Robinhood

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**December 4, 2023**

Via Electronic Mail (NASAAComments@nasaa.org)

North American Securities Administrators Association, Inc.
750 First Street, NE, Suite 990
Washington, DC 20002

**Re: Proposed Revisions to NASAA's Dishonest or Unethical Business Practices Of Broker-Dealers And Agents Model Rule**

Dear North American Securities Administrators Association, Inc. ("NASAA"):

Robinhood Financial LLC[1] ("Robinhood") submits this letter in response to the request for comment published by the Broker-Dealer Market and Regulatory Policy and Review Project Group and the Broker-Dealer Section Committee of NASAA relating to proposed revisions to NASAA's model rule on *Dishonest or Unethical Business Practices Of Broker-Dealers And Agents* (the "Proposal").[2]

Robinhood's mission is to democratize finance for all, regardless of a customer's background, income, or wealth. There is a large investment and wealth gap in the United States, which has created a divide in our country between the "haves" and the "have nots." Robinhood was founded to close this gap with its accessible product offering and user-friendly mobile application, which rely on technology to remove traditional barriers to investing and empower investors so that they can take control of their financial futures.

Using technology to open the markets to retail investors from all backgrounds is central to our mission. Through our mobile app and website, Robinhood demystifies investing by providing free educational resources, financial literature, and user-directed subscriptions to news updates and information regarding securities in investors' portfolios. Because customers have 24/7 access to these tools and information, they have the freedom to consider and make decisions on their own schedule and time frame in a manner that they believe is right for them. In addition, Robinhood makes trading more accessible by eliminating account minimums and trading commissions, offering investors IPO access, fractional trading, and the first

[1] Robinhood Financial LLC, a FINRA-member broker-dealer, is a wholly owned subsidiary of Robinhood Markets, Inc.

[2] NASAA, Request for Public Comment, *Proposed Revisions to NASAA's Dishonest or Unethical Business Practices Of Broker-Dealers And Agents Model Rule* (Sept. 5, 2023), https://www.nasaa.org/wp-content/uploads/2023/09/Request-for-Public-Comment-on-BD-Best-Interest-Model-Rule.pdf ("Request for Comment").

IRA with a match, no employer necessary, and providing access to free educational resources, such as Robinhood Learn. Using our mobile app, our customers can engage with their investments and access capital markets as they plan for their financial well-being and their futures. This type of engagement is beneficial for investors; the more retail customers are involved in their finances, paying attention to their assets, and learning about investing, the better equipped they are to achieve their financial goals.

But the Proposal would impose impossible compliance burdens on any broker-dealer that makes a "recommendation," as proposed in subpart 1d(5), by using "any means, method or mechanism to feature or promote an account type, specific security, or investment strategy to a retail customer." Although the Proposal purports to reflect updates consistent with the U.S. Securities and Exchange Commission's ("SEC") 2019 adoption of Regulation Best Interest ("Reg BI"),[3] the Proposal's redefinition of "recommendation" would significantly broaden the definition in a way that would conflict with Reg BI as well as existing SEC and FINRA guidance, rendering federally applicable interpretations almost meaningless. Without any evidence or reasonable explanation supporting a reversal of decades of settled securities law, the Proposal would impose an impossible standard on any broker-dealer that proactively provides information to retail investors and by doing so would restrict retail investors' access to products, services, and tools that help retail investors take control of their financial futures. This is a terrible outcome for retail investors and directly contradicts the SEC's intentions when it enacted Reg BI and stated that "[Reg BI] should not stifle investment education as a means to encourage financial wellness."[4]

As a result, Robinhood believes that the Proposal should be withdrawn.

## I. The Proposal's Redefinition of "Recommendation" Conflicts with Reg BI and Existing SEC and FINRA Interpretations.

Although the Proposal purports not to apply to "unsolicited transactions that a broker-dealer or agent execute for a customer in a self-directed or nondiscretionary account," the Proposal would drive a gaping hole through this exception by redefining when a transaction involves a "recommendation" in proposed subpart 1d(5) to include:

> If the broker-dealer or agent utilized **any means, method or mechanism to feature or promote** an account type, specific

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[3] Request for Comment at 1 ("[T]he Committees propose that NASAA amend the Business Practices Rule to: (1) acknowledge and incorporate by reference the new federal conduct standard applicable to broker-dealer and agents pursuant to Reg BI….").

[4] Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 Fed. Reg. 33318, 33338 (July 12, 2019).

> security or investment strategy to a retail customer, whether directly or through a third-party, then that transaction will not be deemed an unsolicited transaction, but rather will be deemed a recommendation to which all of the foregoing obligations set forth in this subsection apply. (emphasis added).[5]

NASAA's *"*any means, method or mechanism to feature or promote" language is exceedingly broad and could capture nearly any communication, information, or graphic provided to a retail investor—such as in-app messages, e-mails, educational websites and help centers, newspaper ads and television commercials—including in the context of self-directed and nondiscretionary accounts. This broad language would render the carve-out for self-directed or nondiscretionary accounts almost meaningless, and it would apply a best interest standard to a large swathe of potential customer interactions that were not intended to be captured by Reg BI or FINRA's suitability rule governing investment recommendations. Although NASAA claims that its Proposal is intended to be "consistent with Reg BI," proposed subpart 1d(5) is wholly inconsistent with how the SEC and FINRA have defined "recommendation" for decades.[6]

A long history of SEC and FINRA guidance establishes how to determine whether a communication constitutes a "recommendation."[7] Under existing guidance, whether a "recommendation" occurs is not susceptible to a bright line definition and instead turns on the facts and circumstances of the particular situation. 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." Determining whether a communication constitutes a "call to action" requires case-by-case analysis of "the content, context, and presentation of the particular communication or set of communications" and "examination of the underlying

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[5] Request for Comment at 6-7.

[6] NASAA, Press Release, *NASAA Publishes Regulation Best Interest Examination Initiative Update and Issues Proposed Revisions to Its Broker-Dealer Conduct Model Rule* (Sept. 5, 2023), https://www.nasaa.org/69493/nasaa-publishes-regulation-best-interest-examination-initiative-update-and-issues-proposed-revisions-to-its-broker-dealer-conduct-model-rule/.

[7] *See, e.g.*, Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 Fed Reg. 33318 (July 12, 2019); NASD, Notice to Members 01-23, Suitability Rule And Online Communications (Mar. 18, 2001), https://www.finra.org/rules-guidance/notices/01-23; Notice of Filing Proposed Rule Change to Adopt FINRA Rule 2090 (Know Your Customer) and FINRA Rule 2111 (Suitability) in the Consolidated FINRA Rulebook, 75 Fed. Reg. 51310 (Aug. 19, 2010), as amended, 75 Fed. Reg. 52562 (Aug. 26, 2010) (discussing what it means to make a "recommendation").

substantive information transmitted to the customer and consideration of any other facts and circumstances, such as any accompanying explanatory message."[8]

For over twenty years, the industry has relied on well-established guidance that investor education tools provided to retail investors are not recommendations even when they provide information about a specific security, account type or strategy.[9] As technology has revolutionized the way retail investors receive information about their finances, broker-dealers have relied on regulatory guidance that makes clear that they are not making recommendations when they provide tools that investors want, such as (1) websites with research pages or "electronic libraries" providing research reports, news, quotes and charts that customers can obtain or request; (2) search engines that enable customers to sort through data about the performance of a broad range of securities, company fundamentals, and industry sectors; (3) research tools that allow customers to screen through a wide universe of securities and request lists of securities that meet broad, objective criteria; or (4) e-mail subscriptions so that customers can elect to receive alerts about news affecting the securities in their portfolios or on their "watch lists."[10]

Critically, and in contrast to NASAA's proposed definition, not all communications that "feature or promote an account type, specific security or investment strategy" are "recommendations." For example, there is ample guidance on types of general advertising and marketing that does not constitute a "recommendation."[11] Instead,

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[8] NASD, Notice to Members 01-23, Suitability Rule And Online Communications (Mar. 18, 2001).

[9] *See id*.

[10] *See* FINRA, *FINRA Rule 2111 (Suitability) FAQ*, https://www.finra.org/rules-guidance/key-topics/suitability/faq; *see also* NASD, Notice to Members 01-23, Suitability Rule And Online Communications (Mar. 18, 2001).

[11] *See, e.g.*, Rules Regarding Conduct, Supervision and Records of Brokers and Dealers Not Members of National Securities Association, 32 Fed. Reg. 11637, 11638 (Aug. 11, 1967) (noting that the SEC's now-rescinded suitability rule would not apply to "general distribution of a market letter, research report or other similar material"); Suitability Requirements for Transactions in Certain Securities, 54 Fed. Reg. 6693, 6696 (Feb. 14, 1989) (stating that proposed Exchange Act Rule 15c2-6, which would have required documented suitability determinations for speculative securities, "would not apply to general advertisements not involving a direct recommendation to the individual"); *DBCC v. Kunz*, No. C3A960029, 1999 NASD Discip. LEXIS 20, at *63 (NAC July 7, 1999) (stating that, under the facts of the case, the mere distribution of offering material, without more, did not constitute a recommendation triggering application of the suitability rule), *aff'd*, 55 S.E.C. 551, 2002 SEC LEXIS 104 (2002); FINRA Interpretive Letter to Name Not Public, *Re: NASD Notice to Members 96-60* (Mar. 4, 1997) ("[T]he staff agrees that a reference to an investment company or an offer of investment company shares in an advertisement or piece of sales literature would not by itself constitute a 'recommendation' for purposes of [the suitability rule].").

only those communications that are individually tailored to a specific customer or a targeted group of customers are more likely to be viewed as a "recommendation."[12]

As a result, communications that would *not* meet the well-established definition of "recommendation" under Reg BI but could fall under NASAA's overly broad definition include:

- A broker-dealer's distribution of marketing materials to retail investors using any media, including newspaper and magazine advertisements, physical mail, radio or television advertising, or any "digital engagement" with customers;
- Websites or app screens that are available to customers or a group of customers with information about specific securities; and
- A broker-dealer's distribution of communications to customers who have identified what information they want and elected to receive communications of interest to them.

Not only is NASAA's proposed definition inconsistent with well-established securities laws, but also it is wholly unnecessary and inappropriate to apply a best interest standard to interactions with retail investors that do not meet the existing SEC and FINRA interpretation of the term "recommendation." Reg BI and FINRA's suitability rule were adopted to, among other things, ensure that broker-dealers reasonably consider an individual customer's investment objectives and whether a particular investment is in a specific customer's best interest when making a recommendation to that customer. Other scenarios, such as purely self-directed or nondiscretionary accounts, do not implicate the same concerns precisely because there is no reasonable expectation by the customer that the broker-dealer is making a recommendation, let alone one that is individually tailored to that customer.

NASAA has not substantiated any reasonable basis for redefining "recommendation." Nor has it identified any customer harm that would warrant imposing a best interest standard on communications that, today, are not considered "recommendations." Yet, all the same, NASAA would impose this higher, one-size-fits-all standard of conduct on interactions that do not involve commensurate risks, contradicting the long-understood definition of "recommendation" under SEC and FINRA guidance as well as the intent of the SEC and FINRA in adopting Reg BI and the suitability rule. The Proposal uses technology as a boogeyman to justify its significant and unsupported departure from existing law and practice.

NASAA cites an SEC request for comment about so-called "digital engagement practices" from more than two years ago as justification for expanding the scope of

[12] *See id.*

its best interest standard to an almost endless array of customer communications.[13] Even if the SEC had announced that it would expand the scope of Reg BI to so-called digital engagement practices—which it has not—the Proposal is inconsistent with and goes beyond the SEC's request for comment, which interprets the term "recommendation" as "consistent with precedent under the federal securities laws and how the term has been applied under FINRA rules."[14] We agree that certain digital communications with customers may constitute a recommendation under the right circumstances; however, the Proposal's redefinition of "recommendation" would be inconsistent with well-established securities laws and would be wholly impractical because it would, without any cognizable limiting principle, encompass virtually any type, form, or level of engagement between a broker-dealer and its retail customer, regardless of whether such communication constitutes a recommendation under the existing SEC and FINRA guidance.

There are already ways to distinguish communications that are recommendations from communications that aren't recommendations—even where a firm uses technology to communicate with customers through digital media. For example, Robinhood makes recommendations to customers in compliance with Reg BI in connection with its "first trade" recommendations and IRA portfolio recommendations. To do so, it collects information about the customer's investing needs and assesses them using an algorithm that has been carefully reviewed by investment professionals and third-party experts, with the goal of recommending a portfolio that seeks to optimize expected returns while taking on an amount of risk that makes sense for the investor. This individualized "call to action" falls squarely within the well-established definition of a recommendation and is supervised and regulated according to the requirements and safeguards of Reg BI. In contrast, NASAA would treat as a recommendation any mass e-mail to customers announcing a new account type (such as retirement accounts), any subway poster highlighting a new offering that could be construed as a "strategy" (such as options), and any website page that provides information about a specific security. There is no need to broadly paint all digital communications with customers as recommendations; NASAA's approach would be arbitrary and capricious.

[13] *See* Request for Comment at 7 n.14. *See also* Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology To Develop and Provide Investment Advice, 86 Fed. Reg. 49067, 49075 (Sept. 9, 2021) ("DEP Request") ("The use of a [digital engagement practice] by a broker-dealer may, depending on the relevant facts and circumstances, constitute a recommendation for purposes of Reg BI.").

[14] *Id*.

## II. The Proposal Unjustly Targets Self-Directed Online Brokerages and Their Customers.

The Proposal's arbitrarily overbroad scope appears to target the self-directed brokerage business model, which generally operates in an online environment and provides certain resources and services to customers that are specifically designed not to generate investment recommendations subject to Reg BI. Businesses like Robinhood that follow this model intentionally avoid the potential conflicts of interest and attendant compliance costs that come with investment recommendations and reserve making recommendations for specific products and services where recommendations and Reg BI compliance are contemplated. Offering recommendations requires investment in extensive compliance infrastructure and resources. By avoiding the significant costs associated with more extensive compliance efforts, self-directed brokerages are able to offer their clients access to information and the markets at lower cost. These businesses were built in reliance on existing SEC and FINRA guidance that indicates what is (or is not) a recommendation triggering certain compliance obligations and costs.

The Proposal would upset the settled expectations of market participants by putting into scope numerous additional touchpoints for customer engagement, creating significant new compliance burdens for broker-dealers, and imposing costs on both firms and their customers. Customers of a self-directed online brokerage have self-selected into that model for the benefits they receive as a result (e.g., lower costs, autonomy, accessible online user interfaces with free educational and informational materials). By increasing the cost of compliance, the Proposal could reduce or eliminate the benefits self-directed investors receive from their brokerage.

NASAA unjustly targets self-directed online brokerage, which is designed to empower retail investors to make their own financial decisions, with unsupported claims that so-called digital engagement practices "feed on and cater to the unique personal attributes of individual retail investors, especially vulnerable unsophisticated investors."[15] The insinuation that brokers use so-called digital engagement practices to prey on their customers is offensive and completely unsupported. Moreover, many retail investors either cannot afford or do not want to rely on full-service brokers or investment advisers; attacking the new model of self-directed brokerage would disproportionately harm these investors.

Robinhood has attached as Exhibit A and incorporates by reference its comment letter in response to the SEC's DEP Request.[16] Among other things, this letter

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[15] Request for Comment at 7.

[16] Letter from David Dusseault, President, Robinhood Financial LLC, to Vanessa A. Countryman, Secretary, SEC, *Re: Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Advisor Use of Technology*

describes how Robinhood uses digital communications, why customers demand and rely on the information that Robinhood provides, and why Robinhood's digital communications with its customers do not involve recommendations. The Proposal implicates many of the same concerns about regulating digital communications as the DEP Request. For many of the same reasons articulated in that letter, there are fundamental problems with treating common digital communications as if they were investment recommendations. The end result of doing so stands only to harm investors by making their investing experience less accessible.

## III. The Proposal Would Restrict Investor Choices and Harm Investor Outcomes.

Rather than advancing the goal of customer protection, the likely effect of applying the Proposal's best interest standard to customer interactions that do not involve investment recommendations would be to limit customer education and access to information about a broker's account types, products, and services. Ultimately, this would harm investors by limiting the tools and information that they can use to their benefit and by depriving investors of autonomy to decide how they want to handle their finances.

For example, in situations where a broker may offer different investment strategies or managed account offerings, the broker would need to decide whether to: (i) conduct a best interest analysis for each customer prior to presenting the available options (which is likely impossible to operationalize at scale and would severely complicate how customers seek and firms provide information about products and services), or (ii) restrict or remove the information it provides. Given these options, we believe that investors ultimately will be restricted or walled off entirely from information that could be helpful to them. At worst, investors will lose access to free educational resources that currently help them navigate investing and learn about the products and services they might use to improve their financial future; at best, financial institutions will restrict the information they make available to investors, limiting communications to only the most high-level, non-specific materials.

Alternatively, to the extent broker-dealers attempt to comply with the best interest standard whenever providing a communication that "features or promotes" an account type, specific security or investment strategy, such efforts would introduce extensive costs that would be borne by investors, eliminating the benefits they receive from selecting a self-directed online brokerage. For example, brokers may need to charge fees or commissions to recoup the costs of trying to comply with the best interest standard as applied to any customer communication–to the extent it would even be possible to comply—and these added costs could discourage some

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*to Develop and Provide Investment Advice, Rel. Nos. 34-92766; IA-5833; File No. S7-10-21* (Oct. 1, 2021), https://www.sec.gov/comments/s7-10-21/s71021-9316498-260092.pdf.

investors from using certain products or services that now cost more or from participating in the financial markets altogether. Either outcome would be harmful to investors and would remove options that investors otherwise have today.

Robinhood attaches as Exhibit B and incorporates by reference its comment letter in response to the SEC's proposed rule relating to Conflicts of Interest Associated with the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers ("PDA Proposal").[17] This letter describes the benefits that technology provides to retail customers by informing and educating them to allow them to take control of their financial futures and make more informed investment decisions at a lower cost and also describes the difficulties and costs of applying what is essentially a best interest standard to the use of technology. NASAA's Proposal implicates many of the same concerns as the SEC's PDA Proposal because it treats technology in the same Luddite fashion and would likely result in the same negative consequences. Like the PDA Proposal, NASAA's Proposal is a solution in search of a problem; NASAA has provided no evidence that retail investors are harmed in any way by having access to an online user interface in a self-directed brokerage model. Removing or restricting that access would only deprive investors of important and useful information and tools—in other words, the Proposal would harm the very investors it seeks to protect.

* * *

Robinhood appreciates the opportunity to comment on the Proposal. Without proper justification, the Proposal would redefine "recommendation" to establish an overly broad framework that differs from and conflicts with the scope of the SEC's and FINRA's existing framework governing recommendations. This standard would apply even to scenarios that the SEC and FINRA have long recognized do not share the same risks of potential conflicts of interest or individually tailored communications associated with investment recommendations. The Proposal unjustly targets self-directed online brokerage services that empower retail investors who might otherwise be unable to access investment opportunities to make their own financial decisions. And, in the name of customer protection, the Proposal would raise investors' costs and restrict retail investor access to important information, tools, products, and services that they want and that can help them make more informed financial decisions. As a result, the Proposal would harm investor outcomes

[17] *See* Letter from Daniel M. Gallagher, Chief Legal and Corporate Affairs Officer, Robinhood Markets, Inc., to Vanessa A. Countryman, Secretary, SEC, *Re: File No. S7-12-23: Conflicts of Interest Associated with the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers* (Oct. 10, 2023), https://www.sec.gov/comments/s7-12-23/s71223-271299-654022.pdf; *see also* Conflicts of Interest Associated With the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers, 88 Fed. Reg. 53960 (Aug. 9, 2023).

without providing any clear benefits. For all these reasons, NASAA should withdraw the Proposal.

Please contact the undersigned at lucas.moskowitz@robinhood.com if you have any questions or comments.

Sincerely,

DocuSigned by:
Lucas Moskowitz
C75CC4056FD04A4...

Lucas Moskowitz
Deputy General Counsel
Robinhood Markets, Inc.

cc: Amy Kopleton, Chair, Broker-Dealer Market and Regulatory Policy and Review Project Group (kopletona@dca.njoag.gov)

James Nix, Chair, Broker-Dealer Section (jnix@ilsos.gov)

# Exhibit A

Robinhood

85 Willow Road
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October 1, 2021

**VIA ELECTRONIC SUBMISSION**

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

**Re:** ***Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Advisor Use of Technology to Develop and Provide Investment Advice, Rel. Nos. 34-92766; IA-5833; File No. S7-10-21***

Dear Ms. Countryman,

Robinhood Financial, LLC ("Robinhood" or "the Firm")[1] submits this letter in response to the U.S. Securities and Exchange Commission ("Commission" or "SEC") request for information and public comment on customer engagement practices by broker-dealers and registered investment advisers through digital "platforms" such as websites and mobile applications (the "Request"), what the SEC has termed "digital engagement practices" (or "DEPs").[2] Robinhood appreciates the opportunity to provide comments. Due to the brevity of the comment period, Robinhood may seek to supplement its comments, and if it does, the Firm respectfully requests that the Commission take such comments into consideration.

