



NASAA

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NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

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By email to: [rule-comments@sec.gov](mailto:rule-comments@sec.gov)

J. Matthew DeLesDernier  
Assistant Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: **File No. SR-FINRA-2020-020: Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Adopt FINRA Rule 3241 (Registered Person Being Named a Customer's Beneficiary or Holding a Position of Trust for a Customer)**

Dear Mr. DeLesDernier:

On behalf of the North American Securities Administrators Association, Inc. ("NASAA"),<sup>1</sup> I am writing in response to U.S. Securities and Exchange Commission ("SEC" or the "Commission") Release No. 34-89218, *Notice of Filing of a Proposed Rule Change to Adopt FINRA Rule 3241 (Registered Person Being Named a Customer's Beneficiary or Holding a Position of Trust for a Customer)* ("Proposed Rule 3241" or the "Proposal").<sup>2</sup> The Proposal is of particular interest to NASAA and its members for its implications for investor protection, particularly for seniors and persons with diminished capacities.

NASAA commends the Commission and the Financial Industry Regulatory Authority, Inc. ("FINRA") for taking up this important topic. NASAA, FINRA and the SEC have worked collaboratively on senior investor protection issues and concerns in the past, and we look forward to doing so again here.<sup>3</sup> NASAA commented previously on Proposed Rule 3241 when it was

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<sup>1</sup> 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.

<sup>2</sup> The Proposal is available at <https://www.sec.gov/rules/sro/finra/2020/34-89218.pdf>.

<sup>3</sup> See Press Release: *SEC, NASAA, and FINRA Issue Senior Safe Act Fact Sheet to Help promote Greater Reporting of Suspected Senior Financial Exploitation*, FOR IMMEDIATE RELEASE 2019-75 (May 23, 2019) available at [https://www.sec.gov/news/press-release/2019-75#\\_ftnref1](https://www.sec.gov/news/press-release/2019-75#_ftnref1); Economic Growth, Regulatory Relief and Consumer Protection Act, Pub. L. 115-174 § 303 (2018); Commissioner Allison Herren Lee, *Remarks at the SEC Roundtable on Combating Elder Investor Fraud* (Oct. 3, 2019), available at <https://www.sec.gov/news/public-statement/lee-remarks-sec-roundtable-combating-elder-investor-fraud>.

introduced by FINRA.<sup>4</sup> We applaud FINRA for recognizing the need for controls in this area. However, FINRA’s decision not to accept certain of our positions warrants reconsideration of those issues by the Commission.

In brief, NASAA maintains that registered persons should be prohibited from being named as beneficiaries or appointed to positions of trust by any customers other than immediate family members. Further, even with respect to immediate family members, registered persons should be required to seek and obtain written authorization from their firms, who should be responsible for scrutinizing such arrangements. Should the Commission, however, decide to move forward with allowing such arrangements as proposed, it should nevertheless require FINRA to create clear standards by establishing a baseline of information that registered persons are required to provide, and more specific guidance on considerations for firm approval. Additionally, in those instances where firms authorize customer beneficiary or trust position arrangements, the accounts at issue should be subject to heightened supervision to ensure that any conditions and limitations are observed faithfully. Finally, firms should be required to apply the resulting rule – along with any account changes, lookback provisions, and further requirements as the Commission deems necessary – both to current and future customers.

**I. Customer Beneficiary and Trust Position Arrangements Should Be Limited to Immediate Family Members, and Those Arrangements Should Be Subject to Firm Scrutiny.**

Proposed Rule 3241 would require certain controls – namely, a requirement for registered persons to notify their firms of customer beneficiary and trust position arrangements, and requirements on firms to perform risk assessments, make reasonable risk determinations, set conditions or limitations, maintain written policies and procedures, and maintain related records – when a registered person is named as a customer’s beneficiary or is placed in a position of trust over a customer’s account. As proposed, however, these controls would not apply to arrangements that involve a registered person’s “immediate family,” which FINRA would define to include enumerated familial relationships and “any other person who resides in the same household as the registered person and the registered person financially supports, directly or indirectly, to a material extent.” NASAA appreciates FINRA’s decision to narrow the inclusion of financially-supported persons as “immediate family” to those who live in the same household as the registered person.

