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February 10, 2020

By email to: rule-comments@sec.gov

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

RE: File No. S7-21-19: NASAA Comment Letter on Proposed Amendments to Rules Regarding Investment Adviser Advertisements and Compensation for Solicitations

Dear Ms. Countryman:

On behalf of the North American Securities Administrators Association, Inc. (“NASAA”),¹ I am writing in response to U.S. Securities and Exchange Commission (the “SEC” or “Commission”) Release No. IA-5407, Investment Adviser Advertisements; Compensation for Solicitations (the “Rule Proposal”), to amend Rules 206(4)-1, 206(4)-3, and 204-2, as well as Form ADV,² under the Investment Advisers Act of 1940 (the “Advisers Act”).³ The Rule Proposal would make significant changes to the existing rules governing the manner in which investment advisers market their services and seek, obtain, and retain clients.

NASAA agrees that the current rules regarding investment adviser advertising and compensation for solicitors – adopted in 1961 and 1979, respectively – should be updated to better reflect modern methods of communication, investor expectations and industry practice. However, the investor protection principles embodied by the original rules must be preserved regardless of the changes in how firms advertise or communicate with clients. Accordingly, while NASAA supports many aspects of the Rule Proposal, it is our view that the Rule Proposal needs to be

¹ Organized in 1919, NASAA is the oldest international organization devoted to investor protection. NASAA’s membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico, and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

² See 17 CFR § 279.1.

³ The Rule Proposal is available at <https://www.sec.gov/rules/proposed/2019/ia-5407.pdf>.

revised in order to better protect investors from potentially misleading advertising claims. Our proposed revisions are set forth below.

1. Investment Adviser Advertisements

The Commission adopted the current investment adviser advertising rule, Rule 206(4)-1, in 1961 to protect investors from potential harm as a result of misleading or deceptive advertising practices by investment advisers. When the Commission initially proposed the rule, it explained that investment advisers should be held “to a stricter standard of conduct than that applicable to ordinary merchants” in their advertising because “securities are ‘intricate merchandise.’”⁴ The Commission also recognized that investors “are frequently unskilled and unsophisticated in investment matters” and it is often to those investors “that a substantial amount of investment advisory advertising is directed[.]”⁵ Rule 206(4)-1 has not been changed substantively since its adoption. The Commission proposes to replace the current Rule 206(4)-1 with a new rule that would substantially revise both the scope of communications regulated as “advertisements” under the rule, as well as the requirements applicable to investment adviser advertisements (the “Proposed Advertising Rule”).

a. The Proposed Advertising Rule appropriately differentiates between retail and non-retail persons.

In certain circumstances, the Proposed Advertising Rule would impose different obligations on investment advisers when they advertise to retail investors than when they advertise exclusively to non-retail investors. The Proposed Advertising Rule would define a “non-retail person” as either a “qualified purchaser” or a “knowledgeable employee,” as both are defined in Rule 3c-5 under the Investment Company Act of 1940.⁶ A “retail person” would be defined to include any person other than a “qualified purchaser” or a “knowledgeable employee.”⁷ Similarly, the Proposed Advertising Rule would define “non-retail advertisement” to be “any advertisement for which an investment adviser has adopted and implemented policies and procedures reasonably designed to ensure that the advertisement is disseminated solely to non-retail persons.”⁸ A “retail advertisement” would be defined to include all other advertisements.⁹

⁴ Investment Advisers Notice of Proposed Rulemaking, Release No. IA-113 (Apr. 4, 1961) (“Notice of Proposed Rulemaking”) [26 F.R. 3070, 3071 (Apr. 11, 1961)]. *See also* Advertisements by Investment Advisers, Release No. IA-121 (Nov. 1, 1961) [26 F.R. 10548, 10549 (Nov. 9, 1961)].

⁵ Notice of Proposed Rulemaking, 26 F.R. at 3071 (Apr. 11, 1961).

⁶ Proposed Rule 206(4)-1(e)(8).