Robinhood's mission is to democratize finance for all, regardless of a customer's background, income, or wealth. There is a large investment and wealth gap in the United States, which has created a divide in our country between the "haves" and the "have nots."[3] Robinhood has helped close this gap

[1] Robinhood is a wholly-owned subsidiary of Robinhood Markets, Inc. ("Robinhood Markets").

[2] *Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology To Develop and Provide Investment Advice*, 86 Fed. Reg. 49,067 (Sept. 1, 2021). By using the term "digital engagement practices," we do not agree with any characterization that customer engagement is new or problematic when it is technology-based. As described in this letter, the examples of "DEPs" — or customer engagement—the SEC identifies in its Request are activities that broker-dealers and advisers have engaged in for decades. As acknowledged in the Request and described below, such engagement provides important benefits to investors.

[3] We use the term "have not" to mean members of communities who traditionally have been underserved by financial institutions and faced barriers preventing or limiting access to traditional brokerage and investment advisory services.

with its "every customer" product offering that has no account minimums, no trading commissions, a uniform margin interest rate, fractional trading, and a user-friendly interface that is easily accessible. Robinhood further promotes financial opportunities for all by communicating with its customers in ways that are designed to enhance retail investors' financial literacy, increase investment awareness, and empower customers to actively manage their investments. An accessible, enjoyable interface that engages customers benefits those customers; and the more time investors spend accessing our free educational tools and resources, the more informed those investors are and the better equipped they are to achieve their financial goals. We believe our efforts to reach investors through straightforward and easy to understand educational content are working. For example, from January 1, 2020 to March 31, 2021, our Robinhood "Learn" content, which we discuss in more detail below, was viewed more than 8 *million* times.

By removing traditional barriers to investing, Robinhood opened the markets to tens of millions of retail investors from all backgrounds. But equally important to providing access, we have demystified Wall Street and engaged these investors. Through our mobile app and website, Robinhood provides its customers with tools, information, and interactions that many could not afford when investors were required to pay commissions and/or advisory fees. Customers are able to engage with their investments and access our capital markets as they plan for their financial well-being and their futures. Engagement in this context is good; the more retail customers are involved in their finances, paying attention to their assets, and learning about investing, the better equipped they are able to build for their financial futures.

To be clear, Robinhood engages with its customers by providing them information they want or need, such as updates on stocks they own or track, answers to questions they or other customers frequently ask, or confirmations when their trades are executed. In other words, we engage our customers with the same types of information that broker-dealers have engaged their customers with for decades. Only now, using our mobile application and website, we are able to engage with everyone, regardless of their wealth, income or background, whenever and wherever they want. Robinhood does *not* use predictive analytics or "deep learning" to make any recommendation that our customers invest in specific securities. And Robinhood does not target customers to induce trading based on who they are or what we predict they will do. Instead, Robinhood does allow customers to subscribe to notifications that alert them to certain news affecting securities in their portfolio or on their watch list. We also provide lists of securities in the same industry (which have been developed by independent third parties) and lists of securities that are popular among Robinhood customers. Our lists are not personalized or tailored to any particular customer; Robinhood simply aggregates and presents complex information in ways that customers find useful, through a mobile app and website interface that is understandable and convenient.

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We believe those "have nots" have been deprived of opportunities for wealth creation and financial well-being previously enjoyed by "haves" who could afford the cost of investing. We do not use the term "have not" disparagingly or to suggest anyone falling under this category lacks the intelligence or capacity to make well-informed investment decisions. We believe every "have not" is capable of managing his or her finances, and deserves the opportunity to participate in the markets and in his or her own financial future. Our belief in empowering previously underserved segments of investors is at the heart of our mission and the core of our values.

Mobile applications, such as the one Robinhood offers, are increasingly important for engaging customers across industries. Customers are accustomed to interacting with apps to order food and groceries, arrange transportation from one place to another, and, importantly, manage their finances. Today, customers want to and do use mobile apps to manage their bank accounts, file their taxes, and even apply for mortgages. Many customers also wish to interact with their broker through an easy to use and understand mobile app. In fact, according to a study from February 2021, nearly half (48 percent) of new investors reported accessing their brokerage accounts primarily through a mobile app.[4]

Our rapid growth proves that retail investors find our mobile app and website helpful and user-friendly; and our customers were waiting for the right platform to help them access and understand the markets. We have over 22 million funded customer accounts as of June 30, 2021, and we are seeing new customers open accounts every day. Over half of the Firm's new customers state that they are new to investing.[5] We believe that this is *unequivocally* a good thing as we have opened the door to investing for a new generation of investors who are younger and more diverse than ever before.[6] Everyday investors have clearly demonstrated their desire and need for understandable information in an accessible medium and a platform that is welcoming and convenient.

As we explain below, Robinhood's use of digital communications and features is driven by our mission to democratize finance for all, including by promoting financial literacy. Section I of this comment letter provides additional background regarding Robinhood, our customers, and our use of so-called DEPs.[7] Section II provides information regarding broker-dealer customer engagement practices generally, the extensive regulatory framework governing brokers' engagement and communication with their customers, and certain legal considerations as the SEC considers potential regulatory actions in response to the Request.[8] Exhibit A ("DEP Categories Identified by the SEC") provides supplemental information regarding Robinhood's use of so-called digital engagement practices as they relate to the nine categories identified in the Request; as noted, Robinhood does not engage in many of the practices

4 FINRA Investor Education Foundation & NORC at the University of Chicago, *Investing 2020: New Accounts and the People Who Opened Them* (Feb. 2021) ("FINRA New Account Study"), https://www.finrafoundation.org/sites/finrafoundation/files/investing-2020-new-accounts-and-the-people-who-opened-them_1_0.pdf.

5 Based on data for the period from January 2015 to March 21, 2021.

6 *See* FINRA New Account Study (finding the majority of new investors were under the age of 45 and were more racially and ethnically diverse than investors who already owned taxable investment accounts prior to 2020); *see also* Aaron Brown, *Stock Investors are Younger and More Racially Diverse*, Yahoo! (Sept. 21, 2020) (reporting the results of a Yahoo Finance Harris poll revealing that the percentage of younger Americans, African-Americans, and Hispanics owning at least one individual stock not held in retirement account increased from 2016 to 2020), https://www.yahoo.com/now/stock-investors-younger-more-racially-100004820.html.

7 This section responds, in part, to Item II.A (Use of DEPs) and II.B (Development of DEPs; Use of Artificial Intelligence or Machine Learning) of the SEC's Request.

8 This section responds to Item II.C (Regulation of DEPs) of the SEC's Request.

identified in the Release.[9] Lastly, Exhibit B provides visual examples of several forms of digital communications and features described in this letter.

While we recognize that appropriately tailored regulation is necessary to ensure that our markets are fair and efficient, and we appreciate the opportunity to respond to the Request, we are concerned that any effort by the SEC to curb broker-dealers' communications with their customers beyond the comprehensive framewo rk that exists today may jeopardize the progress the industry has made in making our markets more diverse and accessible to everyone.

## I. Robinhood's Mission Is to Shrink the Investment Gap and Wealth Disparity, and Technology Is Key to Accomplishing That Goal.

### A. Robinhood's Digital Platform Empowers Everyday Retail Investors.

Robinhood seeks to eliminate the disparity between the "haves" and the "have nots." Investing has traditionally been the domain of the "haves." People who can afford high commissions, minimum account balances, and hundred-dollar single shares of stock—the "haves"—historically had access to the U.S. capital markets. The "have nots"—workers and women and people of color, first time investors, people from rural communities and inner cities alike, gig economy workers and freelancers—did not. By introducing commission-free trading, eliminating minimum account balances, and offering fractional trading, Robinhood changed that.

But providing access alone does not level the playing field. The "haves" do not only benefit from access—they also benefit from continuous engagement. High-net-worth customers paying large commissions to their brokers or fees to their investment advisers to receive information and attention that keeps them engaged in their financial planning. A "have" might receive information from friends and colleagues discussing the markets and finances over dinner, golf, or a cocktail party. A "have" has an investment professional who will answer questions, provide explanations, and highlight relevant information—for example, a broker who monitors the market all day might call to inform a "have" if the price of a stock he owns moves significantly, or invite his client to exclusive events to hear the views of other investment professionals. A "have" receives financial rewards, such as breakpoint or rollover discounts, when he increases his already-substantial investment activity; he also receives rewards such as tickets to professional sporting events, concerts, or shows with his broker, who entertains his client in order to maintain and deepen the relationship. A "have," in other words, receives information and incentives that keep him engaged with the markets and focused on growing his financial wealth.

The Commission is focused here on *digital* engagement. Now that technology has created cost-effective ways for brokers to engage customers who have been historically underserved and/or who cannot afford to pay investment professionals, we fear that at the heart of the Commission's inquiry is a paternalistic view that, these "have nots" simply cannot be trusted to make rational decisions to engage in self-directed trading when presented with the types of information and engagement that have benefited the "haves" for generations.

A "have not" might not have friends and colleagues willing or able to discuss the markets and finances, invitations to hear from investment professionals, or access to a broker who will answer questions and provide explanations. Indeed, a "have not" may not even live in an area where a broker-

[9] This Exhibit responds, in part, to Item II.A (Use of DEPs) of the SEC's Request.

dealer or investment adviser has an office—or if they do, the "have not" may not be able to afford that broker or investment adviser's required minimum investment amount or take time off to meet with the broker or adviser. But with innovations by broker-dealers like Robinhood, a "have not" can now access information and educational resources through a different, accessible, and enjoyable medium wherever and whenever she wants. A "have not" may not be able to pay a broker or investment adviser to monitor the market all day, but she can receive notifications from Robinhood about changes in stock prices or material developments in stocks that she holds or is watching (for example, by placing a stock on her "watch list" and requesting to receive certain notifications about that stock). A "have not" is unlikely to invest enough money to receive discounts (like breakpoints) or gifts (like concert tickets) or business entertainment (like dinners and sporting events) to encourage further investments—but our customers generally remain engaged and committed to their financial health.

In connection with this Request, Chair Gensler recently asked, "How might [the SEC] protect investors in light of the potential conflicts of interest that may exist when DEPs optimize for platform revenues, data collection, or investor behavior?"[10] We do not believe there are conflicts of interest associated with our web- and app-based customer engagement that require additional regulatory action. But even if other broker-dealers' so-called digital engagement practices may create conflicts of interest, we note that conflicts of interest are not new to the financial industry—indeed, the regulatory frameworks established by the SEC, such as Regulation Best Interest ("Reg BI") and the disclosure requirements of the Investment Advisers Act of 1940, rest on the principle that conflicts of interest exist, but investors are able to navigate them when they are adequately disclosed. The current Request concerns whether digital "rewards" like confetti and prize boards (neither of which are available on Robinhood's platform), or artificial intelligence ("AI") or machine learning ("ML") (neither of which Robinhood uses to recommend securities), cause investors to increase their investments, in turn generating more revenue for the customer's broker. Any so-called conflicts of interest presented by digital features pale in comparison to the conflicts presented by the financial discounts and substantial gifts and entertainment that brokers have provided to more traditional investors for decades. Engaging customers is not new; the key difference between human and digital customer engagement is that human engagement is expensive and therefore accessible only by the wealthy. Through digital customer engagement, technology has now leveled the playing field and empowered first-time investors of limited means to engage in the same way with their investments and financial future.

Robinhood's innovative approach seeks to break down the traditional financial barriers to entering the market by offering:

- Zero-commission accounts and no account minimums;[11]

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[10] *See* Chair Gensler, *Statement on Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches* (Aug. 27, 2021).

[11] Robinhood's move to eliminate commissions, which was adopted by the rest of the industry, has saved investors billions of dollars and counting in unnecessary, regressive fees and has made it easier to invest.

- A simple suite of products—exchange-listed equities, exchange-traded funds ("ETFs"), and options;[12]
- Dividend reinvestment, recurring investments (which enable customers to set up recurring investments in particular stocks or ETFs), and fractional trading (which enables customers to purchase large-cap stocks and build diverse portfolios they could not otherwise build, in light of market prices reaching thousands of dollars for a single share of some stocks);
- A mobile app that is easy to use and easy to understand;[13] and
- Tools to enhance financial literacy and enrich retail investors' awareness of the market and their investments, including simple and intuitive ways to access and assimilate large volumes of data to help customers make their own investment decisions.

In addition to making investing more accessible, we recognize that investing is a serious responsibility. Accordingly, Robinhood designed its app to include features that, based on our outreach and research, provide the intuitive experience customers want and expect in a mobile product, while also giving them tools and information to learn about investing, to keep tabs on their finances, and to conduct their own self-directed trading.

### B. Robinhood's Customers Represent the Diversity of the United States.

Despite the importance of active financial planning for the future, the average U.S. retail investor has historically faced significant obstacles to accessing and participating in the capital markets.[14] U.S. investors traditionally faced significant costs related to investing, low levels of financial literacy, and daunting amounts of quickly-changing information about increasingly complex and volatile

[12] Robinhood also offers a limited number of American Depository Receipts ("ADRs") of globally-listed foreign companies.

[13] Unlike some other retail brokers, Robinhood does not offer uncovered options contracts or the ability of customers to sell securities short, and limits the over-the-counter market securities to certain ADRs Receipts of globally-listed foreign companies.

[14] Judy T. Lin & Christopher Bumcrot, *Investors in the United States, A Report of the National Finance Capability Study*, FINRA Investor Education Foundation (Dec. 2019), https://www.finrafoundation.org/files/investors-united-states-report-2019.

markets. We believe democratizing finance for all is an unstoppable movement, and a movement that policymakers on both sides of the aisle have long desired.[15]

Robinhood has made great progress removing barriers to investing and brokerage services for everyday investors. As of February 2021, the median age of our customers was 31, and about half of these customers self-identified as first-time investors.[16] Also as of February, our median customer account size was about $240, with an average account size of about $5,000. What we see is not consistent with narratives suggesting that most of our customers are unsophisticated day traders taking inordinate risks with complex financial products. Those broad mischaracterizations of our customers are false, and only marginalize and alienate a large group of Americans who have been left behind by Wall Street.[17] In fact, our customers are not reckless traders. They engage with our digital application far more often than they execute investment decisions. Each month, on average, more than 21 million customers engage with our application (such as to read the news or educational content, follow their portfolio, and research investments), while only about 7.2 million buy or sell equity securities. The overwhelming majority of our customers—approximately 98% of Robinhood customers—would not qualify as pattern day traders under FINRA's rules.[18]

Our welcoming and user-friendly platform is particularly appealing to investors who have historically been underserved by the financial community. For example, we are proud that the number of women trading on Robinhood's platform nearly tripled in 2020, and women today represent a higher percentage of our customer base than ever before. Based on a representative sampling between July and December 2020, Robinhood customers are also more racially and ethnically diverse than the industry average. African American investors represented nine percent of Robinhood's customer base,

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[15] *See* Chair Gary Gensler, *Testimony Before the United States Senate Committee on Banking, Housing, and Urban Affairs* (Sept. 14, 2021) ("We keep our markets the best in the world through efficiency, transparency, and competition. These features lower the cost of capital for issuers, raise returns for investors, reduce economic rents, and democratize markets"); Chair Jay Clayton, *Testimony before the Financial Services and General Government Subcommittee of the U.S. Senate Committee on Appropriations* (May 8, 2019) ("Other countries want to replicate [U.S. retail investor participation] because such broad investor participation in our capital markets is a significant competitive advantage for our economy, and participation in our capital markets has made many Americans' lives better and their retirements more secure"); Chair Mary Jo White, *Opening Remarks at the Fintech Forum* (Nov. 14, 2016) ("There is relatively widespread agreement that fintech innovations have the potential to transform key parts of the securities industry—and to do so in ways that could significantly benefit investors and our capital markets."); Chair Mary L. Schapiro, *Remarks at the Stanford University Law School Directors College* (June 20, 2010) ("in an area very near to my heart, how can we increase voter participation by retail investors?"); Chair Arthur Levitt, *Plain Talk About Online Investing* (May 4, 1999) ("All of us are participants in an extraordinary social phenomena. The democratization of our markets is a desirable development which regulators should not frustrate. Our mission is not to prevent losers or to modulate the sometimes mercurial movement of our markets.").

[16] All Robinhood customers must be at least 18 years of age.

[17] We believe the generalization that younger investors are taking on excessive risk is also false. For example, a recent study of Millennial and Generation Z investors found that 61% of respondents indicated they were investing for long-term financial stability. *See* The Outsiders, Public.com (Sept. 2021), https://public.com/wp-content/uploads/2021/09/The_Outsiders_Public.com_September2021-FINAL.pdf.

[18] *See* FINRA Rule 4210(f)(8) (defining pattern day trader).

compared with just three percent at incumbent firms. Over the same period, Hispanic investors accounted for 16 percent of Robinhood's customers, compared with seven percent at incumbent firms. Across all brokerage firms in the United States, stock ownership is younger and more diverse than when Robinhood was founded back in 2013, and we believe that our platform has helped to propel those changes across the industry.[19]

From the beginning, we have built products for everyday people. By untethering investment from the desktop computer or brick-and-mortar brokerage offices and demystifying the process, we have seen new groups of people discovering Robinhood and becoming investors.

### C. Robinhood's Customer Engagement Is Key to its Mission of Democratizing Finance for All.[20]

Robinhood, like all businesses, seeks to engage its customers—and that engagement is what empowers our customers to learn about investing and save for longer term financial goals such as paying for college or graduate school, starting a family, or purchasing a home. To this end, Robinhood uses technology to communicate with its customers in a number of ways designed to promote financial literacy, increase investment awareness, and empower customers to actively manage their investments, consistent with our mission. Before describing these practices in more detail, there are six fundamental points to emphasize regarding our customer communications:

- *Customers have the right to opt out of push notifications*. At Robinhood, notifications and alerts are configurable both within the mobile app and the customer's phone. This means that customers may turn off most push notifications in two ways, by setting their preferences in the mobile app or on their mobile device. The only push notifications that customers cannot disable are notifications that serve a regulatory purpose or relate to important account information, such as a margin call.[21]
- *Robinhood's use of technology does not perpetuate social biases or disparities*. We do not differentiate among customers based on race, gender, religion, politics, or sexual orientation or identification; and we do not use predictive data analytics. Our digital engagement is based on relevant objective factors such as a customer's account balance and portfolio holdings, or on a customer's stated preferences, such as notification settings. As described above, Robinhood's accessible platform is a key reason why many people of all backgrounds and socio-economic status are participating in the markets today.
- *We do not use technology to recommend securities or investment strategies involving securities and we do not use AI or ML to engage in such activities*. Under well-established securities law precedent, Robinhood's current customer engagement does not involve making "recommendations." Robinhood does not recommend securities to particular investors or groups of investors using AI, ML (for example by sending or pushing specific

[19] *See* FINRA New Account Study, *supra* note 4.

[20] This section responds, in part, to Item II.A (Use of DEPs) and II.B (Development of DEPs; Use of Artificial Intelligence or Machine Learning) of the SEC's Request.

[21] *See e.g.,* Exchange Act Rules 10b-10 (confirmations); 15c3-3 (account statements); 17a-14 (Form CRS), FINRA Rule 2231 (Customer Account Statements).

investment recommendations or trade ideas tailored to specific customers), or any other method.[22] Rather, Robinhood maintains a self-directed brokerage model, meaning customers have control over their investments, are empowered to make their own decisions, and place their unsolicited orders with us. The SEC acknowledged the benefits of a self-directed model such as Robinhood's in adopting Reg BI,[23] explicitly stating that Reg BI does not apply to this model.[24]

- *Robinhood promotes investor education and financial literacy*. While we do not provide investment advice or recommendations to our customers, we are committed to helping our customers build sustainable, long-term financial success and offer a variety of educational tools and resources to help them achieve their goals. With Robinhood Learn, this commitment extends beyond our customers to the general public. We discuss our educational efforts in more detail below and in our responses to DEP Categories Identified by the SEC, attached as Exhibit A.
- *Our mobile app and website are not social media platforms for customer-to-customer interaction.* Unlike other firms, Robinhood does not provide social forums within our app or our website where customers can "like," "follow" or "share" their investments with other customers; Robinhood does not offer a "chat" feature for customer-to-customer messaging; and Robinhood does not offer a "copy trading" feature. All engagement on our app and platform today is directly between Robinhood and its customers.
- *Our mobile app is not a game.* Unlike other firms, we do not host trading competitions, we do not maintain a "leaderboard," and we do not offer badges or visual markers of achievement. Our app is a tool for investing that is welcoming and understandable for every investor; it is not a game.

As stated above, many of our digital features are designed to promote financial literacy and investment awareness and to provide customers with information they need and want in order to make informed and self-directed decisions about their future investment goals and needs. While these practices have been commonplace in the brokerage industry for decades, we have adapted them for a digital age and a digital platform. These features include the following and are further discussed in Exhibit A ("DEP Categories Identified by the SEC").

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[22] *BNP Paribas Mortg. Corp. v. Bank of Am., N.A.*, 866 F. Supp. 2d 257, 268 (S.D.N.Y 2012) (citing NASD NTM 01-23 (Apr. 2001)) (internal quotations omitted).