NASAA maintains that a registered person should simply be prohibited from being named to customer beneficiary and trust position arrangements, with a narrow exception for arrangements involving a registered person’s immediate family. As we explained in our comment letter in response to FINRA Regulatory Notice 19-36, the conflicts of interest that exist when a registered

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<sup>4</sup> See Regulatory Notice 19-36, *Registered Person Being Named a Customer’s Beneficiary or Holding a Position of Trust for a Customer*, (Nov. 11, 2019) available at <https://www.finra.org/rulesguidance/notices/19-36>; Letter from Chris Gerold, NASAA President, to Jennifer Piorko Michelle, FINRA Office of the Corporate Secretary, *Re: Regulatory Notice 19-36: Rule to Limit a Registered Person from Being Named a Customer’s Beneficiary or Holding a Position of Trust for a Customer* (Jan. 24, 2020), available at <https://www.nasaa.org/wp-content/uploads/2020/01/NASAA-Comment-Letter-re-Finra-Reg-Notice-19-36.pdf> (“NASAA 19-36 Comment Letter”).

person takes on a position of trust or is named a beneficiary cannot be mitigated by additional policies and procedures imposed by the registered person's firm. Moreover, Canadian self-regulatory organizations limit such arrangements to family members out of a recognition that they are personal financial dealings that create unacceptable conflicts of interest.<sup>5</sup>

NASAA's position is consistent with the Commission's approach to broker-dealer conflicts of interest. As the Commission recognizes in the context of Regulation Best Interest – where it has required the elimination of sales contests, sales quotas and certain compensation arrangements – some conflicts of interest are “so pervasive such that they cannot be reasonably mitigated and must be eliminated in their entirety, as we believe they create too strong of an incentive for the associated person to make a recommendation that places their financial and other interest ahead of the interest of retail customers' interests ....”<sup>6</sup> The direct personal incentives inherent in customer beneficiary and trust position arrangements are of equal if not greater concern. They should therefore be prohibited for the same reasons.

While FINRA recognizes these concerns, it nevertheless concludes that such arrangements should be permissible generally with some controls, and that no controls are necessary where immediate family members are involved. As FINRA reasons, “[t]he risk that a registered person misused his or her role in the broker-customer relationship to be named a beneficiary or hold a position of trust is reduced when the customer is an immediate family member.”<sup>7</sup> It is the unfortunate reality, however, that investors can be and are exploited by family members. As we noted in our previous comment letter, the National Council on Aging reports that in almost 60% of elder abuse and neglect incidents, the perpetrator is a family member, with two-thirds of the perpetrators being adult children or spouses.<sup>8</sup> Given the stakes at issue – namely the protection of seniors and persons of diminished capacity – it is not prudent to allow an exception to regulatory scrutiny based on assumptions about familial fidelity. For that reason, NASAA recommended that even customer beneficiary and trust position arrangements involving immediate family member should be subject to firm scrutiny and approval.

A straight forward prohibition on customer beneficiary and trust position arrangements, with an exception for immediate family members subject to additional firm scrutiny, is consistent with the Commission's approach to broker-dealer conflicts of interest generally, and the position

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<sup>5</sup> NASAA 19-36 Comment Letter at 2-3.

<sup>6</sup> SEC Release No. 34-86031, *Regulation Best Interest: The Broker-Dealer Standard of Conduct*, June 5, 2019, at 352-53.

<sup>7</sup> Proposal at 23.

<sup>8</sup> NASAA 19-36 Comment Letter at 4 (*citing* National Council on Aging, *Elder Abuse Facts*, (accessed 7/17/20), available at <https://www.ncoa.org/public-policy-action/elder-justice/elder-abuse-facts/>; see also Stephen Deane, SEC Office of the Investor Advocate, *Elder Financial Exploitation – Why it is a concern, what regulators are doing about it, and Looking Ahead*, (June 2018), available at <https://www.sec.gov/files/elder-financial-exploitation.pdf>, at 23 (*citing* MetLife Mature Market Inst. Et al, *The MetLife Study of Elder Financial Abuse: Crimes of Occasion, Desperation, and Predations Against America's Elders 5* (2011) (stating that data at that time showed that 55% of financial abuse in the United States is committed by family members, caregivers, and close friends).

of FINRA's fellow self-regulatory organizations. It also draws a clear line as to which conflicts of interest are safe to regulate, and which are too risky to allow. Barring an outright prohibition, NASAA nevertheless maintains that all such arrangements, even those involving immediate family members, should be subject to firm scrutiny to help ensure that registered persons are dissuaded from exploiting family members.