⁷ Proposed Rule 206(4)-1(e)(14).

⁸ Proposed Rule 206(4)-1(e)(7).

⁹ Proposed Rule 206(4)-1(e)(13).

The Commission explains that it considered, but is not proposing, to include other standards into the definition of “non-retail person,” including: “accredited investors,” as defined in Rule 501(a) of Regulation D under the Securities Act of 1933 (the “Securities Act”); “qualified clients,” as defined in Rule 205-3(d)(1) under the Advisers Act; and “retail investors,” as defined for the purpose of the Form CRS relationship summary.¹⁰ These standards generally focus on a person’s financial ability to absorb investment losses and the purpose for which they might be seeking financial advice. Therefore, NASAA agrees that these standards would not signal adequately that a person has the necessary analytical and other resources to assess the contents of an advertisement and avoid being misled. NASAA believes that the Commission has appropriately excluded these standards from the definition of “non-retail person.”

The Commission’s approach in the Rule Proposal is appropriate and will enhance the investor protection benefit from the Proposed Advertising Rule if it is adopted.

b. The proposed definition of “advertisement” must be more narrowly tailored with respect to certain communications.

In order for a communication to be treated as an “advertisement” under the current Rule 206(4)-1, it must be disseminated in writing, by radio, or by television, and it must “offer” certain services related to securities.¹¹ In the decades since the Commission adopted Rule 206(4)-1, advances in technology and common methods of communication have rendered the current definition obsolete and ineffective. The Proposed Advertising Rule would substantially expand and generalize the definition of “advertisement” to include any communication that is (1) disseminated by any means, (2) by or on behalf of an investment adviser, and (3) offers or promotes the investment adviser’s services, or seeks to obtain or retain investment advisory clients or investors in a pooled investment vehicle. This proposed definition of “advertisement” better captures modern methods of communication and focuses the definition on the goal of the communication. It also is more likely to remain relevant as methods of communication evolve.

However, certain communications would be excluded from the proposed definition of “advertisement,” and therefore from the investor protections provided by the rule. These include all non-broadcast live oral communications and “materials that provide general educational information about investing or the markets.” It is NASAA’s view that these exclusions are overbroad. The Proposed Advertising Rule should take a more tailored approach to these types of communications, rather than exclude them categorically.

¹⁰ Rule Proposal at 114.

¹¹ 17 CFR § 275.206(4)-1(b).

i. Non-broadcast live oral communications should be treated as advertisements.

Under the Proposed Advertising Rule, “live oral communications that are not broadcast on radio, television, the internet, or any other similar medium” would not be treated as advertisements, even when such communications are clearly promotional in nature.¹² The exclusion appears to be motivated in part by a desire to preserve investors’ ability to have face-to-face conversations with their investment adviser,¹³ as well as a concern that including these communications would pose “compliance difficulties,” such as recordkeeping and “applying the other substantive requirements of the proposed rule” to these remarks.¹⁴ Such live oral communications should be treated as advertisements and subject to the requirements of the Proposed Advertising Rule in a tailored manner.

The Commission recognizes that the exclusion would apply to communications that are commonly promotional in nature.¹⁵ In fact, the Commission explains these statements would be treated as advertising if they were prepared in advance in writing.¹⁶ The Commission does not explain in the Rule Proposal why such a discrepancy should exist, at least not with respect to the content requirements in the Proposed Advertising Rule. Such a categorical exclusion could be abused by unscrupulous registrants, and therefore promotional communications, however offered to an investor, should fall under the definition. The perceived recordkeeping and other logistical difficulties are an insufficient reason to offer investment advisers a clear means to evade the intent of the Proposed Advertising Rule. Moreover, it is those investors “frequently unskilled and unsophisticated in investment matters”¹⁷ that are the intended beneficiaries of the rule, and yet at the same time are the investors most likely to be misled by unscrupulously crafted oral promotional communications.