[23] *Regulation Best Interest: The Broker-Dealer Standard of Conduct*, 84 Fed. Reg. 33,318, 33,322 (Jul. 12, 2019) ("Reg BI Adopting Release") (concluding that a standard of conduct not appropriately tailored to the structure and characteristics of a broker-dealer business model (i.e., transaction-specific recommendations and compensation) would "significantly reduce retail investor access to differing types of investment services and products" and "reduce retail investor choice in how to pay for those product and services").

[24] *Id.* at 33,384 ("Nor does Regulation Best Interest apply to self-directed or otherwise unsolicited transactions by a retail customer…").

- *Robinhood Learn* ("Learn") is at the center of the Firm's effort to make investing more accessible and provide financial education to both our customers and to those who have not yet started their investing journey.[25] Learn is available to everyone on the Robinhood website and does not require a Robinhood account to access. Through Learn, Robinhood provides an extensive hub of educational articles for investors of every experience level in an easy-to-read format. We regularly collect feedback from readers to understand whether content is helpful, and this feedback helps guide updates to our Learn articles. Robinhood Financial has published more than 850 articles to help people learn about investing and answer their most basic questions about investing such as "What is a Limit Order?" along with articles covering a host of more complex subjects. As previously mentioned, from January 1, 2020 to March 31, 2021, Robinhood Learn content was viewed more than 8 million times.
- *In-App Education*. Robinhood provides customers with news and educational content directly in the app to empower our customers to learn about the markets and make their own informed investment decisions. For example, Robinhood offers *free* news from reliable sources including *Barron's*, *Reuters* and *The Wall Street Journal*. We also recently rolled out interactive lessons that help customers learn and build a knowledge base as they use the app, and we have begun to integrate Learn directly into the app. We believe our customers prefer and benefit from educational content delivered in-context, as they are using our app. Consistent with our mission, Robinhood is committed to continually increasing the amount of content provided to customers on their mobile phones, recognizing that our customers want digestible information wherever and whenever they need it.
- *Robinhood Snacks*. Robinhood Snacks is another avenue for educating our customers and the general public about investing in a very approachable and entertaining format. Snacks is a curated digest of business news stories delivered both daily and weekly. Snacks can be accessed in written, audio, or video formats, including via a podcast and newsletter, and allows subscribers to start their days with the top business news of the day in an accessible, digestible medium. Our Robinhood Snacks Newsletter was opened more than 200 million times in the first half of 2021, while the podcast was downloaded over 21 million times in the same period. We believe the Robinhood Snacks Newsletter is one of the most read newsletters today.
- *Watch Lists*. Robinhood also allows customers to create their own lists of companies that the customer is interested in "watching," and based on these watch lists, it provides customers with news updates regarding the companies and stocks the customer has elected to add to the list. When a customer opens an account, Robinhood pre-populates a "watch list" that the customer can change or eliminate. The same default "watch list" is displayed to all new customers.

[25] *See The building blocks of your financial journey,* Robinhood*,* https://learn.robinhood.com/ (last visited Sept. 30, 2021).

- *Cards*. "Cards," are brief messages that surface on the app and the website and link to additional content. Cards provide a customer with updated news about companies that the customer has placed on his or her watch list or general information about certain products and services available on our platform. Clicking on a card regarding a company takes the customer to a news article concerning that company; clicking on the card does not take the customer to a trading screen.
- *Notifications*. One of the great advantages of using mobile devices is the ability to receive notifications and alerts regarding everything from your account being logged into by another device for the first time, to a notice that someone is at your front door, to a notice that your mortgage has been approved. Likewise, Robinhood believes that many customers expect to have notifications/alerts about their investments available to them and rely upon them. Robinhood has the ability to send notifications and alerts as (1) push notifications that appear on a customer's mobile device; (2) e-mail communications; and (3) in-app messages. As stated above, push notifications and e-mail alerts are configurable by a customer to that customer's preferences.

  We believe it is unequivocally a good thing, and in our customers' best interest, for Robinhood to have the ability to notify our customers of certain events and occurrences regarding their accounts or securities they own or have chosen to watch. For example, through notifications we are able to notify customers about unique risks associated with certain products (e.g., leveraged or inverse ETFs) so they can make better informed investment decisions.[26] We are also able to share with customers important information regarding their holdings, such as corporate actions, bankruptcies, and shareholder votes. Other examples include: notifying a customer when the price of a stock the customer already owns reaches a 52-week high or low or changes by 5% or 10%; suspicious activity in the customer's account; margin maintenance alerts or margin call warnings; and options expiration reminders.[27] With the exception of certain notifications that serve a regulatory purpose or provide important account information, a customer may opt out of receiving push notifications and emails in her app and/or on her phone.
- *Sector & Other Lists*. Robinhood (like most brokerage firms) provides customers with lists of well-known stock sectors such as: Technology, Energy, Energy & Water, Healthcare, Software, Automotive, Finance, Food & Drink, Banking, Pharma and one category titled, "Tech, Media and Telecom." These lists are developed using data from a third-party vendor (FactSet for equities and Morningstar for ETFs) and are not personalized for any particular customer. Robinhood also provides lists reflecting data from our platform—the 100 Most Popular Stocks on Robinhood, Daily Movers, and IPOs that are available on Robinhood.28 By providing information categorized in these ways for free, Robinhood empowers its customers to access and synthesize information about thousands of different

[26] For an example of this type of notice, see Exhibit B ("Examples of Customer Engagement").

[27] For a more detailed description of Robinhood's notifications, *see* Exhibit A ("DEP Categories Identified by the SEC").

[28] The Robinhood generated lists are compiled with objective parameters. As noted above, this is consistent with the practice of many other broker-dealers.

publicly-traded companies without paying the fees/commissions often associated with this type of data in more traditional advisory and brokerage models.

- *Celebrations for milestones.* Robinhood does celebrate certain milestone events such as a customer opening an account, funding an account, and first investment. These digital "celebrations" may take the form of animation and graphics that create a familiar and welcoming experience for the customer. The SEC's own Office of Investor Education and Advocacy recognized the importance of celebrating milestones in a recent tweet, stating that "[w]hen you realize the importance of diversification, that's knowledge worth celebrating." Notably, this statement was accompanied by some of the DEPs the SEC has identified for comment—specifically, a video featuring confetti, balloons, and a couple celebrating.[29] In the past, Robinhood used animated confetti—which is a widely-recognized symbol of celebration—to acknowledge milestones. Robinhood, however, stopped this practice and now uses a different form of animation to mark milestones in our customers' financial journeys.[30]

- *User-Friendly Application Interface.* Another important way that Robinhood engages retail customers is through a mobile-design feature that is user-friendly and easily accessible. Designing a mobile-first platform for customers is challenging because of the limited space on a phone screen, which varies from phone to phone. Screens must be used efficiently—visual cues, colors, and the use of plain English all combine to create a user interface that is simple to understand and use. The efficiency of design that creates a delightful customer experience should not be considered "gamification" and does not indicate any intent to manipulate customers. Just as Apple designs iPhones to look, feel, and operate for the convenience and enjoyment of its customers, mobile applications can, and should, be designed for customer use and enjoyment. By making our mobile application straightforward and enjoyable, we make investing more accessible and less intimidating. In fact, securities regulators traditionally have endorsed the use of user-friendly and accessible communications as something that should be promoted, not penalized.[31]

In short, education and information are core to accomplishing our mission, and one of the primary ways we educate and inform is through our so-called DEPs. We believe access to easy-to-understand investment information and education is fundamental to expanding participation in the U.S.

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[29] SEC Investor Ed (@SEC_Investor_Ed), TWITTER (Jun. 23, 2021, 4:33PM), https://twitter.com/SEC_Investor_Ed/status/1407799023210319874. This statement and video were for the purpose of promoting a new SEC webpage, "investor.gov."

[30] *A New Way to Celebrate with Robinhood*, Robinhood (Mar. 31, 2021), https://blog.robinhood.com/news/2021/3/31/a-new-way-to-celebrate-with-robinhood.

[31] For example, the instructions to the SEC's new Form CRS specifically encourage registrants to use charts, graphs, tables, and other graphics, text features, colors, and graphical cues designed to enhance a retail investor's understanding of the material in the relationship summary. *See* Form CRS, Instruction 3.A. Although we have heard some officials state that creating a customer experience that causes users to stay on an app may be a "recommendation," it is not possible to find support in the law for such a far reaching interpretation (much less, a definition) of what constitutes a recommendation.

financial system. Avoiding complex industry jargon is crucial to our goal of demystifying finance for retail investors. We fully recognize, and have always taken seriously, the responsibility that comes with giving customers the tools to invest on their own terms. That's why Robinhood provides free educational resources available to everyone—not just our customers—on the Robinhood Learn website. We have also rolled out features like our "Year in Review" feature that helps customers reflect on their investing activity and understand the diversity of their investments—all with a focus on simplicity and ease-of-understanding.

Historically, the U.S. securities regulators have recognized the importance of customer engagement to overcome barriers to entry that prevent underserved communities from participating in the wealth opportunities provided by U.S. capital markets. As recognized by FINRA, financial literacy is highly correlated with positive future financial outcomes and behaviors.[32] Furthermore, differing levels of financial literacy may contribute to inequality.[33] The SEC also recognized the importance of investor education efforts in the Reg BI Adopting Release, agreeing that "Regulation Best Interest should not stifle investment education as a means to encourage financial wellness."[34]

## II. Digital Engagement Practices Are Well Established and, for U.S. Broker-Dealers, Already Subject to Extensive Regulation.

### A. The U.S. Economy Is a Digital Economy.

Digital engagement is not only a lower-cost way to engage customers; it is now the most effective way to interact with individuals in business, education, and everyday life. Today, people can pay their taxes, purchase a car, and obtain a loan or a mortgage, all through a mobile app on their smartphone. Even state and federal governments rely heavily on their ability to engage constituencies through digital means. State and local governments, for example, use direct text messaging campaigns, social media, and customized "exposure alerts" to encourage people to obtain COVID vaccinations and to notify citizens of potential exposures. Governmental engagement is not limited to the health crisis. Individuals rely on mobile apps as their primary source for government-provided information, interaction, and entertainment.[35] As described above, the SEC itself relies on various forms of

[32] Marco Angrisani, Jeremy Burke, Annamaria Lusardi, and Gary Mottola, *The Stability and Predictive Power of Financial Literacy: Evidence from Longitudinal Data* (Oct. 2020), https://www.finrafoundation.org/sites/finrafoundation/files/stability-and-predictive-power-financial-literacy-evidence-longitudinal-data.pdf.

[33] *See e.g.,* FINRA New Account Study ("because New Investors and Experienced Entrants differ markedly along racial/ethnic and age groups, these needs may be further impacted by cultural differences and familiarity with investing, as well as disparities in investor education."); Gutter, M.S., and Fontes, A., *Racial Differences in Risky Asset Ownership: A Two-Stage Model of the Investment Decision-Making Process. Journal of Financial Counseling and Planning*, 17(2), 64–78 (2006).

[34] Reg BI Adopting Release at 33,338.

[35] For example, the state of Massachusetts created a "Mass Lottery app" that purports to offer various features designed to promote the state's lottery. According to the website, the app was recently re-designed so that participants can "enjoy the thrill of winning wherever [they] are." Mobile App, MassLottery (last visited Sept. 30, 2021), https://www.masslottery.com/tools/mobile-app.

technology to communicate information to investors and market participants.[36] For the same reasons the government relies on digital forms of engagement, businesses also rely on customer engagement through digital forms to maintain customer relationships in a safe, efficient, and effective manner.

The same is true for the equity markets, where 30% of retail investors in the United States placed orders using a mobile app, according to 2018 FINRA surveys. That number grows to 59% when looking solely at participants aged 18-34. Innovative technology-based companies are challenging traditional norms and engaging people in new ways.

Customers now expect and demand intuitive, engaging, and easy-to-use products. According to a report by PricewaterhouseCoopers LLP ("PwC"), 73% of consumers worldwide point to customer experience as an important factor in their purchasing decisions, and 65% of U.S. consumers find a positive experience with a brand to be more influential than great advertising.[37] At the same time, smartphone usage is not only the norm, but a critical component of how people interact with the world around them. Americans rely on their phones for information, interaction, and entertainment. And they expect access whenever and wherever it is needed.

The securities industry's use of DEPs is just part of this bigger picture. There is nothing inherently more problematic about web- or app-based communications than there is about in-person, written, or oral engagement. To be sure, the securities regulators have acknowledged customer preferences for accessing their accounts primarily through mobile applications, particularly new investors.[38] There is no reason why the use of digital engagement in the securities industry should be singled out for enhanced scrutiny and suspicion.

### B. Broker-Dealer Communications and Customer Engagement Practices—Whether Digital or Traditional—Are Already Subject to Extensive Regulation.[39]

Unlike other industries that rely on digital engagement, broker-dealer communications and customer engagement practices are already subject to extensive regulations under SEC and FINRA rules. The existing regulatory framework is focused on promoting conduct that, among other things, protects investors from abusive practices. This framework applies equally to DEPs as well as to more traditional forms of communication and customer engagement.

First and foremost, as noted in the SEC's Request, the anti-fraud provisions of the federal securities laws and FINRA rules require broker-dealers to deal fairly with their customers and observe high standards of commercial honor and just and equitable principles of trade.[40] To the extent the SEC

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[36] See *supra* note 29 and surrounding text. *See also* the SEC's "Howey Coins" website (last visited Sept. 30, 2021), https://www.howeycoins.com/index.html.

[37] Future of Customer Experience Survey, PwC (2018), https://www.pwc.com/us/en/zz-test/assets/pwc-consumer-intelligence-series-customer-experience.pdf.

[38] FINRA New Account Study.

[39] This section responds to Item II.C of the SEC's Request.

[40] *See, e.g.,* Section 17(a) of the Securities Act of 1933, Sections 10(b) and 15(c) of the Securities Exchange Act of 1934; FINRA Rule 2010.

is concerned that broker-dealers or investment advisers will use the types of practices described in the Request to commit fraud or manipulation, existing securities laws and regulations address such conduct. And engagement practices that promote investor education and more information would help combat such schemes. In addition, broker-dealers are subject to an extensive set of specific rules governing communications with the public, including advertising and marketing communications.[41] All communications must be based on principles of fair dealing and good faith, be fair and balanced, and comply with a number of other content standards.[42]

We believe reasonable regulation is essential for the fair working of the securities industry and protection of investors. For example, existing regulations prohibit broker-dealers from sending false or misleading notifications to customers. Existing regulations also require broker-dealers to reasonably supervise their customer communications for compliance with applicable securities laws and regulations. We agree with the SEC's statement in the Request that, at least in some circumstances, "[t]he use of a DEP by a broker-dealer may, depending on the relevant facts and circumstances, constitute a recommendation for purposes of Reg BI." If a broker-dealer were to send a customer a notification actually recommending that the particular customer buy or sell a specific stock, whether that recommendation comes directly from a person or through the use of AI, we agree that the broker-dealer would be required to comply with Reg BI.

However, none of Robinhood's digital features today include "recommendations," and they would not trigger Reg BI. A recommendation is a "call to action" in which a broker-dealer brings a specific security to the attention of a customer. The regulators have recognized the "content, context, and presentation of the particular communication or set of communications" must be analyzed in order to determine whether a communication is considered a recommendation.[43] The more individually tailored the communication is to a particular customer or group of customers, the more likely the communication will be viewed as a "recommendation."[44] FINRA has stated that a broker does not make a recommendation if it "allows customers to subscribe to emails or other electronic communications that alert customers to news affecting the securities in the customer's portfolio or on the customer's 'watch list.'"[45] Further, a broker does not make a recommendation when it provides tools on its website or mobile app allowing customers to screen through a wide universe of securities and to request lists of securities meeting broad, objective criteria.[46]

As discussed in Section I, Robinhood does not use digital engagement practices to recommend securities or strategies involving securities. While Robinhood provides information about securities a particular customer owns or places on her "watch list" (*e.g.*, push notifications about market movement or cards concerning recent news), these are not "calls to action" under well-established guidance and

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[41] *See e.g.,* FINRA Rule 2210.

[42] *Id.*

[43] *See* NASD NTM 01-23 (Apr. 2001); FINRA Regulatory Notice 11-02 (Oct. 7. 2011).

[44] FINRA Regulatory Notice 11-02 (Oct. 7, 2011).

[45] NASD NTM 01-23 (Apr. 2001).

[46] *Id.*

are commonly used by broker-dealers offering self-directed brokerage.[47] Any SEC rulemaking that results in applying Reg BI to self-directed brokerage activity merely because a broker-dealer uses digital features to engage with customers would be inappropriate and inconsistent with Reg BI itself.[48]

Importantly, none of the engagement practices identified in the Release are new to the industry: as discussed above, broker-dealers have engaged in these practices in a non-digital form for years, and FINRA and the SEC have regulated these practices for years. For example, professionals at brick and mortar broker-dealers have always been able to congratulate new customers for opening an account with the firm or making their first investment. Broker-dealers have always been able to distribute educational materials and research reports to customers and provide curated lists of securities categorized by sector, market capitalization, dividend yield, or otherwise. Broker-dealers regularly entertain their customers—which at brick and mortar firms may include engaging in-person with high net worth and institutional customers at expensive dinners, sporting events, and performances (subject to FINRA rules on gifts and entertainment). And the brokerage industry has provided notifications by phone, fax, and electronic mail for decades to their customers (both institutional and retail) when there are notable events (e.g., price target changes). As early as 2001, FINRA addressed how these notifications should be handled when provided in electronic form.[49] FINRA provided these interpretations using a technology neutral, principles-based framework that we believe has withstood the test of time.

Many of the digital practices that the SEC characterizes as “DEPs” do nothing more than expand access to traditional forms of engagement to everyone, regardless of their wealth, income, or background, and wherever and whenever they want. Practices such as notifications, graphics, visual cues and curated lists are low-cost ways to present market information to individuals and families that previously faced systemic barriers to receiving it. These practices provide demonstrable benefits for customers in the form of information (as opposed to expensive meals or tickets to sporting events). To be sure, if firms stopped providing timely information about market conditions or the status of a customer’s account to customers, they could face criticism by the SEC and FINRA because in many instances, digital engagement may be the most effective way to provide important information to customers. To this end, singling out DEPs for special scrutiny or suspicion because they create a positive experience is antithetical to the idea that investors should be free and empowered to invest in the companies they believe in, and to take greater control of their finances. Indeed, the Chair recently endorsed the view that “investors get to decide what risks they wish to take.”[50] This view is consistent with the whole purpose of the self-directed retail brokerage model where investors affirmatively elect

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[47] *Id.*

[48] “Regulation Best Interest *would not* … apply to self-directed or otherwise unsolicited transactions by a retail customer.” Reg BI Adopting Release, at 33,384-85.

[49] NASD NTM 01-23 (Apr. 2001).

[50] Gary Gensler, *Chinese Firms Need to Open Their Books*, Wall St. J. (Sept. 13, 2021) (“In response to the Great Depression, President Franklin Roosevelt and Congress established a basic bargain. Investors get to decide what risks they wish to take. Companies that are raising money from the public must make full and fair disclosures to investors. This bargain has been a source of America’s economic success for 90 years.”), https://www.wsj.com/articles/china-accounting-standards-shell-company-vie-investment-sarbanes-oxley-sec-gensler-11631563524.

to engage in investment activities, and it is up to the investors what that investment activity involves—be it ETFs, options, or fractional shares.

Ultimately, any regulation that results in less customer engagement and less customer choice is a bad policy outcome.[51] Today, many retail investors choose a self-directed brokerage model because it is more cost-efficient and provides them with the tools they want and need to invest. These customers may not be able to afford commissions or qualify for the asset thresholds that investment advisers demand. Other customers simply prefer the autonomy that comes with a self-directed model. When it adopted Reg BI, the SEC recognized the important benefits of a self-directed brokerage model.[52] Providing customers with recommendations and advice requires brokers and investment advisers to implement significant supervisory structures and compliance processes to ensure compliance with the securities laws. Those costs are passed along to investors who use those services. Self-directed brokerages, in contrast, offer investors access to the capital markets without these additional fees and expenses.

Retail investors have had more opportunities to participate in the financial markets than ever before because of self-directed firms like Robinhood. The SEC should be celebrating this fact, not engaging in rulemaking that undermines this retail participation by preferencing brokerage models that only the "haves" can afford. In the adopting release to Reg BI, the SEC recognized that over-regulation could limit choices for retail investors. Specifically, the SEC discussed the now-vacated Department of Labor ("DOL") Fiduciary Rule, which would have imposed significant costs on broker-dealers providing recommendations to certain accounts. The SEC noted that the Fiduciary Rule would have resulted in "significant reduction in retail investor access to brokerage services," and stated the belief that "the available alternative services were higher priced in many circumstances."[53] The SEC also cited a SIFMA Study finding that, for the majority of retail customers whose brokers limited their services because of the Fiduciary Rule, customers chose to move to self-directed accounts rather than fee-based accounts.[54] The SEC should heed the lessons from the failed Fiduciary Rule and not make the same mistakes in the context of digital engagement.