**II. Registered Persons Seeking Approval of Customer Beneficiary and Trust Position Arrangements Should Be Subject to Clear Disclosure Requirements, and Firms Approving Such Arrangements Should Be Required to Take Certain Specific Steps.**

Should the Commission approve FINRA's recommendation to allow customer beneficiary and trust position relationships beyond immediate family members, NASAA maintains the resulting rule should be revised to make clear what disclosures registered persons would be required to provide. As proposed, a firm is advised to consider eight non-exclusive factors to approve a position of trust or beneficiary designation.<sup>9</sup> Yet, firms are not required to take any particular consideration into account. The rule should require a minimum amount of disclosure and required evaluation, from which the firms can expand to a higher standard, to ensure adequate consideration among similar situations across similarly situated firms. As NASAA commented previously,<sup>10</sup> any registered person who seeks approval of a customer beneficiary or trust position arrangement should be required, at a minimum, to disclose:

- relevant information about the customer, including the length of time the registered person has known the customer;
- the nature of any special or familiar relationship between the registered person and the customer;
- the circumstances precipitating any appointment or designation, or any information that might make the customer vulnerable; and
- identification of the role(s) in which the registered person is being appointed.

Likewise, NASAA commented that firm reviews must, at a minimum, document:

- the steps that the member firm undertook to assess the risk prior to the registered person being approved;
- the steps that the member firm will take to minimize the conflict of interest;

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<sup>9</sup> Proposal at 8-9.

<sup>10</sup> NASAA 19-36 Comment Letter at 3-4.

- how the member firm communicated to the customer the risk created by the appointment so that the customer appreciates the risk; and
- an outline of the supervisory measures that will be taken by the member firm.

These measures should be required in addition to the non-exclusive list of potential factors suggested by FINRA. Requiring defined disclosures and assessment considerations would allow regulators to assess and compare approval and supervision practices across firms. Further, firms should be free to impose more stringent controls as they deem necessary up to and including a flat prohibition on such arrangements.<sup>11</sup>

As we expressed in our previous comments,<sup>12</sup> a reasonable assessment and determination process should also include an interview (preferably by a compliance officer in the firm) with the customer outside of the presence of the registered person. This practice would help ensure that the arrangement is well informed, has not been coerced, and does not show indicia of vulnerability or undue influence. Where it is not possible to interview the customer, the firm should at least be required to verify that the customer directed the appointment of his or her own volition and did not feel pressure to name the registered person a beneficiary or appoint the registered person to a position of trust.

### **III. All Firm-Approved Arrangements Should Be Subject to Heightened Supervision and Regular Review.**

Proposed Rule 3241 states that “[i]f the member imposes conditions or limitations on its approval of the person’s assuming such status or acting in such capacity, the member shall reasonably supervise the registered person’s compliance with such conditions or limitations.”<sup>13</sup> This language is too permissive. The Proposal presupposes that a firm could decide to impose no limitations or conditions. Further, general supervision is insufficient to address what should be regarded as concerning or problematic business practices and flagged for heightened supervision.<sup>14</sup> FINRA’s publications and continued work with high risk brokers and high risk firms also showcase the necessity of heightened supervision and increased scrutiny of arrangements with greater risk which require enhanced investor protection.<sup>15</sup> NASAA has stated previously that

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<sup>11</sup> *Id.* at 6.

<sup>12</sup> *Id.* at 5.

<sup>13</sup> Proposed Rule 3241(b)(3) (emphasis added).

<sup>14</sup> *See* FINRA Rule 3110.12 (Standards for Reasonable Review); FINRA Rule 3270.01 (Obligations of Member Receiving Notice).

<sup>15</sup> FINRA Reg. Notice 18-15, *Heightened Supervision - Guidance on Implementing Effective Heightened Supervisory Procedures for Associated Persons with a History of Past Misconduct*, (Apr. 30, 2018), available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-18-15\\_1.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-18-15_1.pdf); FINRA Reg. Notice 18-16, *High Risk Brokers - FINRA Requests Comment on FINRA Rule Amendments Relating to High-Risk Brokers and Firms that Employ Them*, (Apr. 30, 2018), available at <https://www.finra.org/sites/default/files/Regulatory-Notice-18-16.pdf>; Letter from Joseph Borg, NASAA President, to Jennifer Piorko Michelle, FINRA Office of the

heightened supervision plans are necessary and effective tools to root out misconduct in instances where unavoidable conflicts of interest exist.<sup>16</sup> Accounts with customer beneficiary and trust position arrangements, if authorized by a firm, create significantly enhanced incentives for misconduct by registered persons, and therefore should be subject to heightened supervision generally.

