

Via electronic submission to NASAAComments@nasaa.org, kopletona@dca.njoag.gov, and stephen.bouchard@dc.gov

December 4, 2023

NASAA Broker-Dealer Market and Regulatory Policy and Review Project Group
Amy Kopleton, Project Group Chair

NASAA Broker-Dealer Section Committee
Stephen Bouchard, Section Chair

c/o North American Securities Administrators Association, Inc.
750 First Street, N.E., Suite 1140
Washington, D.C. 20002

Re: Proposed Revisions to NASAA's Model Rule on Dishonest or Unethical Business Practices of Broker-Dealers and Agents (the "Proposal")

Dear Project Group and Section Members, Ms. Kopleton and Mr. Bouchard:

Ares Wealth Management Solutions, LLC ("AWMS") respectfully submits the following comments on the Proposal. AWMS is part of Ares Management Corporation (NYSE: ARES), a leading global alternative investment manager offering clients complementary primary and secondary investment solutions across the credit, private equity, real estate, and infrastructure asset classes. We seek to provide flexible capital to support businesses and create value for our stakeholders and within our communities. By collaborating across our investment groups, we aim to generate consistent and attractive investment returns throughout market cycles. As of September 30, 2023, Ares Management Corporation's global platform had approximately \$395 billion of assets under management, with over 2,800 employees operating across North America, Europe, Asia Pacific, and the Middle East. For more information, please visit www.aresmgmt.com.

Ares is a member of The Institute for Portfolio Alternatives which is contemporaneously submitting a comment letter and the substance of that letter is incorporated herein. We would like to emphasize the following concerns with the Proposal from the perspective of a sponsor who employs hundreds of employees in an industry that has undergone a fundamental transformation in the last decade and now is represented by the largest alternative asset managers raising and deploying meaningful capital into the U.S. economy.

- ❖ **The Proposal creates a confusing patchwork of additional regulatory burdens for broker-dealers, who are already subject to federal regulation, including Regulation Best Interest.** The Proposal indicates that NASAA desires to incorporate the definitions and SEC interpretations regarding Regulation Best Interest ("Reg. BI") into NASAA's model rule, however, the Proposal imposes heightened and more restrictive burdens on broker-dealers than those imposed by Reg. BI, noting that NASAA has drafted its own definitions and

interpretations to “fill certain gaps in SEC guidance.” Further, the Proposal indicates that states may adopt some or all of the subparts of the proposed revisions to the model rule, which will result in a standard that may vary from state to state. The Proposal will create significant complexity and confusion as broker-dealers will have to pivot from their current compliance programs that have been developed to comply with the uniform Reg. BI standards and will be required to develop and refine compliance programs that must also take into account the varying compliance requirements of each state and U.S. territory where they participate in the distribution of securities.

- ❖ **The Proposal conflicts with Reg. BI by overemphasizing the importance of cost and risk as paramount above other relevant factors to be considered in making an investment recommendation.** Similar to Reg. BI, the Proposal indicates that a broker-dealer should consider all of the relevant facts and circumstances to ensure that a recommendation is in the “best interest of a retail customer.” However, the Proposal indicates that to satisfy this obligation, a broker-dealer must make a reasonable inquiry regarding “lower-cost and lower-risk securities and investment strategies that are reasonably available to the broker-dealer.” The Proposal acknowledges that this is a “simplified form” of “the SEC’s *lengthy guidance* directing firms to consider lower-cost and lower-risk securities and strategies which they consider reasonably available alternatives.” By simplifying the nuanced analysis that SEC guidance has indicated is required under Reg. BI, the Proposal would result in a conflict with Reg. BI. Due to the Proposal’s emphasis on risk and cost as the most important factors to consider when satisfying the broker-dealer’s duty of care in making a recommendation, and the lack of any discussion of the benefits of the investment to be considered when making a recommendation, broker-dealers may determine that the most conservative approach to complying with state regulatory requirements would be to develop compliance programs that emphasize risk and cost as the primary relevant factors to consider when making a recommendation, while ignoring or minimizing the impact of the other relevant factors that are to be taken into consideration under Reg. BI, such as the potential benefits of the investment, investment objectives, investment experience, and financial situation. While such a limited analysis may minimize the risk that the broker-dealer would be in non-compliance with the requirements outlined in the Proposal, it would not be in the best interests of an investor.