Limiting digital engagement practices will have the practical effect of limiting retail customers' ability to access easily digestible information and make their own self-directed decisions. Rulemaking that would expand regulations such as Reg BI to the self-directed model based on ordinary engagement practices made through digital platforms would increase the cost of offering self-directed brokerage,

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[51] We believe regulatory efforts to curtail digital engagement is also contrary to the SEC leadership's stated policy of encouraging investors to start saving early and regularly. *See* Gary Gensler (@GaryGensler), TWITTER (Sept. 22, 2021, 11:53 AM), https://twitter.com/GaryGensler/status/1440705940567719944 (Statement of Chair Gensler on Twitter encouraging college students to "start saving early, and save regularly"); SEC (@SECGov), TWITTER (Jun. 23, 2021, 4:26 PM), https://twitter.com/SECGov/status/1407797340342304771 (statement of the official SEC twitter announcing a public service campaign to educate investors on the benefits of investing and encouraging investors to use the SEC's free financial planning tools).

[52] Reg BI Adopting Release at 33,319-22.

[53] *Id*. at notes 32, 34, and surrounding text.

[54] *Id.* at note 34.

and therefore increase the cost of investing. It would also draw an arbitrary distinction between the ways in which a digital platform and a traditional broker-dealer are permitted to engage with customers.

Rather than engaging in new rulemaking that may result in less investor education, less customer engagement, and less affordable market access for retail investors, we believe the industry would benefit from the SEC evaluating how it can further reduce the costs of investment and barriers to entry. For example, the SEC could assess prescriptive and potentially outdated existing rules that impose significant costs on market participants—costs that are ultimately passed along to the retail customer.[55] By eliminating extraneous costs and expenses and making investing more affordable, the SEC could *increase* customer choice. In contrast, regulation that would drive up the cost of currently affordable self-directed brokerage services will only *decrease* choices for those "have nots" who only recently entered the market and have begun to appreciate the benefits enjoyed by the "haves" for generations. The SEC also could enforce current laws to ensure that practices that may contravene existing regulation are curtailed—such as "copy trading" where a copied trader may be receiving transaction-based compensation without registering as a broker-dealer.

**C. Potential DEP Rulemaking Will Face Significant Administrative Procedure Act ("APA") Challenges and Require the SEC to Build a Comprehensive and Rigorous Record and Assess the Significant Costs of Regulation.**

To be justified and lawful, any DEP rulemaking will need to address significant issues. Under the APA, the SEC has a foundational duty of reasoned decisionmaking when it comes to rulemakings, particularly rulemakings addressing issues so consequential to retail investors. In order to conduct a proper rulemaking, the SEC will need to "examine the relevant data"—including quantitative and qualitative evidence submitted—"and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choices made.'"[56] This core APA requirement includes the obligation to "consider … important aspect[s] of the problem" before the agency,[57] and it will obligate the SEC to respond to significant points raised in public comments.[58]

Robinhood firmly believes that once the SEC collects, discloses, and analyzes relevant evidence and data, that record will make crystal clear that calls by some for enhanced DEP regulation are in fact solutions in search of a problem. As described in detail above, DEPs used by Robinhood and others are not harming retail investors, rather they are a proven means for educating investors and for lowering barriers to investment.[59] On this score, short-term anecdotes and speculation must not be allowed to

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[55] The SEC's Exchange Act Rule 17a-4(f) consists of technology-specific rules that are more than 20-years old and require broker-dealers to maintain outdated and unnecessarily expensive technology. *See, e.g., Petition for Rulemaking to Amend Exchange Act Rule 17a-4(f),* Futures Industry Association, Securities Industry and Financial Markets Association et al. (Nov. 14, 2017), https://www.sec.gov/rules/petitions/2017/petn4-713.pdf.

[56] *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

[57] *Id.*

[58] *See PPL Wallingford Energy LLC v. FERC*, 419 F.3d 1194, 1198 (D.C. Cir. 2005); *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001); *Tesoro Alaska Petroleum Co. v. FERC*, 234 F.3d 1286, 1294 (D.C. Cir. 2000).

[59] *See supra* pp. 3-12.

substitute for a rigorous review of available evidence. And Robinhood is confident that such a rigorous review of the evidence will conclusively demonstrate the absence of any investor harm that could justify additional DEP regulation. To this end, potential DEP rulemaking will face significant APA challenges:

***First***, as a crucial threshold matter, the SEC will be obligated to demonstrate—with real-world evidence and reliable data—that there are sufficient problems in the marketplace that warrant additional regulatory intervention.[60]

As the D.C. Circuit recently explained, "[r]ules are not adopted in search of regulatory problems to solve," and "unless an agency's authorizing statute says otherwise, an agency regulation *must* be designed to address *identified* problems."[61] In other words, the APA presupposes that the agency has identified a "problem" in need of a government-mandated remedy;[62] it follows that a regulation cannot be a "solution in search of a problem."[63] In fact, a "regulation perfectly reasonable and appropriate in the face of a given problem may be highly capricious if that problem does not exist."[64]

When it comes to assessing the risk of harms that might justify regulation, moreover, conjecture by the SEC will not do. "[M]ere speculation" does not constitute "adequate grounds upon which to sustain [an agency's] conclusion."[65] Indeed, "agency actions based upon speculation are arbitrary and capricious."[66] The Request is a step in the right direction in terms of collecting evidence bearing on the existence of harm, if any, from current practices, but the SEC must follow the evidence and avoid using speculation about future risks to fill evidentiary gaps.

As part of this evidence-gathering process, basic APA principles will require the SEC to disclose and make available for comment and public input all key materials (including data and studies) on which the SEC relies.[67] "Integral to an agency's notice requirement" under the APA "is its duty to 'identify and make available technical studies and data that it has employed in reaching the decisions to propose

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[60] *E.g., National Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831, 843 (D.C. Cir. 2006) ("Professing that an order ameliorates a real industry problem but" citing no reliable "evidence demonstrating that there is in fact an industry problem is not reasoned decisionmaking.").

[61] *New York Stock Exch. LLC v. SEC*, 962 F.3d 541, 556 (D.C. Cir. 2020) (emphases added).

[62] *State Farm*, 463 U.S. at 43.

[63] *New York v. U.S. Dep't of Health & Human Servs.*, 414 F. Supp. 3d 475, 546 (S.D.N.Y. 2019).

[64] *City of Chicago v. Fed. Power Comm'n*, 458 F.2d 731, 742 (D.C. Cir. 1971).

[65] *Natural Res. Def. Council, Inc. v. EPA*, 859 F.2d 156, 210 (D.C. Cir. 1988); *see also Otay Mesa Prop., L.P. v. Dep't of the Interior*, 344 F. Supp. 3d 355, 370 (D.D.C. 2018).

[66] *Horsehead Res. Dev. Co., Inc. v. Browner*, 16 F.3d 1246, 1269 (D.C. Cir. 1994).

[67] *See U.S. Lines, Inc. v. Fed. Mar. Comm'n*, 584 F.2d 519, 534 (D.C. Cir. 1978) (explaining "require[ment]" that "information in agency … reports identified by the agency as relevant … be disclosed … for adversarial comment"); *Chamber of Commerce v. SEC*, 443 F.3d 890, 900 (D.C. Cir. 2006); *Air Transp. Ass'n of Am. v. FAA*, 169 F.3d 1, 7 (D.C. Cir. 1999).

particular rules.'"[68] This requirement is "anchored" in the APA's "statutory provision[s]" governing rulemakings, and is bedrock administration law.[69]

***Second,*** and closely related to the SEC's obligation to demonstrate an actual need for additional regulation, the SEC will need comprehensively and thoughtfully to examine existing regulations of broker-dealers and investment advisers and to explain why those protections are sufficient or not to accomplish the SEC's purported regulatory objectives.[70] As detailed above, customer engagement practices, now manifesting as digital engagement practices, not new and they are already subject to significant existing regulatory controls designed to protect retail investors.[71] Before the SEC rushes to impose new and costly regulatory mandates on the market, the SEC must analyze this "existing regime" and determine whether "sufficient protections" already exist.[72] A "failure to analyze" carefully existing regulations would render any SEC final regulation "arbitrary and capricious."[73]

***Third***, even assuming the SEC could identify a justification for enhanced regulation of DEPs, the SEC will be obligated to give careful consideration to alternatives to any additional regulations that the SEC ultimately adopts.[74] This "reasonable alternatives" standard is not a pro forma legal requirement, but one that strikes at the heart of the APA's duty of reasoned decisionmaking by ensuring that agencies identify which alternatives they have considered and reasonably explain why those alternatives could not achieve the relevant regulatory objectives. Failure to do so here would result in vacatur of any final DEP regulation.

***Fourth,*** we observe that any SEC rulemaking restricting the use of digital engagement practices must be consistent with the statutory grants of rulemaking authority to the SEC in the Exchange Act. The SEC does not have *carte blanche* under the Exchange Act to restrict non-deceptive, non-manipulative DEPs that do not constitute "personalized investment advice." DEPs that engage subscribers by providing truthful information and making the platform more convenient, accessible, and user-friendly are not ones that the SEC has clear authority to regulate. The SEC should be conscious of the limits on its statutory authority in any proposed regulation of DEPs.

***Fifth***, and critically, the SEC will be obligated to pay careful attention to the potentially significant costs, as well as supposed benefits, of additional regulation of DEPs. As the Supreme Court has explained, "reasonable regulation ordinarily requires paying attention to the advantages *and* the

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[68] *Kern Cty. Farm Bureau v. Allen*, 450 F.3d 1072, 1076 (9th Cir. 2006).

[69] *Am. Radio Relay League, Inc. v. FCC*, 524 F.3d 227, 236-237, 239 (D.C. Cir. 2008) (citing 5 U.S.C. § 553(b)-(c)).

[70] *American Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 179 (D.C. Cir. 2010) (SEC had obligation "to determine whether, under the existing regime, sufficient protections … exist[]").

[71] *See supra* pp.14-19.

[72] *American Equity*, 613 F.3d at 179.

[73] *Id.*

[74] *See Laclede Gas Co. v. FERC*, 873 F.2d 1494, 1498 (D.C. Cir.1989) (failure to consider reasonable alternatives is arbitrary and capricious).

disadvantages of agency decisions."[75] And here, the SEC will face heightened obligations to quantify and consider the costs, as well as the benefits, of any additional regulations. For example, under the Exchange Act, Congress has required the SEC to consider whether its rules will "promote efficiency, competition, and capital formation."[76] And, under the Securities Act, the SEC must "consider … whether the action will promote efficiency, competition, and capital formation."[77] These requirements "impose[] on the [SEC] an obligation to consider the economic implications of certain rules it proposes."[78] When the SEC fails to meet this obligation and accord "proper[]" consideration to the economic implications of its rules, the agency acts arbitrarily and capriciously.[79]

Consideration of costs will be critical to any rulemaking process for DEPs. Many DEP regulations could have significant costs to the extent that regulatory overreach or one-size-fits-all mandates stifle investment and innovation in products that are designed to educate investors and democratize access to capital markets.[80] It will be imperative that the SEC collect robust and reliable evidence of these costs and give due weight to these interests in any subsequent rulemaking. As the D.C. Circuit has said, an agency thus must "face the trade-off[s]" caused by its decisions and explain why "the trade-off" it selected "was worth it."[81] A one-sided or cursory analysis of costs and benefits of DEP regulation would not satisfy the APA. Moreover, it will be critical that the SEC fully identify and *explain* the trade-offs and costs inherent in any regulation: the APA demands that an agency "give adequate reasons for its decisions,"[82] and, it follows, "conclusory statements will not do; an 'agency's statement must be one of *reasoning*.'"[83] This bedrock requirement will demand that the SEC collect and fairly evaluate evidence bearing on advantages and disadvantages of additional DEP regulation.

What is more, as part of its analysis of the disadvantages of any new regulations in this area, the SEC will be required to identify and account for the "significant reliance interests" of broker-dealers, retail investors, and others on existing regulations and practices.[84] This obligation will require the SEC, for example, "to assess whether there were reliance interests, determine whether they were significant,

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[75] *Michigan v. EPA*, 135 S. Ct. 2699, 2707 (2015).

[76] 15 U.S.C. § 78c(f).

[77] 15 U.S.C. § 77b(b).

[78] *American Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 178 (D.C. Cir. 2010) (considering 15 U.S.C. § 77b(b)).

[79] *See id.* at 179; *see also Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011); *Chamber of Commerce of U.S. v. SEC*, 412 F.3d 133, 144 (D.C. Cir. 2005).

[80] *See supra* pp. 8-13.

[81] *Competitive Enter. Inst. v. National Highway Traffic Safety Admin.*, 956 F.2d 321, 323-324 (D.C. Cir. 1992).

[82] *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125 (2016).

[83] *Amerijet Int'l, Inc. v. Pistole*, 753 F.3d 1343, 1350 (D.C. Cir. 2014).

[84] *Encino Motorcars*, 136 S. Ct. at 2126.

and weigh any such interests against competing policy concerns."[85] Relatedly, if the SEC purports to "change[] prior policy" toward DEPs, it will be required to acknowledge the change and provide a "reasoned explanation" for it.[86] Firms such as Robinhood have invested substantially in bringing innovative products to retail investors in reliance on the existing regulatory framework. Retail investors, moreover, have benefited immensely from these practices and now rely on these practices and features. An abrupt about-face by the SEC in its regulatory approach to DEPs will need to account for these well-founded reliance interests.

The above discussion presents just a sampling of the substantive and procedural requirements to which the SEC will need to conform any rulemaking addressing DEPs. The bottom line is that additional regulation in this area will undoubtedly raise significant legal issues, require a robust record (including a rigorous assessment of the costs and benefits of regulatory action), and demand substantial engagement with stakeholders. A failure by the SEC to adhere to these principles will invite judicial vacatur of new regulation in this area.[87]

**D. The First Amendment Strictly Limits The SEC's Ability To Regulate Digital Engagement Practices Based On Their Communicative Content.**

Also among the "significant aspects of the problem" the SEC will need to consider are the First Amendment implications of any regulation in this area. Robinhood's services are popular and effective in large part because they provide truthful, relevant information about market activity in conjunction with accessible mechanisms for market participation. Its platform fosters a vibrant "marketplace of ideas," producing in the financial sector the same social goods of self-realization, public participation, and improved understanding that other marketplaces of ideas produce for political, cultural, and social issues. Many of the criticisms of consumer-focused trading platforms reflect an unjustified hostility toward retail trading, skepticism of the benefits of individual autonomy in financial decision-making, and unwarranted assumptions that "advised" or "guided" trading is more appropriate for retail investors. These critics effectively claim that it is wrong to make trading too easy or too attractive, discounting investors' ability to make decisions regarding their own interests and the benefits of doing so.

Although it is unclear what regulations the SEC may be considering, many types of regulations of digital engagement practices would raise serious questions under the First Amendment. Whether through words or other modes of communication such as animation and graphics, these practices convey ideas and information and thus constitute speech entitled to First Amendment protection. An

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[85] *Regents of the Univ. of Cal.*, 140 S. Ct. at 1913.

[86] *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 514-515 (2009).

[87] It should go without saying that the SEC will need to identify the source of its statutory authority to regulate DEPs in the manner that may ultimately be proposed and to ensure that the exercise of any regulatory authority conforms to the limits imposed on the agency by the text, structure, and purposes of its organic statutes. As a federal agency, the SEC "literally has no power to act … unless and until Congress confers power upon it." *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986). And it is axiomatic that "[r]egardless of how serious the problem an administrative agency seeks to address …, it may not exercise its authority 'in a manner that is inconsistent with the administrative structure that Congress enacted into law.'" *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 125-126 (2000). In issuing any NPRM, the SEC should take care to describe the source of its authority and to explain how the proposed regulations adhere to the relevant statutory framework.

effort to regulate digital engagement practices based on their communicative content would therefore face strict First Amendment scrutiny—which regulations rarely survive. The SEC may, of course, prevent the dissemination of false or misleading information. But the agency may not suppress ideas, opinions, or truthful information because it fears investors exposed to such expression will make decisions the SEC believes are not in their best interests. That is no less true simply because broker-dealer communications are, as discussed above, already regulated for certain purposes. *See Nat'l Ass'n of Mfrs. v. SEC*, 800 F.3d 518, 521 (D.C. Cir. 2015) (rejecting argument that SEC disclosure regulations can evade First Amendment scrutiny "because the United States is thick with laws forcing '[i]ssuers of securities' to 'make all sorts of disclosures about their products'"). As in other spheres, regulation in this area must respect the First Amendment principle "that information is not in itself harmful, that people will perceive their own interests if only they are well enough informed, and that the best means to that end is to open the channels of communication rather than to close them." *Sorrell v. IMS Health, Inc.*, 564 U.S. 552, 578 (2011).

*1. Digital Engagement Practices Are Fully Protected Speech.*

At the outset, there can be no real dispute that the digital engagement practices at issue in the Request implicate protected speech under the First Amendment. Many of these practices—as the SEC's own description of them makes clear—are expressly designed to convey ideas and information to investors. *See* 86 Fed. Reg. at 49,069 (discussing digital platforms that "present 'ideas'" to investors such as "curated lists" and "news headlines"); *id.* (discussing the use of "notifications" regarding, e.g., movements in stock prices); *id.* (discussing the provision of "additional features," such as "access to research reports, briefs, webcasts, and newspaper subscriptions"). Without question, the expression of ideas and "the creation and dissemination of information are speech within the meaning of the First Amendment." *Sorrell*, 564 U.S. at 570; *see also Bartnicki v. Vopper*, 532 U.S. 514, 527 (2001) ("if the acts of 'disclosing' and 'publishing' information do not constitute speech, it is hard to imagine what does").

So, too, are other features used by digital platforms such as animation and graphics that, although they may not present information in so many words, nonetheless convey protected ideas. Visual and auditory devices communicate *ideas*, e.g., that retail investors' participation in the financial markets is a good thing and that taking charge of one's financial affairs by learning to invest is an important achievement. Just as a painting or a symphony is entitled to no less First Amendment protection than a novel or a newspaper article, digital platforms do not lose First Amendment protection when they express ideas through "animation and graphics" or "visual cues." 86 Fed. Reg. at 49,069. Indeed, the very use of such features, which are ubiquitous on today's e-commerce and other digital platforms, itself conveys the message that investing in the financial markets is not an activity reserved for the wealthy, but one that should be broadly accessible to the masses. *See Brown v. Entm't Merchants Ass'n*, 564 U.S. 786, 790 (2011) (affording full First Amendment protection to video games, which "communicate ideas—and even social messages—through many familiar literary devices (such as characters, dialogue, plot, and music) and through features distinctive to the medium (such as players' interaction with the virtual world)").

Nor do digital engagement practices fall within the category the Supreme Court has referred to as "commercial speech." To the extent the "commercial speech" doctrine retains vitality,[88] it is a narrow exception generally reserved for commercial communications, like advertisements, that do "no more than propose a commercial transaction." *Edenfield v. Fane*, 507 U.S. 761, 767 (1993); *see also City of Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 423 (1993); *Bolger v. Youngs Drug Prods. Corp.*, 463 U.S. 60, 66 (1983). The practices at issue do not propose commercial transactions at all, let alone do "no more" than propose commercial transactions. Rather, they provide truthful information that investors can use to inform their investment decisions and enhance their investment experience. The mere fact that the speech concerns economic activity does not make it less worthy of First Amendment protection; nor does the fact that digital platforms are for-profit businesses that have economic incentives for communicating with their subscribers. *See Sorrell*, 564 U.S. at 567 ("While the burdened speech results from an economic motive, so too does a great deal of vital expression."). Were it otherwise, for-profit financial news services (and much else besides) would be commercial speech. That is not the law. And, in all events, even speech that is deemed "commercial speech" is still entitled to "substantial" First Amendment protection, *Bolger*, 463 U.S. at 68, requiring "heightened scrutiny," *Sorrell*, 564 U.S. at 571–72.

Finally, regulations of digital engagement practices cannot evade First Amendment scrutiny as purported regulations of "professional speech." Digital platforms like Robinhood—unlike, e.g., investment advisers—do not offer investment advice, let alone do so within the confines of a professional relationship of trust and confidence. *See Lowe v. SEC*, 472 U.S. 181, 228–29 (1985) (White, J., concurring) (discussing the government's latitude to regulate investment advisory services in light of the fiduciary relationship between investment advisers and their clients). They therefore are not "professionals" for First Amendment purposes. In any event, the Supreme Court has afforded lesser protection for "professional speech" in only two circumstances—when laws either (i) "require professionals to disclose factual, noncontroversial information in their 'commercial speech,'" or (ii) "regulate professional conduct, even though that conduct incidentally involves speech." *Nat'l Inst. of Family & Life Advocates v. Becerra*, 138 S. Ct. 2361, 2372 (2018). Neither circumstance is present here. As just explained, digital engagement practices involve fully protected speech, not commercial speech. And if the SEC sought to regulate how digital platforms use such practices to communicate with their customers, it would clearly be regulating speech, not conduct. *See Barr v. Am. Ass'n of Political Consultants*, 140 S. Ct. 2335, 2347 (2020) (holding that law restricting robocalls regulated speech, not conduct, because it "focuse[d] on whether the caller [was] *speaking* about a particular topic"); *Expressions Hair Design v. Schneiderman*, 137 S. Ct. 1144, 1151 (2017) (holding that, although a law regulating prices regulates conduct, a law regulating "how sellers may communicate their prices" regulates speech).