¹² Proposed Rule 206(4)-1(e)(1)(i), Rule Proposal at 472.

¹³ Rule Proposal at 42.

¹⁴ Rule Proposal at 43.

¹⁵ Rule Proposal at 43 (“We recognize that excluding such public oral communications from the proposed definition of ‘advertisement’ may result in many commonly used forms of promotional communication not being subject to the protections and requirements of the proposed rule.”).

¹⁶ Rule Proposal at 41 (“[A]ny script or storyboards, or other written materials prepared in advance for use during a live oral communication, as well as any slides or other written materials presented alongside or distributed as part of the live oral communication, would fall within the proposed definition of ‘advertisement’ if those materials otherwise meet the definition of ‘advertisement.’”).

¹⁷ Notice of Proposed Rulemaking, 26 F.R. at 3071 (Apr. 11, 1961).

The Commission offers relatively innocuous-sounding examples of communications that would be excluded, including “an unscripted talk at a luncheon or a conference appearance.”¹⁸ However, the exclusion would also apply to more direct promotional communications such as investor pitch meetings and restaurant seminars. State regulators have frequently encountered restaurant seminars targeting vulnerable investors or promoting risky alternative investments. In the experience of NASAA’s members, oral pitches are all too often vehicles for a variety of investing ills, from the distribution of unsuitable products to outright frauds. Yet, the Proposed Advertising Rule would exclude the remarks made during such seminars from meaningful oversight. Absent review and approval of written materials beforehand, and meaningful supervision to ensure that the live remarks are not deceptive or misleading, it is not clear that there would be any accountability for statements made during these seminars. In fact, by justifying the exclusion with the purported difficulty of “applying the other substantive requirements of the proposed rule to such unscripted remarks,”¹⁹ the Commission seems to imply that an investment adviser cannot reasonably be expected to supervise these promotional activities in any meaningful way. The Commission’s discussion also contains an assumption that oral promotional communications are typically ad hoc and conversational. In the experience of state enforcement personnel, that is often not the case.

The better approach would be to treat certain non-broadcast live oral communications as advertisements subject to the rule, and prohibit such communications unless the investment adviser has first reviewed and approved a written script, detailed outline, slide deck, or other similar written material setting out the content of the communication. If the Commission is disinclined to require that certain non-broadcast live oral communications be scripted in advance, live oral communications should at least be subject to the general prohibitions and the provisions regarding performance advertising, testimonials, endorsements, and third-party ratings. In order to tailor the rule to the practical limitations of these communications, the Proposed Advertising Rule could exempt non-broadcast live oral communications from the review, approval, and recordkeeping provisions. Under either approach, the Commission should clarify that an investment adviser’s supervisory obligation includes taking reasonable steps to ensure that live oral communications are consistent with pre-approved written material and otherwise comply with the substantive requirements in the Proposed Advertising Rule.

- ii. *“Materials that provide general educational information about investing or the markets” should be treated as advertisements when they are prepared, developed, or published by or on behalf of the investment adviser.*

In the Rule Proposal, the Commission explains that it would not view “materials that provide general educational information about investing or the market” as communications that offer or promote investment advisory services, or that seek to obtain or retain investors.²⁰ The

¹⁸ Rule Proposal at 43.

¹⁹ Rule Proposal at 43.

²⁰ Rule Proposal at 32.

Commission illustrates its point with the example of an investment adviser disseminating “a newspaper article about the operation of investment funds or the risks of certain emerging markets.”²¹ However, many investment advisers prepare and disseminate their own content, whether in writing, in mailings, over the internet, on the radio, or on television. When an investment adviser writes an article, disseminates a client newsletter, or appears on a radio or television show, they are likely doing so, at least in part, to promote their services by demonstrating their knowledge and competence. Accordingly, the Proposed Advertising Rule should differentiate between the dissemination of third-party materials that are literally “passed on” by an adviser and the dissemination of general educational communications that are developed or sourced by the investment adviser itself. The latter should be treated as advertisements in light of their promotional nature and potential to mislead investors.

c. The Commission should provide additional guidance as to the meaning of “fair and balanced.”

