph (a)(25) to read as follows:

§ 240.17a-3 Records to be made by certain exchange members, brokers and dealers.
(a)***

(25) For each retail customer to whom a recommendation of any securities transaction or investment strategy involving securities is or will be provided:
(i) A record of all information collected from and provided to the retail customer pursuant to § 240.15*l*-1, as well as the identity of each natural person who is an associated person, if any, responsible for the account.

(ii) For purposes of this paragraph (a)(25), the neglect, refusal, or inability of the retail customer to provide or update any information required under paragraph (a)(25)(i) of this section shall excuse the broker, dealer, or associated person from obtaining that required information.

* * * * *

4. Amend § 240.17a-4 by revising paragraph (e)(5) to read as follows:

§ 240.17a-4 Records to be preserved by certain exchange members, brokers and dealers.

* * * * *
(e) ***
(5) All account record information required pursuant to § 240.17a-3(a)(17) and all records required pursuant to § 240.17a-3(a)(25), in each case until at least six years after the earlier of the date the account was closed or the date on which the information was collected, provided, replaced, or updated.