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[88] The extent to which the "commercial speech" doctrine survives as a distinct tier of First Amendment scrutiny is open to question, with the Supreme Court not having invoked the doctrine to uphold a commercial speech regulation in decades. *See* Martin H. Redish, *Commercial Speech and the Value of Free Expression*, Cato Inst. Pol'y Anal. No. 813, 2 (2017) (noting "it is difficult to find a Supreme Court decision upholding governmental suppression of truthful commercial speech in the last 25 years"); *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 523–28 (1996) (Thomas, J., concurring) (calling for strict scrutiny of laws suppressing truthful commercial speech).

### 2. *Many Regulations Of Digital Engagement Practices Could Be Subject To—And Would Likely Fail—Strict First Amendment Scrutiny.*

Because digital engagement practices constitute fully protected speech, efforts by the SEC to regulate them on the basis of their content or the viewpoints they express would likely trigger strict First Amendment scrutiny. Content- and viewpoint-based regulations of fully protected speech are "presumptively unconstitutional and may be justified only if the government proves that they are narrowly tailored to serve compelling state interests." *Nat'l Inst. of Family & Life Advocates*, 138 S. Ct. at 2371. Few regulations pass this "stringent standard," which "reflects the fundamental principle that governments have no power to restrict expression because of its message, its ideas, its subject matter, or its content." *Id.*; *see also Iancu v. Brunetti*, 139 S. Ct. 2294 (2019) (striking down as viewpoint discriminatory Lanham Act provision prohibiting registration of "immoral or scandalous" trademarks); *Reed v. Town of Gilbert*, 576 U.S. 155 (2015) (striking down as content discriminatory town sign code that applied different restrictions to different messages); *United States v. Playboy Entertainment Group, Inc.*, 529 U.S. 803, 818 (2000) ("It is rare that a regulation restricting speech because of its content will ever be permissible.").

Although the constitutionality of any regulation would depend on the specifics of the regulation and the record underlying it, heightened First Amendment review would impose real constraints on many types of regulation in this area. *First*, a regulation restricting digital engagement practices in an effort to prevent them from influencing investor behavior in ways the SEC disapproves would almost certainly be a content- or viewpoint-based restriction triggering strict scrutiny. For example, regulations restricting platforms' ability to send notifications or otherwise communicate information about, e.g., movements in stock prices or the activity of other investors would be content-based because they would turn on the subject matter of the speech. *See Barr*, 140 S. Ct. at 2346 (a law that disfavors speech on certain topics "is a content-based restriction on speech"); *Reed*, 576 U.S. at 169 ("a speech regulation targeted at specific subject matter is content based"). Similarly, a regulation restricting practices that convey the message that self-directed trading is a good thing would be viewpoint-based, reflecting a preference for "guided" investing. *See Iancu*, 139 S. Ct. at 2299 ("The government may not discriminate against speech based on the ideas or opinions it conveys.").

*Second*, the SEC could not shield its regulations from strict scrutiny by claiming that its purpose is to protect investors, not suppress ideas. "A law that is content based on its face is subject to strict scrutiny regardless of the government's benign motive, content-neutral justification, or lack of animus toward the ideas contained in the regulated speech." *Reed*, 576 U.S. at 165; *see also id.* at 166 ("an innocuous justification cannot transform a facially content-based law into one that is content neutral"). Moreover, the paternalistic notion that the government can suppress truthful speech to protect individuals from the lawful choices they might make if they heard it is "incompatible with the First Amendment." *Sorrell*, 564 U.S. at 577.

*Third*, the SEC would bear a heavy burden to demonstrate that there is "an actual problem in need of solving," i.e., that the purported harms it seeks to prevent are real and that there is a "direct causal link" between the practices the SEC seeks to regulate and the purported harms it seeks to prevent. *Brown*, 564 U.S. at 799. "This burden is not satisfied by mere speculation or conjecture," *Edenfield*, 507 U.S. at 770, or even by "predictive judgment" based on empirical studies, *Brown* 564 U.S. at 799. Rather, the SEC would be required to substantiate its assertions with evidence; and because the

SEC would bear the burden of proof and "the risk of uncertainty, ambiguous proof will not suffice." *Id.* at 799–800; *see id.* at 801 n.8 (concluding that empirical studies did not establish a causal link between violent video games and antisocial behavior "with the degree of certitude that strict scrutiny requires").

*Fourth*, in addition to establishing a compelling government interest, the SEC would be required to show that its regulations are "narrowly drawn to serve that interest," i.e., that "the curtailment of free speech [is] actually necessary to the solution." *Id.* at 799. To satisfy this requirement, the regulations would have to be "the least restrictive alternative that can be used to achieve" the SEC's asserted interests. *Ashcroft v. ACLU*, 542 U.S. 656, 666 (2004). That is an exacting standard that is rarely met, especially when the government's asserted interests could be achieved through more speech, rather than less speech. *See Citizens United v. FEC*, 558 U.S. 310, 361 (2010) ("it is our law and our tradition that more speech, not less, is the governing rule"); *Whitney v. California*, 274 U.S. 357, 377 (1927) (Brandeis, J., concurring) (when the government objects to speech, "the remedy to be applied is more speech, not enforced silence"). Conversely, a regulation that burdens some speech while leaving unrestricted other speech or practices that create the same problem will be struck down as underinclusive. *See Reed*, 576 U.S. at 172 ("[A] law cannot be regarded as protecting an interest of the highest order, and thus as justifying a restriction on truthful speech, when it leaves appreciable damage to that supposedly vital interest unprohibited."); *Brown*, 564 U.S. at 802 ("Underinclusiveness raises serious doubts about whether the government is in fact pursuing the interest it invokes, rather than disfavoring a particular speaker or viewpoint."). As the Supreme Court has often instructed, "[p]recision must be the touchstone when it comes to regulations of speech." *Nat'l Inst. of Family & Life Advocates*, 138 S. Ct. at 2372.

*Fifth*, as with other forms of underinclusiveness, the Supreme Court's "precedents are deeply skeptical of laws that distinguish among different speakers, allowing speech by some but not others," as such laws "run the risk that the State has left unburdened those speakers whose messages are in accord with its own views." *Id.* at 2378. Thus, regulations that target the speech of digital platforms without addressing more traditional forms of communication used by broker-dealers and financial advisers—such as financial publications that routinely publish lists or information about the most active stocks or other widely traded securities—are unlikely to survive First Amendment scrutiny. *See Sorrell*, 564 U.S. at 564 (striking down law that "disfavor[ed] specific speakers" by "preventing detailers—and only detailers—from communicating with physicians in an effective and informative manner"); *Reed*, 576 U.S. at 170 ("Because speech restrictions based on the identity of the speaker are all too often simply a means to control content, we have insisted that laws favoring some speakers over others demand strict scrutiny when the legislature's speaker preference reflects a content preference.").

*Finally*, rigorous First Amendment scrutiny would apply not only to a complete ban on particular forms of speech by digital platforms, but also to measures that burden such speech through regulations. "The distinction between laws burdening and laws banning speech is but a matter of degree," and "the Government's content-based burdens must satisfy the same rigorous scrutiny as its content-based bans." *Sorrell*, 564 U.S. at 565–66. "Lawmakers may no more silence unwanted speech by burdening its utterance than by censoring its content." *Id.* at 566.

In short, although much will depend on the specific nature of the regulations the SEC is considering, the First Amendment will likely present a substantial obstacle to any attempt by the SEC to regulate digital engagement practices because the SEC disapproves of the messages they convey or believes that investors will make unwise decisions if given truthful information.

* * * * *

We appreciate the opportunity to comment on the Request. Please contact the undersigned or Robinhood's Deputy General Counsel, Lucas Moskowitz, at [redacted] if you have any questions or comments.

Sincerely,

DocuSigned by:
David Dusseault
2FD230F46B54425...

David Dusseault
President
Robinhood Financial, LLC

**Exhibit A:**

**DEP Categories Identified by the SEC**

| ***SEC Identified DEP*** | ***Response*** |
|---|---|
| ***Social networking tools*** | Robinhood does not provide social forums within our app or our website where customers can "like," "follow" or "share" their investments with other customers; Robinhood does not offer a "chat" feature for customer-to-customer messaging; and Robinhood does not offer a "copy trading" feature. All engagement on our app and platform today is directly between Robinhood and its customers.<br><br>As part of the account creation process, Robinhood assigns investors a unique account profile identifier and allows customers to upload a picture to their application profile. However, all profile information is private and users are not permitted to share their Robinhood application profiles with other users. |
| ***Games, streaks and other contests with prize*** | Robinhood does not employ games that use interactive graphics to offer prizes for completing investing tasks.<br><br>Robinhood does offer customers free stock when a customer opens and funds a new account and for referring new customers. Customers may decline, and must opt in to accept the free stock before it is deposited in the customer's account. Robinhood also conducts sweepstakes for brand awareness and to promote customer loyalty. For example, Robinhood offered $500 to 200 sweepstakes winners who referred friends or signed up for a Robinhood account and linked their bank account, in the summer of 2021. No purchase was necessary to participate in the sweepstakes, and any customer or non-customer was also free to participate in the sweepstakes by using a mail-in entry, without making any referral or account application. |
| ***Points, badges, and leaderboards*** | We understand that some digital platforms may use points or similar "scorekeeping" related to trading activity. For example, some platforms offer "paper trading" (i.e., simulated trading) competitions that enable investors to practice trading without real money. Certain platforms also offer badges as visual markers of achievement as well as leaderboards to rank individuals based on investment performance-based criteria developed by the firm. Robinhood does not offer "paper trading" (i.e., simulated trading) competitions that enable investors to practice trading or other rankings or scorekeeping in connection with investment performance. We understand, however, that such competitions are not unique to online firms and have been offered by traditional "brick and mortar" broker-dealers. |

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| | Robinhood, however, does not host trading competitions, we do not maintain a "leaderboard," and we do not offer badges or visual markers of achievement. |
| ***Notifications*** | At Robinhood, notifications and alerts are generally configurable by customers. This means that customers may turn-off push notifications by going into the settings of their mobile device unless the notifications serve a regulatory purpose or relate to important account information. Robinhood has the ability to send notifications and alerts as (1) push notifications that appear on a customer's mobile device; (2) email communications; and (3) in-app messages. As stated above, push notifications and e-mail alerts are configurable by a customer to that customer's preferences. With the exception of certain notifications that serve a regulatory purpose or relate to important account information, a customer may opt out of receiving push notifications and e-mails in her app and/or on her phone. These notifications are provided for informational purposes and alert customers to important news regarding their accounts or investments. Examples of notifications include: the price of a stock the customer owns reaching a 52-week high or low or changing by 5% or 10%; suspicious activity in the customer's account; margin maintenance alerts or margin call warnings; options expiration reminders; upcoming dividend payments by companies who stock the customer owns; upcoming earnings announcements by companies whose securities the customer owns; and a friend whom the customer referred through the Stock Referral Program joining Robinhood.<br><br>Notifications and alerts are not new or novel. Market participants with significant assets have, for years, paid investment professionals to monitor these types of circumstances and provide real-time updates. The securities industry has used these notifications for decades and the securities regulators have been comfortable with it for decades. *See* FINRA Regulatory Notice 11-02 (Oct. 7, 2011). Digital platform notifications are not only faster and more efficient than other forms of communication, but also more fair and equitable because they provide information to all interested customers at the same time. This is an improvement over the days when brokers would call their customers and some customers received information much earlier than others – which in turn creates information disparity and may result in unfair advantages for some customers. |
| ***Celebrations for trading*** | Robinhood does celebrate certain milestone events such as a customer's opening an account, funding an account, and a first investment. These digital "celebrations" may take the form of animation and graphics. In the past, Robinhood used animated confetti – which is a widely-recognized symbol of celebration – to |

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| | acknowledge milestones. Now, we use a different form of animation to mark milestones in our customers' financial journeys. U.S. securities regulators traditionally have viewed retail investor participation in the securities markets as important because of the opportunities for wealth accumulation that accompanies this participation. *Cf.* https://www.finra.org/media-center/newsreleases/2021/finra-launches-educational-initiative-aimed-newer-investors. Robinhood's acknowledgment of investors' milestones is consistent with these views. |
| ***Visual cues*** | As with most broker-dealers, Robinhood's application contains visual cues such as objects, pictures, symbols and words. Visual cues are not new or novel. Every broker-dealer or investment adviser's website, storefront, print ad, desk inside an affiliated bank, TV commercial, and news segment is a visual cue that increases brand awareness and may trigger further engagement by a customer with that entity. U.S. securities regulators traditionally have endorsed the use of "visually engaging and effective designs" to appeal to retail customers and make information more accessible, noting that "[t]here is also empirical evidence that visualization improves individual perception of information." *Cf.* Form CRS, 84 Fed. Reg. 33492, 33581 (Jul. 12, 2019). |
| ***Ideas presented at order placement and other curated lists or features*** | Robinhood does not present ideas at order placement. Robinhood does not recommend clients purchase any particular securities or engage in any investment strategies. Robinhood does not send client-specific investment recommendations based on their investment profile, demographic information, or geographic information confirm.<br><br>Robinhood does offer customers the ability to create their own "Watch Lists" or other lists of securities of interest. Based on these customer-generated lists, Robinhood provides customers with news updates regarding the stocks the customer has elected to add to the list. Customers may choose not to create any custom lists. When a customer opens an account, Robinhood pre-populates a "Watch List" that the customer can change or eliminate. The same default "Watch List" is displayed to all customers. Robinhood also generates 5 lists of securities based on Robinhood customer data, including the "100 Most Popular" listing the stocks that are most commonly held by Robinhood customers. Robinhood-generated lists generated are based on objective standards and are not personalized to the customer; the same content is displayed to every customer.<br><br>Additionally, Robinhood offers lists generated by an interdependent research firm, Morningstar, Inc., which categorizes and lists |

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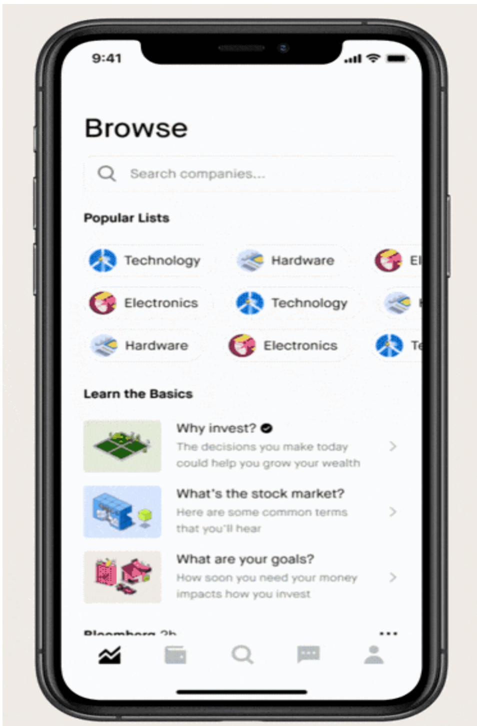
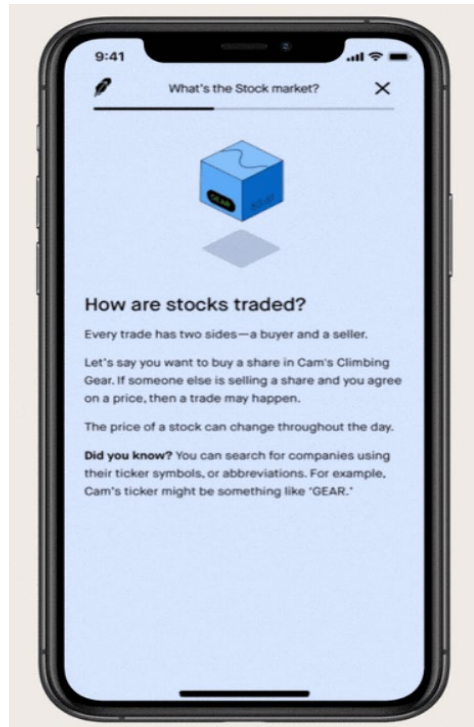
| | securities by sector (e.g., the technology list includes 894 individual stocks).<br><br>By providing information categorized in these ways, Robinhood empowers its customers to assimilate and synthesize information about thousands of different publicly-traded companies without paying the fees/commissions associated with this type of data in more traditional advisory and brokerage models.<br><br>Notably, the securities industry has provided customers with lists of issuers by category (e.g., most actively traded or current buy ratings), trade ideas, and research reports for decades, and FINRA has confirmed that providing customers with tools to screen through a wide universe of securities, as well as lists of securities meeting broad, objective criteria does not constitute a recommendation. *See* FINRA Regulatory Notice 11-02 (Oct. 7, 2011). |
| ***Subscriptions and membership tiers*** | At Robinhood, the "upgraded" membership tier is an upgrade to Gold, which costs $5 per month and provides an investor with advanced research, instant deposits, market data, and the first $1,000 in margin interest. Robinhood offers customers the opportunity to try one month of Gold membership for free. Customers can cancel their Gold membership at any time (including after their trial period has ended).<br><br>Subscription services at broker-dealers are not new. Broker-dealers have historically offered services such as research and access to certain market data for a subscription fee. Subscription services provide customers the option to pay for additional products and services, and tailor their investment experience to their own preferences. |
| ***Chatbots*** | Robinhood uses automated chats within its in-app messaging function when customers request certain information. For example, through the in-app messaging system, customers may cancel an order or request additional information. A chatbot is technology that simulates human conversation. Conversations with customers have always existed and when the industry leverages technology to communicate with customers, the customer can remain informed and empowered to ask questions without increasing the cost of brokerage services by requiring human interaction. |

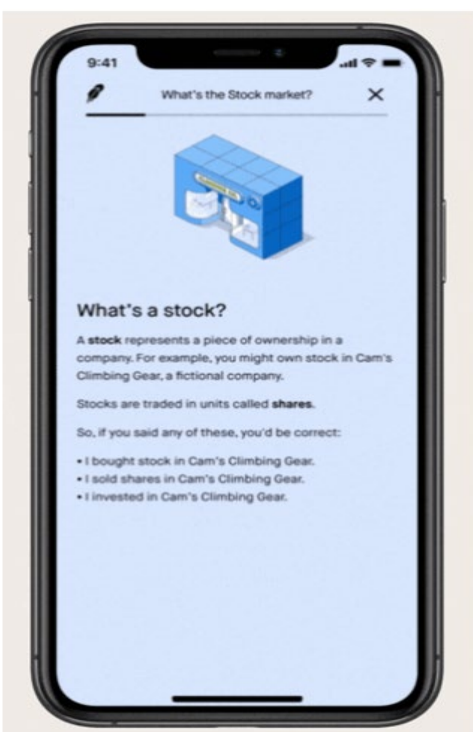
# Exhibit B:

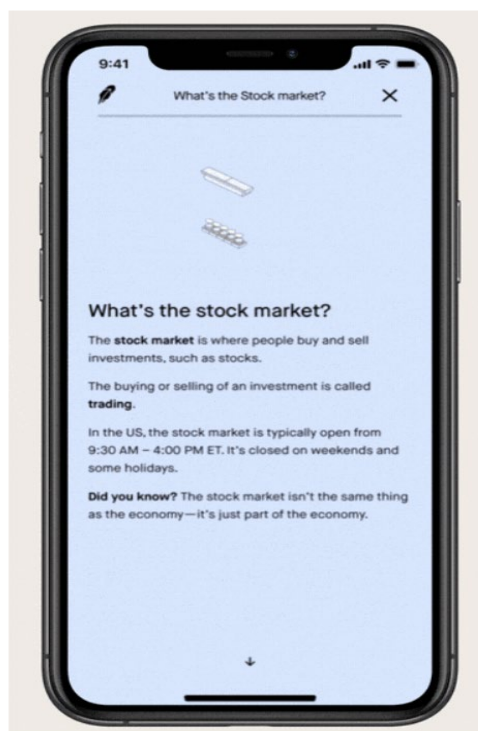
## Example Digital Communications and Features