The Proposed Advertising Rule would lift the *per se* prohibition on references to past specific recommendations²² and replace it with the requirement that references to past specific recommendations be “fair and balanced.”²³ The Proposed Advertising Rule would also allow performance advertising, subject to the same standard.²⁴ The Commission provides limited guidance on how advisers and Commission staff will determine that the presentation of past specific recommendations or performance results is “fair and balanced.” The best the Commission has done is to provide a few examples and note that the relevant factors “will vary based on the facts and circumstances.”²⁵

The principles-based “fair and balanced” approach leaves too much to the discretion of the investment adviser. The Commission does not explain what it would deem “sufficient information and context to evaluate the merits of th[e] advice,”²⁶ “sufficient information for an investor to assess how the results were determined,”²⁷ or “sufficient context for the investor to evaluate the utility of the results[.]”²⁸ The lack of clear limits would likely create an incentive for many

²¹ *Id.*

²² 17 CFR § 275.206(4)-1(a)(2)

²³ Proposed Rule 206(4)-1(a)(5), Rule Proposal at 469.

²⁴ Proposed Rule 206(4)-1(a)(6), Rule Proposal at 469.

²⁵ Rule Proposal at 64-66, 69.

²⁶ Rule Proposal at 64.

²⁷ Rule Proposal at 69.

²⁸ *Id.*

investment advisers to test the bounds of the rule in order to attract as many clients as possible, which would result in poorly informed decisions on the part of investors and could yield substantial investor harm.

The Commission notes that Rule 156 under the Securities Act²⁹ and FINRA Rule 2210³⁰ both contain a similar provision.³¹ NASAA encourages the Commission to provide further guidance as to the meaning of “fair and balanced,” including whether the Commission intends to incorporate the body of judicial and administrative decisions regarding Rule 156 and FINRA Rule 2210.

d. The Proposed Advertising Rule should retain certain prohibitions from the current Rule 206(4)-1 in retail advertisements.

The Commission correctly recognizes that the goal of advertisements – to obtain or retain business – creates an incentive for investment advisers to mislead existing and prospective investors about the advisory services they would receive.³² In order to protect investors from these risks, Rule 206(4)-1 broadly prohibits certain content in investment adviser advertisements. Specifically, the current rule prohibits the dissemination of advertisements that contain: (1) reference to testimonials of any kind; (2) reference to past specific recommendations which were or would have been profitable to any person, unless the investment adviser provides details of *all* of its recommendations during the immediately preceding period of not less than one year; (3) representations that any graph, chart, formula, or other device being offered can be used by itself to determine which securities to buy and sell or when to do so; (4) statements to the effect that any report, analysis, or other service will be free or without charge, unless it actually will be provided without any condition or obligation; and (5) untrue statements of material fact and statements which are otherwise false or misleading.³³

The Proposed Advertising Rule would replace these prohibitions with principles-based provisions and conditions intended to ensure that advertisements containing such references and representations are not misleading to investors. While many of the provisions are reasonably drawn, the Commission should retain certain *per se* prohibitions in the Proposed Advertising Rule.

²⁹ 17 CFR § 230.156, Investment company sales literature.

³⁰ Communications with the Public.

³¹ Rule Proposal at 56.

³² Rule Proposal at 8.

³³ 17 CFR § 275.206(4)-1(a).

i. The Proposed Advertising Rule should prohibit the presentation of performance results in retail advertisements.

The Proposed Advertising Rule would permit investment advisers to disseminate advertisements containing performance results, including hypothetical performance, as long as the presentation is “fair and balanced,” and complies with other substantive conditions.³⁴ The Commission justifies this proposed change by explaining that “a prospective investor may reasonably wish to see performance results attributable to an adviser that the prospective investor may consider hiring.”