- ❖ **Rather than incorporating SEC guidance concerning the meaning of the terms “recommendation” and “retail customer” for purposes of Reg. BI, the Proposal definitively defines those terms in a manner that is inconsistent with SEC guidance, which will create undue confusion and complexity for broker-dealer compliance programs.** Under the Proposal, the definition of “recommendation” includes “any means, method or mechanism to feature or promote an account type, specific security or investment strategy to a retail customer, whether directly or through a third party.” This would be a departure from SEC guidance regarding the meaning of recommendation, which the SEC has said “is not

susceptible to a bright line definition.”¹ The definition of recommendation in the Proposal would mean that items such as a public-facing website, newspaper advertisement, or educational seminar about a multitude of different investment strategies would be considered a “recommendation” to any retail investor who had viewed the item. Similarly, the Proposal defines “retail customer” in a manner that is not consistent with Reg. BI.² The Proposal expands the definition of “retail customer” to include virtually all “current and prospective customers and clients,” excluding certain institutional investors and “institutional buyers,” which is a term that may be defined differently on a state-by-state basis, creating additional confusion. Based on the definitions of “recommendation” and “retail customer” under the Proposal, any natural person who reads a broker-dealer’s advertisement, attends its educational webinar about investment strategies, or otherwise receives anything that “features or promotes” an account type, specific security, or investment strategy, whether directly or through a third party, would be a retail customer of the broker-dealer and the broker-dealer would be required to act “in the best interest” of that person. The expansion of the meanings of these terms will create significant compliance burdens and uncertainty for broker-dealers.

- ❖ **The Proposal would effectively prohibit many forms of compensation that are permitted to be paid to broker-dealers and registered investment advisers under SEC and FINRA rules.** The Proposal indicates that a broker-dealer will be “presumed to have placed its financial interest ahead of the interest of the retail customer” where the broker-dealer accepts compensation other than sales commissions and trail fees. The Proposal claims that other forms of compensation are not prohibited, but by imposing this presumption that the broker-dealer must affirmatively rebut, it will effectively ban all other forms of compensation, as broker-dealers are not likely to engage in activities that are automatically presumed to violate the model rule. This will result in broker-dealers being prohibited from receiving forms of compensation permitted under Reg. BI and other SEC and FINRA rules, and will effectively prohibit forms of compensation that registered investment advisers, including those regulated by the states, are permitted to receive. For decades, broker-dealers have been permitted to receive other forms of

¹ In Regulation Best Interest – A Small Entity Compliance Guide (www.sec.gov/info/smallbus/secg/regulation-best-interest#_edn1), the SEC stated the following with respect to the meaning of “recommendation” for purposes of Reg. BI:

The determination of whether a broker-dealer has made a recommendation that triggers application of Regulation Best Interest turns on the facts and circumstances of a particular situation, and therefore, whether a recommendation has been made is not susceptible to a bright line definition. Factors considered in determining whether a recommendation has taken place include whether the communication “reasonably could be viewed as a ‘call to action’” and “reasonably would influence an investor to trade a particular security or group of securities.” The more individually tailored the communication to a specific customer or targeted group of customers about a security or group of securities, the greater the likelihood that the communication may be viewed as a “recommendation.”

² Reg. BI defines “retail customer” as a natural 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; and
- uses the recommendation primarily for personal, family, or household purposes.

compensation, including items such as nominal gifts, other non-cash compensation items and reimbursements of expenses to attend educational seminars, but the Proposal would upend the established broker-dealer business model in a manner that far exceeds the requirements of Reg. BI. This may result in firms eliminating broker-dealer services from their platforms, forcing investors to choose between moving to fee-based advisory accounts or internet-based, execution-only platforms, diminishing investor options.

- ❖ **The Proposal suggests that conflicts of interest should be “neutralized” which may have a detrimental effect on investor choice.** Similar to Reg. BI, the Proposal indicates that broker-dealers must avoid and mitigate conflicts of interest. However, the Proposal imposes a far more limiting definition of conflict mitigation, indicating that mitigating a conflict means “neutralizing or reducing the potential for harm or adverse impact of the conflict to the retail customer.” The term “neutralize” is not defined in the Proposal, and we fear that it may serve to severely limit investor choice, as broker-dealers may not recommend investments that are otherwise suitable for a particular investor based on the investor’s objectives, strategy and financial situation, simply because the investment is subject to a higher front-end load than another, less suitable investment for the investor.

[signature page follows]

December 4, 2023

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Sincerely,

ARES WEALTH MANAGEMENT SOLUTIONS, LLC

By *Casey Galligan*

Casey Galligan

Co-Chief Executive Officer

With copies to:

Ms. Clothilde V. Hewlett
Commissioner
One Sansome Street, Suite 600
San Francisco, CA 94104
(415) 972-8540
clothilde.hewlett@dbo.ca.gov

Ms. Tung Chan
Securities Commissioner
1560 Broadway
Suite 900
Denver, CO 80202
(303) 894-2320
tung.chan@state.co.us

Ms. Shamiso Maswoswe
Chief, Investor Protection Bureau
28 Liberty Street
15th Floor
New York, NY 10005
(212) 416-8222
Shamiso.Maswoswe@ag.ny.gov