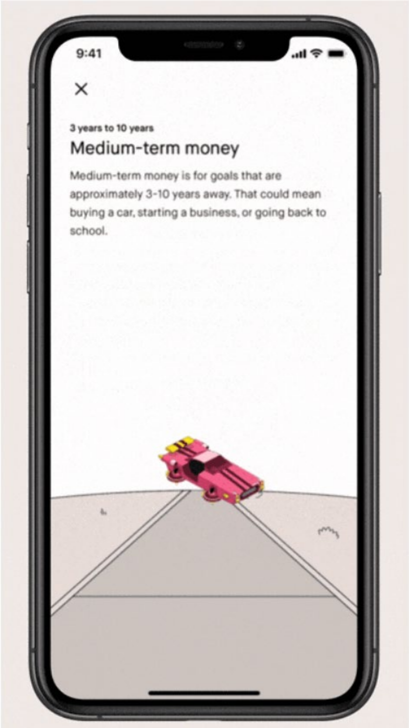
*Educational Materials*

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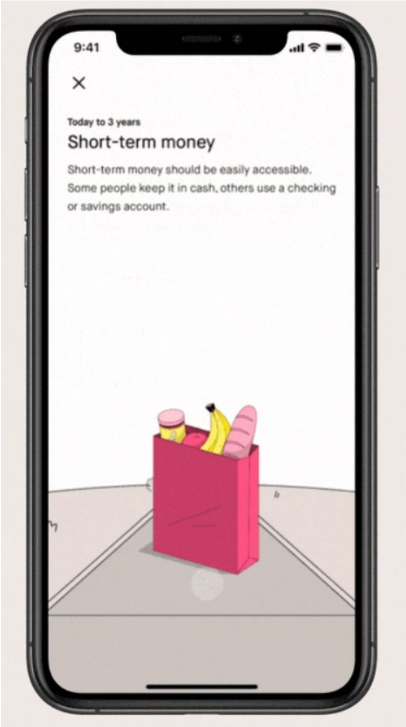
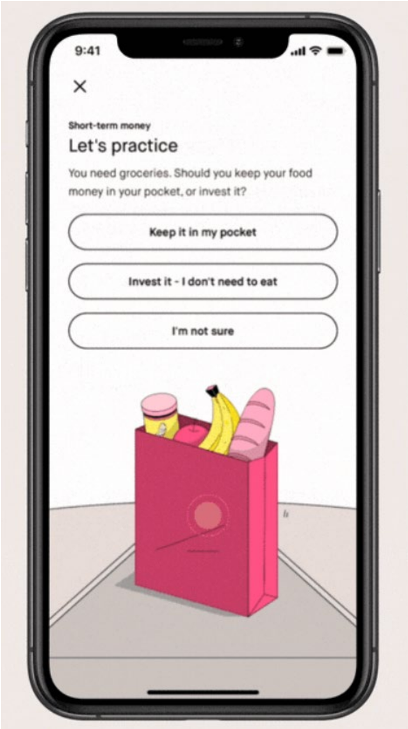
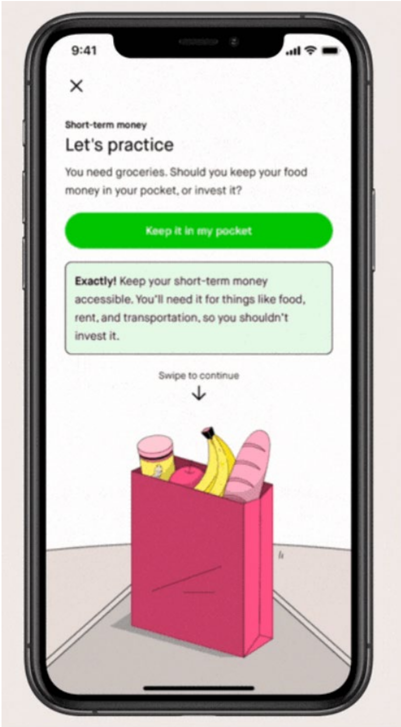
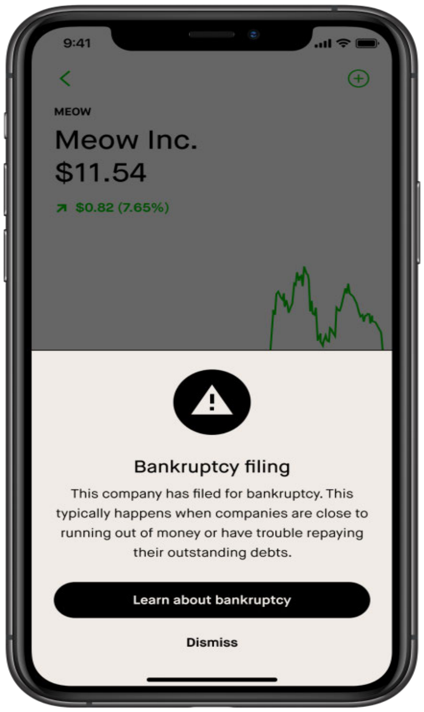
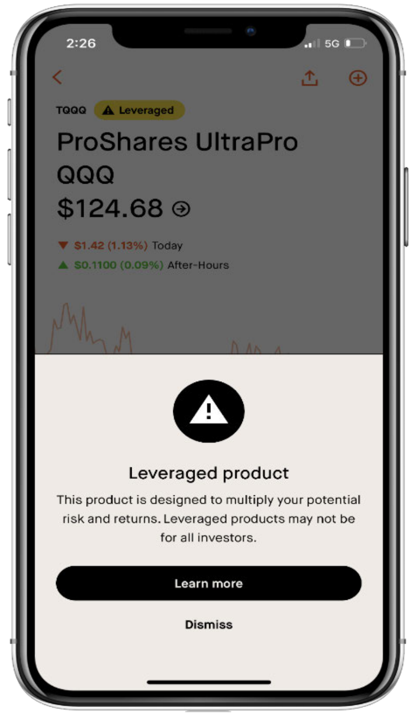
3 years to 10 years
Medium-term money
Medium-term money is for goals that are approximately 3-10 years away. That could mean buying a car, starting a business, or going back to school.


9:41
Today to 3 years
Short-term money
Short-term money should be easily accessible. Some people keep it in cash, others use a checking or savings account.

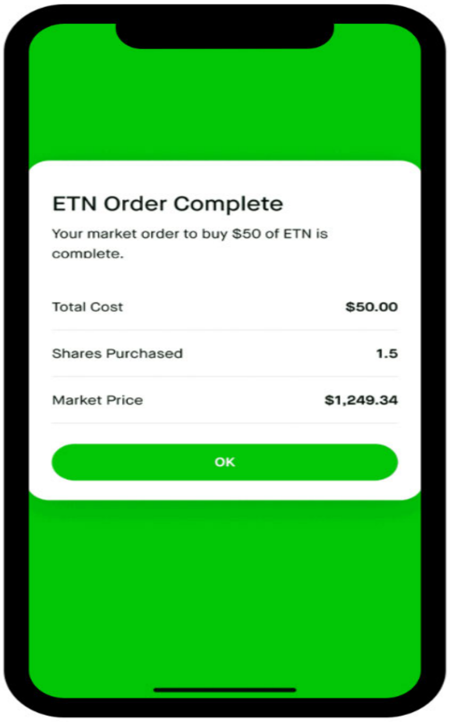

9:41
Short-term money
Let's practice
You need groceries. Should you keep your food money in your pocket, or invest it?
Keep it in my pocket
Invest it - I don't need to eat
I'm not sure

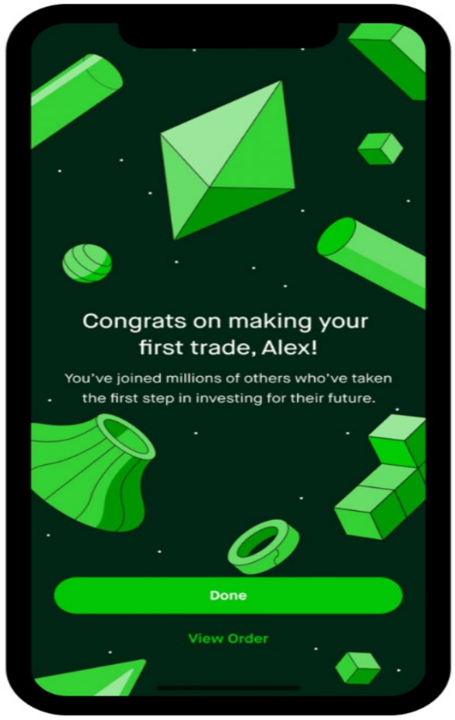

9:41
Short-term money
Let's practice
You need groceries. Should you keep your food money in your pocket, or invest it?
Keep it in my pocket
Exactly! Keep your short-term money accessible. You'll need it for things like food, rent, and transportation, so you shouldn't invest it.
Swipe to continue

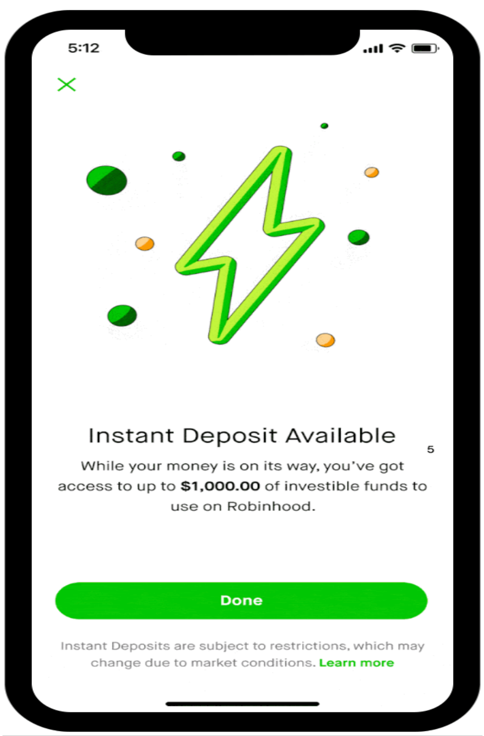

9:41
MEOW
Meow Inc.
$11.54
$0.82 (7.65%)
Bankruptcy filing
This company has filed for bankruptcy. This typically happens when companies are close to running out of money or have trouble repaying their outstanding debts.
Learn about bankruptcy
Dismiss

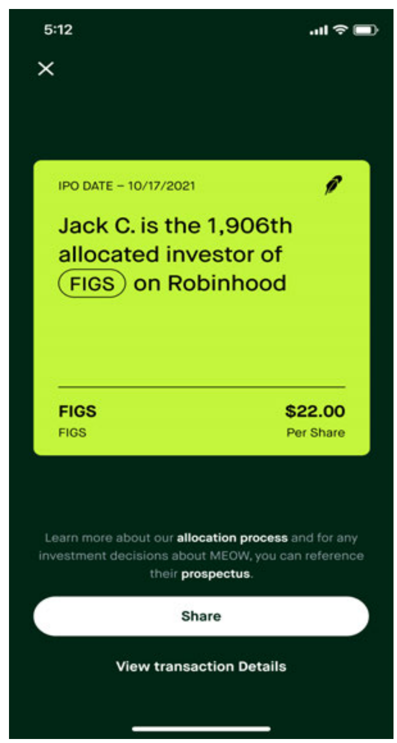

2:26
5G
TQQQ
Leveraged
ProShares UltraPro QQQ
$124.68
$1.42 (1.13%) Today
$0.1100 (0.09%) After-Hours
Leveraged product
This product is designed to multiply your potential risk and returns. Leveraged products may not be for all investors.
Learn more
Dismiss

*Celebrations*



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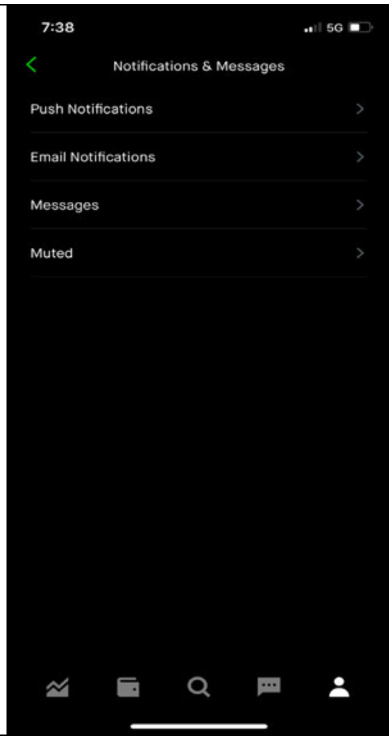
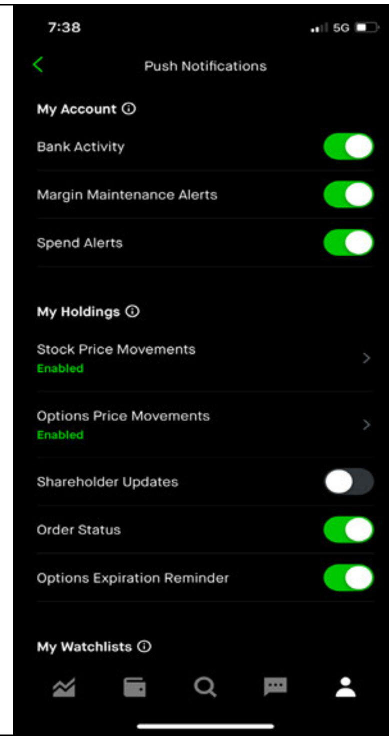
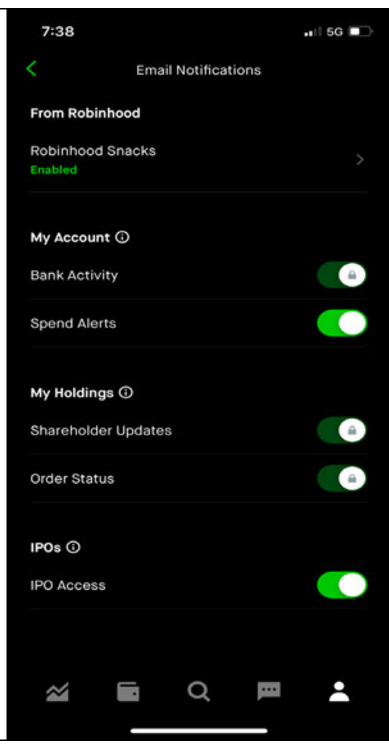
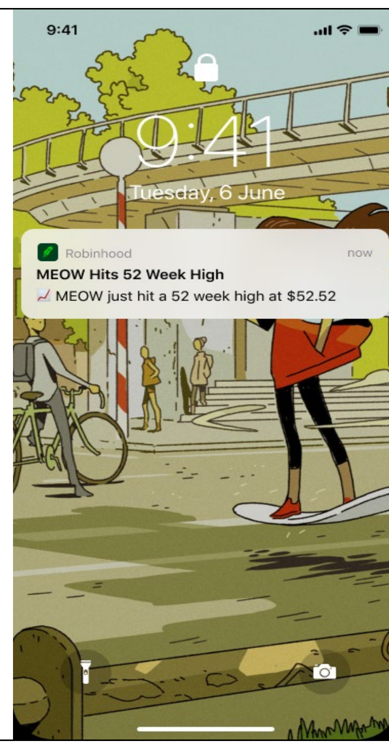
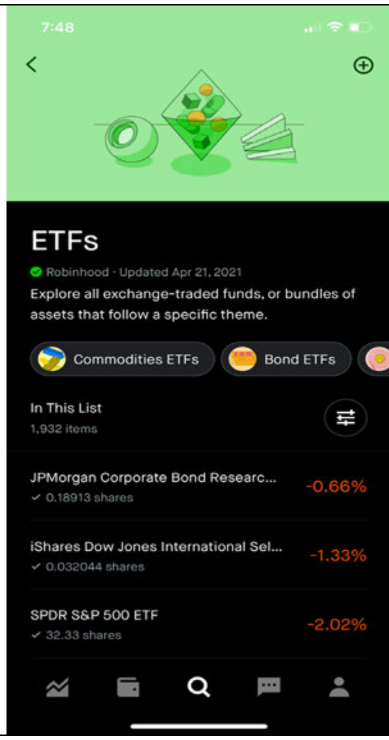


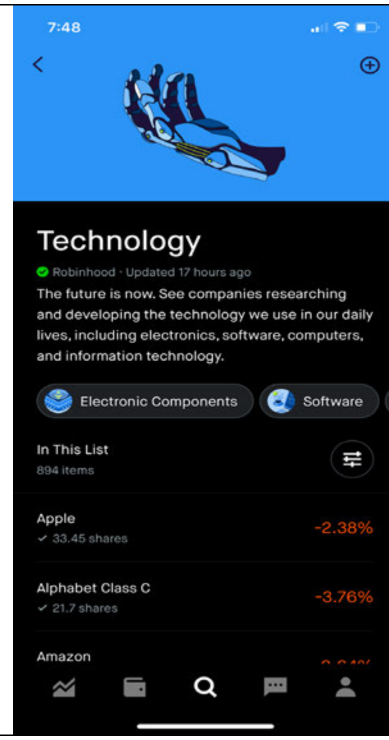



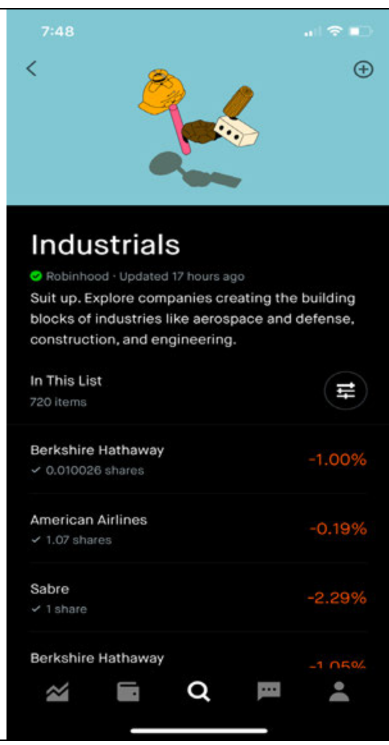



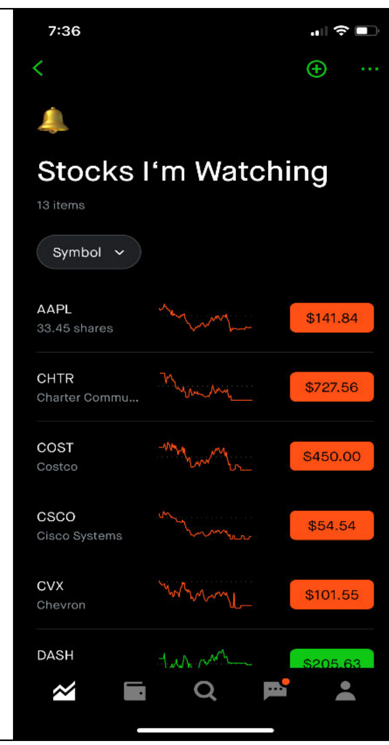



*Lists*


7:48
ETFs
Robinhood · Updated Apr 21, 2021
Explore all exchange-traded funds, or bundles of assets that follow a specific theme.
Commodities ETFs
Bond ETFs
In This List
1,932 items
JPMorgan Corporate Bond Researc...
0.18913 shares
-0.66%
iShares Dow Jones International Sel...
0.032044 shares
-1.33%
SPDR S&P 500 ETF
32.33 shares
-2.02%


7:48
Technology
Robinhood · Updated 17 hours ago
The future is now. See companies researching and developing the technology we use in our daily lives, including electronics, software, computers, and information technology.
Electronic Components
Software
In This List
894 items
Apple
33.45 shares
-2.38%
Alphabet Class C
21.7 shares
-3.76%
Amazon


7:48
Industrials
Robinhood · Updated 17 hours ago
Suit up. Explore companies creating the building blocks of industries like aerospace and defense, construction, and engineering.
In This List
720 items
Berkshire Hathaway
0.010026 shares
-1.00%
American Airlines
1.07 shares
-0.19%
Sabre
1 share
-2.29%
Berkshire Hathaway


7:36
Stocks I'm Watching
13 items
Symbol
AAPL
33.45 shares
$141.84
CHTR
Charter Commu...
$727.56
COST
Costco
$450.00
CSCO
Cisco Systems
$54.54
CVX
Chevron
$101.55
DASH

# Exhibit B

Robinhood

85 Willow Road
Menlo Park, CA 94025
robinhood.com

**October 10, 2023**

Via Electronic Mail (rule-comments@sec.gov)

Vanessa A. Countryman, Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

**Re: File No. S7-12-23: Conflicts of Interest Associated with the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers**

Dear Ms. Countryman,

Robinhood Financial LLC[1] ("Robinhood") submits this letter in response to the U.S. Securities and Exchange Commission's ("Commission" or "SEC") recently proposed rules under the Securities Exchange Act of 1934 ("Exchange Act") and Investment Advisers Act of 1940 ("Advisers Act") intended to address theoretical conflicts of interest related to the use of "predictive data analytics" by broker-dealers and investment advisers (the "Proposal").[2] Robinhood incorporates by reference its comment letter submitted in response to the Commission's 2021 Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology to Develop and Provide Investment Advice ("DEP Request").[3]

Robinhood's mission is to democratize finance for all, regardless of a customer's background, income, or wealth. There is a large investment and wealth gap in the United States, which has created a divide in our country between the "haves" and the "have nots." Robinhood was founded to close this gap with its accessible product offering and user-friendly mobile application, which rely on technology to remove traditional barriers to investing and empower investors so that they can take control of their financial futures.

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[1] Robinhood Financial LLC, a FINRA-member broker-dealer, is a wholly owned subsidiary of Robinhood Markets, Inc.

[2] Conflicts of Interest Associated with the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers, 88 Fed. Reg. 53,960 (Aug. 9, 2023) ("Proposing Release").

[3] *See* Letter from David Dusseault, President, Robinhood Financial LLC, to Vanessa A. Countryman, Secretary, SEC (Oct. 1, 2021), https://www.sec.gov/comments/s7-10-21/s71021-9316498-260092.pdf; *see also* DEP Request, 86 Fed. Reg. 49,067 (Sept. 1, 2021).

Using technology to open the markets to retail investors from all backgrounds is central to our mission. Through our mobile app and website, Robinhood demystifies investing by providing free educational resources, financial literature, and user-directed subscriptions to news updates and information regarding securities in investors' portfolios. Because customers have 24/7 access to these tools and information, they have the freedom to consider and make decisions on their own schedule and time frame. In addition, Robinhood makes trading more accessible by eliminating account minimums and trading commissions and offering investors IPO access, fractional trading, and the first IRA with a match, no employer necessary. Using our mobile app, our customers can engage with their investments and access capital markets as they plan for their financial well-being and their futures. Engagement in this context is good; the more retail customers are involved in their finances, paying attention to their assets, and learning about investing, the better equipped they are to achieve their financial goals.