Performance results, particularly hypothetical performance, are of questionable utility to most investors. Backtested performance may suffer from hindsight bias. Representative, or “model” portfolio, performance may not be an accurate representation of how an investment adviser will manage a portfolio with real assets at risk for investors with varying degrees of risk tolerance. Targets and projections are undefined in the Proposed Advertising Rule and may often be presented in a manner that implies more certainty than is appropriate. Again, regulatory enforcement experience is instructive here; both federal and state regulators have found fault with hypothetical and backtested performance results in terms of assumptions used, investments selected, and hindsight revisions to models that are not representative of how the adviser acted previously, or how its approach would have performed in actual practice.

The limited utility of performance information is outweighed by the risk that such a presentation will materially mislead investors, especially those who are less familiar with the many components that influence the capital markets and portfolio performance. The Commission appears to recognize the many risks presented by performance advertising, including the risk that “reasonable investors” will make “unwarranted assumptions” that the advertised performance results are predictive of what the investor would achieve under the investment adviser’s management.³⁵ NASAA agrees that “investors may be influenced heavily by the manner in which past performance is presented,”³⁶ and this is most likely to be the case with retail persons, who most often lack access to the analytical and other resources necessary to assess and verify the advertised performance.³⁷ The guardrails proposed by the Commission for performance advertising do not sufficiently mitigate these risks.

The Proposed Advertising Rule would require that the presentation of performance results be “fair and balanced” and generally not false or misleading. However, as explained above, these standards are not well-defined in the Rule Proposal and leave too much to the discretion of investment advisers who have an incentive to push the boundaries of the rule. The specific

³⁴ See Proposed Rule 206(4)-1(a), (c), Rule Proposal at 468-71.

³⁵ Rule Proposal at 100.

³⁶ Rule Proposal at 100.

³⁷ See Rule Proposal at 101.

information required to be provided alongside performance results³⁸ is of limited value to a retail investor who may not have the requisite analytical resources to understand the significance of much of this information. The Commission acknowledges that hypothetical performance will often be ill-suited to the needs of retail investors.³⁹ Further, the Commission provides scant explanation regarding what information would be deemed “sufficient to enable [a] person to understand the assumptions made in calculating” hypothetical performance or “sufficient information to enable [a] person to understand the risks and limitations of using such hypothetical performance.”⁴⁰

Accordingly, NASAA strongly urges the Commission to revise the Proposed Advertising Rule to prohibit the presentation of performance results in retail advertisements. This information is of little utility to the vast majority of retail investors and that limited utility is outweighed by the risk of overreliance and unwarranted assumptions about the advertised performance and the perverse incentives it creates for the investment adviser crafting the advertisement. If the Commission is disinclined to retain this limited prohibition from the current Rule 206(4)-1, the Commission must provide additional guidance regarding investment advisers’ obligations with respect to the content requirements.

ii. The Proposed Advertising Rule should prohibit references to testimonials, endorsements, and third-party ratings in retail advertisements.

The Proposed Advertising Rule would permit investment advisers to disseminate advertisements containing reference to testimonials, endorsements, and third-party ratings. When the Commission adopted Rule 206(4)-1 in 1961, it recognized that investment adviser testimonials “are misleading; by their very nature they emphasize the comments and activities favorable to the investment adviser and ignore those which are unfavorable. This is true even when the testimonials are unsolicited and are printed in full.”⁴¹ The Commission’s analysis at the time it adopted Rule 206(4)-1 was reasonable and appropriate, but the Commission now appears to be abandoning that analysis. The Proposed Advertising Rule would allow investment advisers to disseminate advertisements referencing testimonials, endorsements, and third-party ratings, even when the investment adviser has paid for that content.⁴² The Commission should instead retain the prohibition in retail advertisements.

³⁸ See generally Proposed Rule 206(4)-1(c).

³⁹ Rule Proposal at 171.

⁴⁰ Rule Proposal at 172-77; Proposed Rule 206(4)-1(c)(1)(v), Proposed Rule at 470-71.