#### **IV. Firms Should Apply the Resulting Rule to All Current and Future Customers.**

In our comment letter on FINRA's Regulatory Notice 19-36, we stated that member firms should advise customers of the restrictions applicable to naming a registered person, an immediate family member of a registered person, or an entity controlled by a registered person, as a beneficiary or to a position of trust in the account application process. FINRA asserts in the Proposal that a conversation or any other communication could also be effective to inform customers of potential conflicts of interest, restrictions from Proposed Rule 3241, or restrictions imposed by the firm's procedures. We disagree and maintain that customers should be advised in writing of the conflicts that arise when they seek to appoint a registered person to a position of trust or name her or him as a beneficiary, and the requirements of the rule as approved by the Commission. The effective date of this rule is the appropriate time to require firms to notify current account holders of the requirements of the new rule, and to implement procedures established by the rule to all applicable arrangements.

NASAA understands the argument that applying this rule to pre-existing beneficiary designations or positions of trust may constitute a significant undertaking. However, the cost associated with communicating this information, and applying the new rule retroactively, could provide benefits to investors by identifying potential ongoing abuses.

Finally, the customer definition must be readdressed. The Proposed Rule provides a six-month look-back period for determining whether an individual was a registered person's "customer" for purposes of trustee or beneficiary designations.<sup>17</sup> NASAA commented that a 12-month look-back provision is more appropriate to prevent circumvention of the restrictions.<sup>18</sup> FINRA responds that a "six-month period strikes an appropriate balance between achieving the regulatory objective of addressing circumvention ... and imposing reasonable requirements on

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Corporate Secretary, *Re: Regulatory Notice 18-16: High Risk Brokers* (Aug. 1, 2018), available at <https://www.nasaa.org/wp-content/uploads/2011/07/NASAA-18-16-Comment-Letter-1.pdf>; FINRA Reg. Notice 19-17, *Protecting Investors from Misconduct*, (May 2, 2019), available at <https://www.finra.org/sites/default/files/2019-05/Regulatory-Notice-19-17.pdf>; Letter from Michael Pieciak, NASAA President, to Jennifer Piorko Michelle, FINRA Office of the Corporate Secretary, *Re: Regulatory Notice 18-16: Protecting Investors from Misconduct* (July 1, 2019), available at <https://www.nasaa.org/wp-content/uploads/2019/07/NASAA-Reg.-Notice-19-17-Comment-Letter-7-1-19.pdf>.

<sup>16</sup> See NASAA Broker Dealer Section, *Coordinated Exam Report*, (September 2018), at 8, available at <https://www.nasaa.org/wp-content/uploads/2018/09/BD-Coordinated-Examination-Report-2018.pdf>; see also Proposal at 3-4 (FINRA's steps to address misconduct in this area creating a quasi-heightened supervision).

<sup>17</sup> Proposal at 15-16.

<sup>18</sup> NASAA 19-36 Comment Letter at 7.

member firms tracking of account transfers.<sup>19</sup> Unfortunately, the appearance is that FINRA is more concerned with the burden on its members than the benefits to investors. A 12-month period would significantly curtail attempts to circumvent the purpose of Proposed Rule 3241 and would inure to the benefit of investors. When accounting for the books and records requirements for much of the same data, which can run from three to six years, NASAA does not believe that a 12-month look-back period is overly burdensome.<sup>20</sup>

## V. Conclusion

NASAA supports the work of the Commission and FINRA in protecting senior investors and appreciates the opportunity to comment on the Proposal. In summary, NASAA believes that registered persons should be prohibited from being named as beneficiaries or appointed to positions of trust by any customers other than immediate family members. Even with immediate family members, registered persons should be required to obtain written approval from their firms, and firms should be responsible for scrutinizing such arrangements. Should the Commission, however, decide to move forward with allowing such arrangements as proposed, it should nevertheless require FINRA to establish clear standards for firms by laying a foundation for the information that registered persons must provide and more specific guidelines on considerations for firm approval. In addition, where firms approve beneficiary designations or trust position arrangements, the accounts in question should be subject to heightened supervision to ensure that the conditions and restrictions are met. Finally, the resulting final rule should be applied to both current and future customers.

Thank you for considering these views. NASAA looks forward to continuing to work with FINRA and the Commission in the shared mission to protect investors. Should you have questions, please contact either the undersigned or NASAA's General Counsel, Vince Martinez, at (202) 737-0900.

Sincerely,



Christopher Gerold  
NASAA President  
Chief, New Jersey Bureau of Securities

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<sup>19</sup> Proposal at 27.

<sup>20</sup> See 17 CFR § 240.17a-3(a)(17)-(18); FINRA, Books and Records Guidance, <https://www.finra.org/rules-guidance/key-topics/books-records>; FINRA, Books and Records Checklist, <https://www.finra.org/compliance-tools/books-and-records-checklist>.