We are deeply concerned that the SEC's misinformed Proposal will jeopardize the progress we and the industry have made in making U.S. markets more diverse and accessible to everyone. The SEC's Proposal starts from the apocryphal premise that broker-dealers' and investment advisers' use of technology is inherently conflicted and necessarily causes investor harm. The Proposal then places such onerous burdens and costs on broker-dealers and investment advisers (collectively, "firms") that use technology that—by the SEC's own admission—some firms will stop providing certain (maybe most) technologies to customers altogether.

Disregarding the many benefits that technology provides to investors and the marketplace,[4] the Proposal's anti-technology, regressive approach appears primarily based on a false narrative regarding the so-called "meme stock" events in early 2021.

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[4] *See, e.g.*, SEC, *Report to the Congress: The Impact of Recent Technological Advances on the Securities Markets*, Executive Summary (Nov. 26, 1997), https://www.sec.gov/news/studies/techrp97.htm (During the dawn of the Internet Age, noting that "[t]he Commission is mindful of the benefits of increasing use of new technologies for investors and the markets, and has encouraged experimentation and innovation by adopting flexible interpretations of the federal securities laws[,]" and that "[t]he Commission also has adopted rules that permit markets and market participants to make use of technology, and has modified other rules or interpretive positions that might conflict with technological innovations."); Conference Report on H.R. 3005, National Securities Markets Improvement Act of 1996 (Oct. 21, 1996) (In enacting the SEC's general exemptive authority under Section 28 of the Securities Act and Section 36 of the Exchange Act, which permit the SEC to grant exemptions from the requirements of such Acts as "necessary or appropriate in the public interest," one Congressman highlighted that the "public interest" included "the promotion of responsible financial innovation."). *See also* Judy T. Lin et al., *Investors in the United States: The Changing Landscape: A Report of the FINRA Foundation National Financial Capability Study* (Dec. 2022), https://www.finrafoundation.org/sites/finrafoundation/files/NFCS-Investor-Report-Changing-Landscape.pdf.

While certain SEC officials persist in using early 2021's trading in GameStop Corp. stock and the findings of the GameStop Report[5] as a boogeyman to attack retail brokers that use technology to interact with investors,[6] we and others who actually know the markets continue to reject the theory that so-called "digital engagement practices" in any way caused GameStop to experience volatile trading, and we reject today that such market events had anything to do with predictive data analytics or similar technologies that the Proposal would regulate.[7] The facts, and the GameStop Report itself, simply do not support such a conspiracy theory.[8] Like most market participants, Robinhood knows that conspiracy theories damage investor trust and confidence in our markets. And to the extent that the SEC is concerned about certain technologies being used in a manner that directly or indirectly causes a substantial number of retail investors to trade large volumes of securities in a short period of time, the SEC has failed both to substantiate this concern and to demonstrate how the Proposal would address this concern. Among other things, the SEC has failed to provide a single shred of real evidence that: (1) broker-dealers or investment advisers are using technology in a manner that would cause problematic trading at all, let alone at a level significant enough to justify further regulation, and (2) firms' customers are actually engaged in such trading. The responses to the SEC's DEP Request also do not support the theory that firms are using technology in a manner that causes or promotes problematic trading by retail investors. As we stated in our response to the DEP Request, Robinhood does not use technology in that manner.

Robinhood recognizes the promise that technology—from the most basic spreadsheet to emerging artificial intelligence, natural language processing, and

[5] SEC Staff Report, *Equity and Options Market Structure Conditions in Early 2021* at 2 (Oct. 14, 2021), https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf ("GameStop Report") (drawing unsupported normative conclusions regarding how retail traders "might trade more frequently" due to no commission trading and so-called "digital engagement practices" of broker-dealers).

[6] *See, e.g.*, Gary Gensler, Chair, SEC, *Testimony Before the House Committee on Financial Services* (May 6, 2021), https://www.sec.gov/news/testimony/gensler-testimony-20210505.

[7] GameStop Report at 2 (The SEC Staff itself recognized that "these features are not necessarily the cause of the meme stock volatility.").

[8] The volatile trading in GameStop was caused by a unique confluence of factors, including increased retail investor participation in the stock market, which the SEC and SEC officials are now quick to malign and ascribe to the use of digital engagement practices of broker-dealers without consideration of other significant contributing factors relating to those events or the benefits of retail investor market participation. Notably, the GameStop Report merely recommended that game-like features be studied, which the SEC did not do prior to publishing the Proposal. *See id*. at 15-17 (identifying potential contributing factors, such as increased individual market participation, large price fluctuations and short interest in GameStop stock, and social and mainstream media buzz about GameStop, as well as "underlying causes of the meme stock phenomenon that are unrelated to market structure are a subject of speculation that is beyond the scope of this report.").

other advanced technologies—holds for the future of investing. Robinhood also recognizes the importance of developing and implementing these technologies in a responsible and regulated manner, consistent with the full panoply of SEC and FINRA rules that already apply to protect investors and the markets, including rules that specifically focus on investor interactions. Instead of meaningfully enhancing the existing regulatory framework, the SEC would simply displace it with a regulatory land grab that would result in its overseeing nearly all uses (or potential uses) of any mode of technology by broker-dealers and investment advisers that may occur in interactions with investors—from a simple calculator, Excel spreadsheet, or email to a quantum computer and advanced artificial intelligence.[9] Through this Proposal, the SEC would also impose an unsupported new uniform standard of conduct on any retail broker-dealer and any investment adviser that uses technology to interact with its customers, effectively overriding years of study and analysis that led to the Commission's Regulation Best Interest ("Regulation Best Interest" or "Reg BI") and its Interpretation Regarding Standard of Conduct for Investment Advisers ("Fiduciary Interpretation").[10] The SEC seeks to justify this broad expansion of its authority by speculating about the potential, theoretical, and future harm that technology might cause, without identifying any actual harm that its Proposal would address. And along the way, the SEC confesses its belief that retail investors—millions of Americans working hard to improve their financial positions—are too stupid to understand basic customer disclosures.[11]

The SEC's approach to regulation in the Proposal is extreme and out of step with modern markets and the Biden Administration's approach to innovation and technology.[12] The Proposal also raises significant constitutional issues and vastly exceeds the authority given the SEC by Congress. It is not only contrary to decades of securities law precedent using disclosure to address conflicts of interest, but it is also contrary to the SEC's own mission to protect investors, facilitate capital formation,

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[9] *See* Proposing Release, 88 Fed. Reg. at 53,973-74.

[10] Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 Fed. Reg. 33,318 (July 12, 2019) (codified at 17 C.F.R. § 240.15l-1); Fiduciary Interpretation, 84 Fed. Reg. 33,669 (July 12, 2019).

[11] *See* Proposing Release, 88 Fed. Reg. at 53,967. *See also id*. at 53,998 ("These conflicts of interest are exacerbated by firms' use of certain covered technologies because the technologies that firms use may be complex and opaque to investors, who may not have the knowledge or time to understand how firms' use of these technologies may generate conflicts of interest in their interactions with investors.").

[12] For example, a key piece of President Biden's Investing in America agenda is the development of regional technology and innovation hubs across the United States. *See* Press Release, U.S. Econ. Dev. Admin., *Biden-Harris Administration's Tech Hubs Competition Applications Show Nationwide Excitement for Investing in America's Technological Future* (Aug. 30, 2023), https://www.eda.gov/news/press-release/2023/08/30/biden-harris-administrations-tech-hubs-competition-applications-show.

promote competition, and maintain fair, orderly, and efficient markets. In short, the Proposal is vague and overbroad, excessively burdensome, and overall bad policy that would harm not only broker-dealers and investment advisers, but also the markets in which they operate and, most importantly, the investors they serve.

**EXECUTIVE SUMMARY**

The Commission's Proposal would create new Rule 15l-2 under the Exchange Act and Rule 211(h)(2)-4 under the Advisers Act. These rules would be adopted under the SEC's statutory authority to "examine and *where appropriate*" prohibit or restrict "*certain* … conflicts of interest… *contrary to the public interest and the protection of investors.*"[13]

In reality, the proposed rules represent an unprecedented expansion of the SEC's role and far exceed this modest statutory authority.[14] The Proposal seeks to impose a framework that would regulate almost *any use* of almost *any technology* by investment advisers and retail broker-dealers in almost *any interaction* with their customers—regardless of whether doing so is appropriate or necessary for the protection of investors. There is no principled limitation on the so-called "covered technology" that the SEC seeks to control—the SEC would regulate everything from mundane forms of technology, such as spreadsheets, emails and graphic design (which have been widely used across industries for decades), to the most sophisticated algorithms used by firms.[15] The SEC would impose excessive burdens and costs on firms that use this covered technology to interact with investors—including technology that investors specifically seek out for their own purposes. For example, if a broker-dealer provides news updates regarding stocks in a customer's portfolio, even at the customer's request and for free, that would be "covered technology" subject to costly regulation. So too would a website that allows users to self-select and view or download financial literature from a database. The proposed rules would impose costly regulation on even these simple technological tools that are unquestionably good for the investing public.

The breadth of the rule's application and the excessive costs and burdens that would apply to firms' use of technology cannot be overstated. First, firms would be required to survey and identify *every* individual technology that could be a "covered

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[13] 15 U.S.C. §§ 78o(l)(2)80b–11(h)(2) (emphasis added). *See* Proposing Release, 88 Fed. Reg. at 53,971.

[14] This concern is heightened because the authority the SEC is relying on is currently pending court review. *Petition for Review, Nat'l Ass'n of Private Priv. Fund Managers v. SEC*, No. 23-60471 (5th Cir. Sept. 1, 2023), ECF No. 1-1.

[15] The proposed rules broadly define "covered technology" as "an analytical, technological, or computational function, algorithm, model, correlation matrix, or similar method or process that optimizes for, predicts, guides, forecasts, or directs investment-related behaviors or outcomes." Proposed Rules 15l-2(a; 211(h)(2)-4(a); Proposing Release, 88 Fed. Reg. at 54,021-22, 54,023.).

technology." This could capture everything that broadly relates to securities and investments.

Next, firms would be required to identify whether the technology is used or "potentially could be used" in an "investor interaction." Again, this includes virtually every contact with an investor—both direct and indirect—from emails to phone calls to in-person meetings, to simply hosting a website or operating a mobile app or providing investors with tools to get market updates. Then, firms would be required to identify if a "conflict of interest" exists for the technology. Again, effectively every use of technology would be "conflicted" because contrary to the conventional understanding of "conflicts of interest," the SEC has stated that "[c]onsideration of *any* firm interest would be sufficient for a conflict of interest to exist" under the proposed rules.[16]

But the burdens do not stop there. After a firm has identified almost every piece of technology that it uses in almost any communication—directly or indirectly—with investors, it would be obligated to undertake a series of laborious, manually intensive tasks *for each spreadsheet, automated email, calculator, web page, and every other piece of covered technology*: (1) evaluate the technology (including testing) to identify any actual use *or potential use* of the technology that might take into consideration *any* firm interest; (2) determine whether this "conflict of interest" places the firm's or its associated persons' interests ahead of investors; (3) eliminate or neutralize the effect of any such conflict of interest; and (4) repeat steps 1-3 on a periodic basis and every time there is a material change to the technology. Firms would need to have detailed descriptions and written policies and procedures for identifying covered technology that could be used in investor interactions, identifying conflicts, and neutralizing or eliminating conflicts. They would need to conduct annual reviews of these policies and create new, highly detailed books and records of *each piece of covered technology* to document their compliance.

Not only are these tasks extraordinarily burdensome and daunting, but in some cases they would be "impossible"—as the SEC itself even admits in the Proposal.[17] Even when not "impossible," the SEC acknowledges that "the requirement to identify conflicts of interest in a technology could dissuade firms from using certain technologies when it is too difficult or costly to adequately evaluate the use of the covered technology, identify a conflict of interest, or determine whether they place the firm's or an associated person's interest ahead of an investor's."[18]

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[16] Proposing Release, 88 Fed. Reg. at 53,985 (emphasis included).

[17] *See id*. at 53,978 ("In certain cases, it may be difficult or impossible to evaluate a particular covered technology or identify any conflict of interest associated with its use or potential use within the meaning of the proposed rules.").

[18] *Id*. at 54,010-11.

Ultimately the costs will be borne by investors.[19] As the SEC admits, "[f]irms might pass the cost of the requirements along to investors through higher fees, commissions, or other methods" and "[i]nvestors would lose the benefit of such technologies if firms determine that the process of eliminating, or neutralizing the effect of, conflicts is too difficult, costly, or uncertain to succeed."[20] Given the breadth of "covered technology" and "conflict of interest," this means that even free educational tools, resources, and information, including customer-requested updates about their portfolio or the market, are susceptible to being eliminated because of the costs and regulatory burdens imposed by this Proposal.

And for what benefit and whose benefit? One of the primary potential benefits that the SEC identifies is that the new written documentation and recordkeeping requirements "would serve to aid the examinations staff."[21] Stated differently, the SEC is imposing massive new burdens and costs on the industry and investors for its own convenience.

Given the significant substantive and process concerns with the proposed rulemaking, we urge the Commission not to move forward with the Proposal.

**As discussed more fully below in Section I, the Proposal is arbitrary and capricious**. The SEC has not demonstrated a need for placing unprecedented regulatory burdens on firms' use of technology. The SEC also has provided no evidence that there is any actual harm caused by "covered technology" that would be addressed by its Proposal and that cannot be addressed by existing regulation. There also is no evidentiary support for the Proposal's radical requirement to "eliminate or neutralize" conflicts in lieu of addressing them through disclosure, which remains permissible and, in many instances, is prescribed under the federal securities laws to address other conflicts of interest. The lack of evidentiary support for the Proposal is not surprising given that the SEC failed to conduct the necessary analysis or fact gathering that is required for rulemaking.

**As discussed in Section II, the Proposal is fatally flawed because the SEC has failed to conduct any credible cost-benefit analysis**. In particular, the SEC has not gathered the requisite information to conduct a serious cost quantification and analysis and, instead, offers a speculative and incomplete assessment. There is limited discussion

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[19] The costs facing retail investors only would be compounded if the SEC's equity market structure proposals are adopted; however, the SEC has made no attempt to reconcile how those proposals would interact with this one or to assess the cumulative effects on retail investors or the industry overall. *See* Disclosure of Order Execution Information, 88 Fed. Reg. 3,786 (Jan. 20, 2023); Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, 87 Fed. Reg. 80,266 (Dec. 29, 2022); Order Competition Rule, 88 Fed. Reg. 128 (Jan. 3, 2023); Regulation Best Execution, 88 Fed. Reg. 5,440 (Jan. 27, 2023).

[20] Proposing Release, 88 Fed. Reg. at 54,010-11.

[21] *Id.* at 54,006.

of the benefits technology provides to investors today that could be impacted by the Proposal. And for the few costs that it does quantify, the SEC greatly underestimates the cost of compliance. At the same time, the SEC has failed to quantify and identify any clear benefits to the Proposal that could offset the Proposal's significant costs. Finally, the SEC has failed to consider the sufficiency of existing regulation in its cost-benefit analysis. Specifically, the SEC has failed to identify any problems relating to the use of covered technology that could not be addressed by existing SEC and FINRA regulations.

**As discussed in Section III, the SEC has unlawfully exceeded its statutory authority with this Proposal.** The Proposal would restrict nearly every aspect of a modern customer-facing securities business, presenting numerous questions about the SEC's authority to promulgate such a rule. The SEC seeks to expand its statutory authority beyond any reasonable reading of the statutory provisions it relies on, Section 15(l)(2) of the Exchange Act and Section 211(h) of the Advisers Act. The Proposal also violates the First Amendment because it improperly seeks to regulate free speech. The SEC's entire Proposal is based on the false premise that technology is inherently and irrevocably conflicted when used by broker-dealers and investment advisers to interact with investors. While regulators may prevent the dissemination of false or misleading information (and already have tools to do that), the SEC may not suppress ideas, opinions, or truthful information because it fears investors exposed to such expression will make decisions that the SEC believes are not in their best interests.

**Finally, as discussed in Section IV, the SEC should withdraw the Proposal because it is bad policy and unlawful for a multitude of other reasons.** As a threshold matter, the Proposal cannot be squared with the SEC's recently adopted Reg BI or the SEC's longstanding tradition of relying on a disclosure-based framework to address conflicts of interest for broker-dealers. The Proposal is also bad policy because it would disempower investors and is blatantly anti-technology and anti-innovation. It would indiscriminately and broadly regulate and restrict communications because of the medium through which they are delivered. And, fatally, the Proposal is unlawful and inconsistent with the SEC's rulemaking mandate because it will reduce efficiency, stifle competition, and deter capital formation.

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## I. The Proposal Is Arbitrary And Capricious Because The SEC Has Not Demonstrated A Need For Placing Unprecedented Regulatory Burdens On Firms' Use Of Technology.

The Proposal represents one of the most radical, unprecedented rulemaking initiatives in the SEC's history (or that of any other federal regulator for that matter). Based on an unsubstantiated theory that investment technology is rife with treacherous conflicts of interest, the SEC seeks to impose an unnecessarily expansive framework that would regulate almost *any use* of technology by retail broker-dealers and investment advisers in almost every interaction they have with investors, effectively creating a uniform, heightened standard of conduct for firms that use technology, i.e., virtually all firms today. The Proposal would regulate all "covered technology" that is directly or indirectly used or "reasonably foreseeable" to have "potential use" in any investor interaction, thereby imposing on the industry excessive costs and burdens which would harm investors as well as broker-dealers and investment advisers. The SEC would upend a marketplace that has worked so well for millions of investors and fails to provide any credible justification for doing so. Specifically, the SEC has (1) failed to identify any actual investor harm posed by conflicts of interest in firms' use of covered technology, (2) failed to provide any basis for its claim that disclosure is inadequate to address conflicts, and (3) failed to explain why the existing regulatory framework does not adequately address firms' use of this technology. The SEC's failure to identify an actual harm or need for its Proposal is the inevitable result of its flawed rulemaking process. Rather than conducting a data-driven, fact-based process before issuing the Proposal, the SEC broke from tradition and relied primarily on speculation, hearsay, and irrelevant academic literature. The SEC is better than this proposal.

### A. There Is No Evidentiary Support For The Proposal's Application To A Broad Swathe Of Technologies And Investor Interactions.

While the purported purpose of the Proposal is to address broker-dealers and investment advisers that improperly use "predictive data analytics," "artificial intelligence," and "machine learning," technologies, these terms appear to be window dressing. The SEC does not bother to identify any firms that use such technology or any use of such technology that creates an actual harm to investors. And to the extent that the SEC is concerned about retail investors trading a large volume of securities in a short period of time, the SEC has failed to demonstrate how the Proposal would address this concern. Among other things, the SEC has failed to provide a single shred of evidence that: (1) broker-dealers or investment advisers are using technology in a manner that would cause problematic trading, and (2) firms' customers are engaged in such trading. Moreover, the responses to the SEC's DEP Request (including Robinhood's response) cannot support the theory that firms are using technology in a manner that causes problematic customer trading.

Instead of identifying a real problem and then drafting a rule appropriately targeted to that problem, the Proposal captures almost every form of technology interaction, including the use of mundane programs that are clearly not predictive data analytics, artificial intelligence, or machine learning—such as spreadsheets, emails, and graphic design—and requires firms to identify and "eliminate or neutralize the effect of" certain "conflicts of interest" relating to this technology.[22] In the absence of any evidence that there is a discernible problem that requires solving and is not already addressed by the existing regulatory framework, the SEC relies on irrelevant, conclusory and outlandish claims to justify the need for the Proposal. These "sources" include, among other things:

[22] *See id*. at 53,963, 53,974.

- academic literature that has nothing to do with the use of technology in a customer-facing investment services business[23];
- speculative fear-mongering with hyperbolic, clickbait titles about the future of technology[24];
- unsupported emotional appeals and claims by individuals that demonstrate a fundamental misunderstanding of the state of the securities markets and regulation[25];
- publications that amount to little more than political marketing spin intended to generate "buzz" around existing or planned AI technology programs[26]; and
- comment letters responding to the DEP Request taken out of context or used to make points those letters do not support.[27]

With these sources, the SEC may as well also consult *The Terminator* (1984) for a showcase of the potential dangers of technology.

The SEC also presents no credible analysis or evidence that technology (in general or with regard to a specific technology) causes investors harm by causing them to trade in a manner that is too "frequent" or "excessive." Nor is there evidence that technology leads investors to any particular outcome—positive or negative. The so-called "support" the SEC cites for this proposition includes outdated academic articles from an era where customers were charged commissions on every trade.[28] Thanks to Robinhood, the commission era is over, and today's investors are able to self-direct their trading at historically low costs and, thanks to technology, with ready access to tools and information that many could not afford when investors were required to pay commissions. The scant, outdated academic literature referenced by the SEC is hardly sufficient to justify the Proposal's excessive costs and the harm it would do to disempower investors. But instead of doing the hard work of conducting a robust

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[23] *See, e.g.*, *id*. at 53,963, nn.24 & 26.

[24] *See, e.g.*, *id*. at 53,963, n.27, 53,964, nn.41 & 42, 53,968, nn.84 & 85.