⁴¹ Advertisements by Investment Advisers, Release No. IA-121 (Nov. 1, 1961) [26 FR 10548, 10549 (Nov. 9, 1961)]

⁴² Proposed Rule 206(4)-1(b), Rule Proposal at 469.

NASAA does not dispute that “[t]echnological advances, including the development of the internet and social media platforms, have made the use and dissemination of testimonials easier and more widespread, and they continue to be an important resource for consumers and businesses.”⁴³ However, the Commission appears to ignore the necessary question of whether investment advisory services *should* be marketed in the same way as typical consumer goods and services. In our view, investment advice is critical to the everyday wellbeing of many investors, and investors should be encouraged to carefully consider whether to retain a particular investment adviser’s services. Allowing investment advisers to include testimonials, endorsements, and third-party ratings in its advertisements encourages the opposite. Many retail investors are unlikely to read the prescribed disclosures and will instead choose the highest rated investment adviser, regardless of whether that investment adviser’s investment philosophy and service offerings are truly best for that person. This, in turn, will provide incentive for investment advisers to purchase positive testimonials, endorsements, and third-party ratings, and to aggressively curate the presentation of this content in exactly the manner that the Commission was concerned about when it adopted Rule 206(4)-1 in 1961.

Accordingly, the Proposed Advertising Rule should be revised to prohibit testimonials, endorsements, and third-party ratings in retail advertisements. This approach is tailored to permit investment advisers to include such content in their advertisements if they take steps to ensure that these advertisements will only reach those who are well-situated to assess their reliability, *i.e.*, non-retail persons. If the Commission is disinclined to prohibit all testimonials, endorsements, and third-party ratings in retail advertisements, it should at minimum prohibit the use of those that are made by persons that are compensated by the investment adviser or those in which the investment adviser has influenced the content.

2. Compensation for Solicitors

The Commission adopted the current cash solicitation rule, Rule 206(4)-3, in 1979. The Commission proposes to expand Rule 206(4)-3 (the “Proposed Solicitation Rule”), “in part to reflect regulatory changes and the evolution of industry practices” since its adoption.⁴⁴ The Proposed Solicitation Rule would expand in several ways that would ultimately enhance the protections provided under the rule. Specifically, the Proposed Solicitation Rule would apply to non-cash compensation arrangements in addition to cash compensation, would require greater detail about compensation and conflicts of interest in the required disclosures, would apply equally to the solicitation of investors in private funds, and would incorporate certain actions by state securities regulators as disqualifying criteria for solicitors. Additionally, the Rule Proposal helpfully clarifies that the existing exclusion of solicitation for the provision of impersonal advisory services does not apply to robo-advisers and internet advisers, as these businesses provide individualized investment advisory services to their clients based on information provided by those clients.

⁴³ Rule Proposal at 76.

⁴⁴ Rule Proposal at 200.

These significant changes better reflect the regulatory and economic realities in the investment advisory industry and would meaningfully enhance the investor protections provided by oversight of compensated solicitors. NASAA generally supports the Proposed Solicitation Rule and encourages its adoption with certain revisions, outlined below.

a. Solicitors should provide the required disclosures in a written document.

Rule 206(4)-3 currently requires solicitors to deliver a “written disclosure document” at the time of any compensated solicitation activities.⁴⁵ The purpose of the disclosure requirement is “to ensure that the investor’s attention would be directed to the fact that the adviser pays the solicitor a cash referral fee and the incentives it may create.”⁴⁶

The Proposed Solicitation Rule would enhance solicitor disclosures by affirmatively requiring that the disclosure include a description of the investment adviser’s relationship with the solicitor, the details of any compensation arrangement, a description of any potential material conflicts of interest resulting from such relationships, and the amount of any additional cost to the client or private fund investor as a result of the solicitation.⁴⁷ However, the Proposed Solicitation Rule would not require the solicitor’s disclosure to be delivered in a written document.⁴⁸ NASAA views this as a negative change. Emails, text messages, instant messages, electronic presentations, videos, podcasts, and other modern methods of communications are commonly used for a variety of purposes. However, such communications do not adequately ensure that the investor will read, hear, or understand the importance of the disclosures. Furthermore, these and similar electronic communications are ill-suited to allowing the client to retain a copy of the disclosure in a form and location that can easily be recalled when necessary.

Accordingly, the Proposed Solicitation Rule should be revised to require that solicitors deliver the required disclosure to the client in a written document that the client can easily read and retain for their records.

b. The Proposed Solicitation Rule should not provide any *de minimis* exemption.

Rule 206(4)-3 currently requires an investment adviser to comply with certain conditions when paying a cash fee to a solicitor, but is silent as to other forms of compensation.⁴⁹ The

⁴⁵ 17 CFR § 275.206(4)-3(a)(2)(iii).

⁴⁶ Rule Proposal at 213.

⁴⁷ Proposed Rule 206(4)-3(a)(1)(iii).

⁴⁸ Compare 17 CFR § 275.206(4)-3(a)(2)(iii)(A) (requiring delivery of “a separate written disclosure document”) with Proposed Rule 206(4)-3(a)(1)(iii), Rule Proposal at 476 (requiring delivery of “a separate disclosure”); Rule Proposal at 361.

⁴⁹ 17 CFR 275.206(4)-3(a).

Commission correctly recognizes that non-cash compensation creates the same conflicts of interest as cash compensation.⁵⁰ Therefore, the Proposed Solicitation Rule appropriately extends the rule to include all forms of compensation, including directed brokerage business, sales awards and prizes, training or educational meetings, outings, tours, other forms of entertainment, and discounted advisory services.⁵¹ This expansion of the rule more closely reflects the economic realities of many common solicitor arrangements today.

Unfortunately, the Proposed Solicitation Rule also includes wholly new exemptions from the requirements of the rule. Under one such exemption, if an investment adviser pays a solicitor \$100 or less for solicitation services during the preceding twelve months, the investment adviser would not have to enter into a written agreement with the solicitor, exercise any oversight over the solicitor's activities, or conduct meaningful due diligence of the solicitor.⁵² Consequently, the solicitor would not be required to disclose any details about its relationship to the investment adviser or the compensation the solicitor would receive for the referral.

The Commission should not include a *de minimis* exemption in the final rule. Just as non-cash compensation creates the same conflicts of interest as cash compensation, small dollar value compensation creates conflicts between the solicitor and the investor being solicited. Further, even a solicitor who refers a large number of potential investors may receive "*de minimis*" compensation if those referrals are not ultimately successful. This would not mitigate the conflict arising from the solicitor's economic interest in steering the investor to the investment adviser. In fact, it may even exacerbate the impact of excluding such an arrangement from the disclosure requirements in the Proposed Solicitation Rule. At a minimum, this conflict should be disclosed to the investor being solicited.

3. Conclusion

NASAA generally supports the Commission's effort to modernize its investment adviser advertising rule to reflect modern methods of communication, investor expectations and industry practice. However, the Commission should tailor the requirements of the rule to the practical limitations of certain communications, rather than excluding those communications from oversight entirely, and should retain certain limited prohibitions from the current rule. NASAA generally supports the proposed expansion of the compensated solicitation rule, and encourages its adoption, with the revisions referenced above.

Thank you for considering these views. NASAA looks forward to continuing to work with

⁵⁰ Rule Proposal at 207.

⁵¹ Rule Proposal at 207.

⁵² See Proposed Rule 206(4)-3(b)(4).

Vanessa Countryman
February 10, 2020
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the Commission in the shared mission to protect investors. Should you have questions, please contact either the undersigned or NASAA's Executive Director, Joseph Brady, at 202-737-0900.

Sincerely,

A handwritten signature in black ink, appearing to read "C. Gerold". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Christopher Gerold
NASAA President
Chief, New Jersey Bureau of Securities