[25] See, e.g., *id*. at 53,968, n.81, 53,969, n.92.

[26] *See, e.g.*, *id*. at 53,962, n.15, 53,964, n.31, 53,965, n.54, 54,001, n.266.

[27] *See, e.g.*, *id*. at 53,969-70, nn.92, 99 & 101 (letters from Robinhood and Scopus Financial Group).

[28] *See, e.g.*, *id*. at 53,999, n.240 (citing Brad M. Barber & Terrance Odean, *Trading Is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors*, 55 J. Fin. 773–806 (2000), which includes as part of its thesis why trading is hazardous to your wealth the finding that "[t]rading costs are high" due to commissions that were prevalent during that time, *id.* at 775)); Proposing Release, 88 Fed. Reg. at 53,998, n.232 (citing Hamid Mehran & René M. Stulz, *The Economics of Conflicts of Interest in Financial Institutions*, 85 J. Fin. Econ. 267–96 (Aug. 2007) (discussing in the context of mutual funds that a "broker's advice might be biased if the broker earns more by directing an investor to specific funds." *id*. at 271)).

economic analysis, the SEC relies on political talking points in a vain attempt to justify this Proposal.

The only time the SEC cites an actual example of a firm's use of technology to support its Proposal, it is in a wholly irrelevant and inapposite context that has nothing to do with broker-dealers.[29] Specifically, the SEC cites an example of robo-adviser conduct for which, as the SEC concedes, there are already regulations and protections that are sufficient to address the entity's use of technology—which moots any need for the Proposal.[30]

Even on the Proposal's own terms, the Proposal's stated rationales cannot justify its draconian remedies. The Proposal is predicated on claims about the uniquely powerful and supposedly conflict-prone nature of new technologies, such as artificial intelligence. These claims are the given justification both for the onerous obligations the Proposal places on firms to scour all their technologies for possible conflicts of interests, and for the unusually draconian remedy the Proposal prescribes—disclosure is insufficient, the Commission argues, because of the insidious "scalability" of new technologies. Although the Commission is mistaken on these matters even with respect to the *new* technologies it uses to justify this rule, there is simply no basis in reason to apply obligations targeted at *those* technologies to the full range of "covered technologies" under the Proposal, including Excel spreadsheets, for example, or calculators. The Commission's stated rationale for the Proposal cannot begin to justify the onerous obligations and restrictions it places on all technologies, and not merely on the handful of new technologies used to justify this Proposal. The mismatch between the Proposal's narrow premise on the one hand, and its sweeping coverage and crushing burdens on the other, is the essence of arbitrary and capricious agency action. It must be rectified. And of course, such a fundamental re-tooling of the Proposal will also require re-proposal.

Rather than invoking inapposite examples and propagating conspiracy theories that inject doubt into the fairness of our markets, the SEC should rely on facts and data in explaining why its Proposal is necessary—because the nation's securities regulator will receive no deference from a court for its dystopian musings about the wickedness of technology.

**B. There Is No Evidentiary Support for the Proposal's Radical Requirement To "Eliminate or Neutralize" Conflicts In Lieu of Addressing Conflicts Through Disclosure.**

The SEC's justification for the Proposal's "eliminate or neutralize" requirement is equally problematic. Without any basis, the SEC now claims that its 90-year-old convention of addressing conflicts of interest with disclosure is no longer valid: "due to the scalability of [covered] technologies and the potential for firms to reach a broad

[29] *See* Proposing Release, 88 Fed. Reg. at 53,968.

[30] *See id*.

audience at a rapid speed."[31] The SEC also points to the "inherent complexity and opacity" of technology as justification for eschewing disclosure as an effective mitigant, even while broadly defining covered technologies to include simple calculators and excel spreadsheets.[32]

Putting aside the fact that the SEC fails to explain what it means by "scalability" and how it applies to its vast universe of "covered technology," these conclusory statements that "disclosure will not work" fail to demonstrate how and why disclosure will not work when it has worked well for decades in contexts involving actual conflicts of interest. Unlike the Proposal's amorphous, undefined "conflicts," these conflicts are real and significant. For example, SEC and FINRA rules rely on disclosure to customers of critical conflicts of interest such as compensation, third party remuneration, and control relationships in connection with securities transactions.[33]

More recently, in the context of recommendations, the SEC adopted Reg BI[34] which relies primarily on disclosure to manage even *material* conflicts of interest and identifies only a specific and limited set of conflicts that must be eliminated.[35] When making a recommendation to a retail customer, broker-dealers are required by Reg BI to disclose "[a]ll material facts relating to conflicts of interest associated with the recommendation."[36] Reg BI only requires the elimination of "sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time."[37] These provisions were adopted by the SEC in 2019, after a multi-year rulemaking process that involved lengthy studies, several requests for information, over 6,000 comment letters, and in-person feedback from multiple investor roundtables and forums. Surely, conflicts of interest in the context of recommendations are by any measure more important and sensitive than "investor interactions" where only information is provided, and yet, the Commission determined that disclosure was generally appropriate. The Commission must explain why "conflicts" that are not even true conflicts (*see infra* at Section III.A.3), in interactions that may not even involve advice

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[31] *Id*. at 53,961.

[32] *Id*. at 53,967.

[33] *See, e.g.,* 17 C.F.R. § 240.10b-10 (Confirmation of transactions), 17 C.F.R. § 240.15c1-5 (Disclosure of control), 17 C.F.R. § 240.15c1-6 (Disclosure of interest in distribution); FINRA Rules 2262, 2269.

[34] Regulation Best Interest, 84 Fed. Reg. 33,318.

[35] Rule 15l-1(a)(2), Regulation Best Interest, 84 Fed. Reg. at 33,491.

[36] Rule 15l-1(a)(2)(i)(B), Regulation Best Interest, 84 Fed. Reg. at 33,491.

[37] Rule 15l-1(a)(2)(iii)(D), Regulation Best Interest, 84 Fed. Reg. at 33,491.

or recommendations, are less capable of being addressed by disclosures than real and genuine conflicts of interest relating to a recommendation.

The Proposal fails to explain what has changed since 2019 to make the SEC now reject disclosure as an effective means for addressing potential conflicts of interest even in interactions that do *not* involve a recommendation or actual transaction. Mobile apps and online trading sites have been available to retail investors well before 2019 when Reg BI was issued, and "technology" like calculators and spreadsheets have been used for decades. Why and how technology in all forms has suddenly become "conflicted" and to such a degree that disclosure is no longer effective is inexplicable.

The SEC's conclusory statement that "disclosure will not work" is flawed for a second reason: it ignores the fact that delivery of information to customers through technology can *better* inform customers of potential conflicts and risks. The SEC suggests that the delivery of information to customers through technology has some unbridled capacity to cause mischief because of its "scalability." However, the SEC ignores the fact that information delivered through technology can provide disclosures and risk statements in a more effective manner than if that same information were delivered through a different medium. Instead of sending a hard copy disclosure statement by mail and assuming that the customer will eventually receive and review it, firms use technology to provide more timely and targeted disclosures, such as through in-app messages, alerts, and education. Information delivered through technology also can reinforce the importance of disclosures, for example, by requiring customers to acknowledge or scroll-through important disclosures regarding the securities markets or securities products.

The SEC's weak attempts to explain why disclosure is inadequate are unsupported and unconvincing. As stated in the Proposal: "disclosure alone may not necessarily address negative outcomes when 'the issue lies in human psychological factors, rather than a lack of information.'"[38] However, the SEC does not even attempt to identify what these "human psychological factors" are or to provide any evidentiary support that its decade-long disclosure policy is no longer adequate because of these "psychological factors" (nor do we think the SEC has the expertise or authority to evaluate human psychology). Even the SEC's own economists acknowledge that this justification cannot be supported by facts or data, noting that certain benefits and costs identified in the Proposal are "impractical to quantify because quantification would necessitate general assumptions about behavioral responses that would be difficult to quantify."[39]

In truth, for retail investing, technology has meant simplicity, comprehensibility, accessibility, actionability and lower fees—and it is these very features that animate this Proposal, as the Commission worries that technology makes it too easy for individuals to trade "frequently." Given that this is one of the Proposal's premises—

[38] Proposing Release, 88 Fed. Reg. at 53,986, n.181.

[39] *Id.* at 53,998

technology simplifies trading—the Commission bears a heavy burden to explain why technology cannot also simplify and facilitate disclosure.

### C. The SEC Has Failed To Provide Any Credible Basis For Why The Existing Regulatory Framework Is Inadequate To Address Any Concerns With Covered Technology.

The Proposal is a highly flawed solution in search of a problem. In addition to failing to provide evidence of an actual harm the Proposal would address, the SEC fails to explain why the existing regulatory framework is not adequate to address any perceived concerns. To the contrary, the SEC seems to recognize that it has all the tools it needs at its disposal to address any concerns relating to covered technology, stating that it: "has and will continue to bring enforcement actions for violations of the Federal securities laws that entail the use of PDA-like technologies."[40]

Throughout the Proposal, the SEC concedes there is an extensive regulatory framework in place applicable to broker-dealers and investment advisers, including the SEC's broad antifraud authority under the Exchange Act and Advisers Act by which it can police potential misconduct and address investor harm that could result from the misuse of technology. For example, the SEC recognizes that "a broker-dealer has a duty to disclose material adverse information to its customers" which "the Commission has enforced … under the antifraud provisions."[41] The SEC also recognizes this existing authority with respect to investment advisers. In fact, just last year, the SEC settled an enforcement action under the Advisers Act Section 206's broad antifraud authority where the SEC alleged that conflicts of interest associated with a firm's use of PDA-like technologies resulted in harm to investors.[42] Because conflicts of interest involving technology have already been and can continue to be addressed by the existing antifraud provisions, the potential benefits of the Proposal are marginal at best.

In addition to the antifraud provisions of the federal securities laws, Reg BI is another tool the SEC already has to ensure that broker-dealers adequately address conflicts of interest in the context of a recommendation. As noted above, Reg BI already would apply to conflicts of interest related to covered technology where a "recommendation" is made to retail customers.[43] Reg BI enhanced the standard of conduct for broker-dealers providing recommendations to customers under the theory that conflicts of interest related to recommendations, more than other types of customer interactions, could lead to investor harm. When adopting Reg BI, the SEC

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[40] *Id.* at 53,967.

[41] *Id.* at 53,966.

[42] *See Charles Schwab & Co.*, Exchange Act Release No. 95,087 (June 13, 2022), https://www.sec.gov/files/litigation/admin/2022/34-95087.pdf; *see also* Proposing Release, 88 Fed. Reg. at 53,968.

[43] *See generally* Regulation Best Interest, 84 Fed. Reg. 33,318.

"proposed to limit conflicts of interest to those associated with recommendations as broker-dealers may provide a range of services not involving a recommendation, and *such services are subject to general antifraud liability and specific requirements to address associated conflicts of interest*."[44] The SEC very explicitly declined to apply Reg BI to communications that serve an educational purpose, such as "[g]eneral financial and investment information, including: [b]asic investment concepts …, effects of inflation, estimates of future retirement income needs, and assessment of a customer's investment profile," and even asset allocation models and interactive investment materials as long as "they do not include, standing alone or in combination with other communications, a recommendation."[45]

It is not clear what has changed in the short time since Reg BI was adopted that would require the imposition of a heightened standard of conduct to nearly every customer interaction where a broker-dealer involves the direct or indirect use of technology. Nowhere in its attempted explanations does the SEC demonstrate that technology poses unique risks to investors even outside the context of recommendations and consequently requires such a heightened standard.

On top of the existing SEC regulatory framework, the SEC has delegated to self-regulatory organizations ("SROs"), including FINRA, the ability to create and enforce rules governing broker-dealer conduct, communications with the public, and supervision that also capture the use of covered technology by broker-dealers and address conflicts of interest.[46] Congress and the SEC deliberately shifted primary responsibility for broker-dealer oversight from the SEC to FINRA, noting that SEC oversight of broker-dealers "was unnecessarily costly and diverted the SEC's limited resources away from areas of major concern, merely to duplicate the functions of the NASD [now FINRA]"[47] and recognizing that "the Commission could not effectively carry out the detailed responsibilities required."[48] Under FINRA rules, broker-dealers are required to observe high standards of commercial honor and just and equitable principles of trade in conducting their business—these standards are a catch-all designed to capture a broad array of conduct.[49] FINRA examines broker-dealers annually (and sometimes more frequently) for compliance with its rules and standards of conduct, including when a firm uses technology to engage in or facilitate

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[44] *Id*. at 33,387 (emphasis added).

[45] *Id*. at 33.337-38.

[46] *See, e.g.*, FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade); FINRA Rule 2020 (Use of Manipulative, Deceptive, or Other Fraudulent Devices); FINRA Rule 2111 (Suitability); FINRA Rule 2210 (Communications with the Public); FINRA Rule 3110 (Supervision).

[47] Concept Release Concerning Self-Regulation, 69 Fed. Reg. 71,256, 71,267 (Dec. 8, 2004).

[48] *Id*. at 71,282.

[49] *See* FINRA Rule 2010.

regulated brokerage functions, whether they are supported by proprietary technology or technology provided by an affiliate or third-party vendor.[50] SRO regulation supplements existing SEC authority to provide meaningful oversight of broker-dealers' interactions with customers without the need for new requirements that the Proposal would impose.[51]

In sum, the SEC puts forth no evidence that the existing regulatory framework is insufficient to address potential conflicts of interest in investor interactions. This is intriguing, to say the least, given the adamant pronouncements by SEC officials that the 90-year-old securities laws are more than adequate to regulate the inherently technology-driven crypto markets.[52] Accordingly, the SEC fails to demonstrate the need for the Proposal.[53]

### D. In A Troubling Departure From Long-Standing Tradition, The SEC Failed To Engage In A Serious Fact-Gathering Or Data-Driven Process Before Issuing The Proposal.

As detailed above, the SEC has failed to demonstrate a need or factual basis for the Proposal. The questionable analysis in this Proposal is a departure from the SEC's traditionally robust, data-driven process for obtaining information and feedback prior to engaging in rulemaking. This is a basic tenet of SEC rulemaking that has been long recognized by SEC Commissioners and should not be controversial.[54] As aptly noted

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[50] *See, e.g.*, FINRA, Regulatory Notice 21-29, *FINRA Reminds Firms of their Supervisory Obligations Related to Outsourcing to Third-Party Vendors* (Aug. 13, 2021), https://www.finra.org/rules-guidance/notices/21-29; FINRA, Notice to Members 05-48, *Members' Responsibilities When Outsourcing Activities to Third-Party Service Providers* (July 22, 2005), https://www.finra.org/rules-guidance/notices/05-48.

[51] *See, e.g.*, FINRA, *Cloud Computing in the Securities Industry* (Aug. 16, 2021), https://www.finra.org/rules-guidance/key-topics/fintech/report/cloud-computing; FINRA, *Artificial Intelligence (AI) in the Securities Industry* (June 10, 2020), https://www.finra.org/rules-guidance/key-topics/fintech/report/artificial-intelligence-in-the-securities-industry.

[52] *See, e.g.*, Ephrat Livni & Matthew Goldstein, *Even After FTX, S.E.C. Chair Sees No Need for New Crypto Laws*, N.Y. Times (Dec. 22, 2022), https://www.nytimes.com/2022/12/22/business/gary-gensler-sec-crypto.html.

[53] *See, e.g.*, Fiduciary Interpretation, 84 Fed. Reg. 33,669 (interpreting the fiduciary duties of an investment adviser in dealings with clients generally, which requires an adviser to act in its client's best interest at all times).

[54] *See, e.g.*, Luis A. Aguilar, Comm'r, SEC, *Exemplifying Fundamentals—Back to Basics* (Mar. 28, 2011) https://www.sec.gov/news/speech/2011/spch032811laa.htm ("A regulator must possess expertise that is informed by current, accurate data and must exercise judgment that is grounded in the mission of the institution and service to the public at large."); Mary Jo White, Chair, SEC, *Keynote Address: Securities Traders Association 83rd Annual Market Structure Conference, Equity Market Structure in 2016 and for the Future* (Sept. 14, 2016), https://www.sec.gov/news/speech/white-equity-market-structure-2016-09-14 (touting the

by then-Commissioner Luis Aguilar, when it comes to rulemaking, "[k]nowledge is always better than speculation"[55] and "new regulatory regimes and rules promulgated by the SEC must have real and verifiable investor protections."[56]

For example, prior to proposing Reg BI, the SEC spent years reviewing the standard of care applicable to broker-dealers and investment advisers, including through the RAND study of investor perspectives commissioned in 2006, the Dodd–Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") Section 913 staff study conducted in 2010-2011, and a request for data and other information in 2013.[57] In response to the 2013 request, the SEC received more than 250 comment letters from industry groups, individual market participants, and other interested persons who provided both qualitative and quantitative data and surveys regarding the benefits and costs of the current standards of conduct for broker-dealers and investment advisers, as well as alternative approaches to these standards. In November 2013, the SEC's Investor Advisory Committee adopted a recommendation on the standard of care that should apply to broker-dealers when providing personalized recommendations to retail customers. In 2017, the SEC again solicited comments from the public on specific areas relating to broker-dealers' standard of care when making recommendations and data and other information that could inform the Commission's analysis.[58] In addition to this request, SEC Chairman Clayton and the staff continually engaged in other outreach, including meetings with retail investors, investor advocacy groups, and industry participants, to better understand these issues.[59] And only after this extensive fact-gathering process was completed did the SEC issue its Reg BI proposal in 2018.

In contrast to this tradition of robust study and analysis before engaging in significant rulemaking, the Proposal is the product of very limited outreach prior to jumping straight into proposing expansive new rules. We are aware of no recent examination

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Commission's "deliberate, data-driven process to assess … more fundamental changes to equity market structure" because "[b]road changes to this market structure—especially those executed precipitously or without adequate data—can have serious unintended consequences for investors and issuers as their impact is fully realized, sometimes years down the road").

[55] Luis A. Aguilar, Comm'r, SEC, *U.S. Equity Market Structure: Making Our Markets Work Better for Investors* (May 11, 2015), https://www.sec.gov/news/statement/us-equity-marketstructure.

[56] Luis A. Aguilar, Comm'r, SEC, *An Insider's View of the SEC: Principles to Guide Reform* (Oct. 15, 2010), https://www.sec.gov/news/speech/2010/spch101510laa.htm.

[57] Jay Clayton, Chairman, SEC, *Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers* (June 1, 2017), https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31.

[58] *Id*.

[59] Regulation Best Interest, 83 Fed. Reg. 21,574, 21,582 (May 9, 2018).

sweep, study, or other information-gathering exercise that was launched in advance of the Proposal regarding the use of predictive data analytics by broker-dealers or investment advisers. The only industry engagement we are aware of with respect to this Proposal is the DEP Request, which underwent a flawed process that limited industry responses due to the brevity of the comment period and the breadth of the SEC's requests.[60] Moreover, the SEC failed to follow up with broker-dealers submitting responses to the DEP Request.[61] And while the DEP Request solicited information regarding broker-dealers' use of technology, the SEC failed to discuss these practices in the Proposal or its cost-benefit analysis (which also underscores a fatal flaw with the SEC's economic analysis).[62]

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[60] DEP Request, 86 Fed. Reg. 49,067; *see, e.g.,* Letter from Kevin M. Carroll, Managing Director and Associate General Counsel, SIFMA, to Vanessa A. Countryman, Secretary, SEC (Sept. 7, 2021), https://www.sec.gov/comments/s7-10-21/s71021-9208235-250006.pdf; Letter from Gail C. Bernstein, General Counsel, IAA, to Vanessa A. Countryman, Secretary, SEC (Oct. 1, 2021), https://www.sec.gov/comments/s7-10-21/s71021-9316151-260068.pdf (letters from industry groups expressing concern about the short comment period and requesting extensions on behalf of the industry).

[61] Indeed, the SEC's website shows that SEC officials met with a financial institution that has a broker-dealer in its corporate structure on only four occasions (two of which were meetings with Robinhood, and two of which involved firms that do not appear to have submitted comment letters) in connection with the DEP Request. *See* SEC, Comments on Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology to Develop and Provide Investment Advice, https://www.sec.gov/comments/s7-10-21/s71021.htm#meetings (last modified July 14, 2023).

[62] For example, the DEP Request posed the following questions to which the Proposal contains no responsive information:

*2.1 To what extent, and how, do firms use (or in the future expect to use) tools based on AI/ML (including deep learning, supervised learning, unsupervised learning, and reinforcement learning) and NLP and NLG, to develop and evolve DEPs? What are the objective functions of AI/ML models (e.g. revenue generation)? What are the inputs relied on by those AI/ML models (e.g. visual cues or feedback)? Does the ability to collect individual-specific data impact the effectiveness of the ML model in maximizing its objective functions?*

*2.10 Are there any particular challenges or risks that firms face in using AI/ML (including deep learning, supervised learning, unsupervised learning, and reinforcement learning), including AI developed or provided by third parties? If so, what are they and how do firms address such challenges or impediments and any risks associated with them? Have firms found that using AI/ML or retail investor data gathered in connection with DEPs raises unique issues related to financial privacy, information security, or identity theft prevention?*

*2.12 What are the benefits associated with the use of the tools and methods identified above (e.g., AI/ML, predictive data analytics, cross-industry research, behavioral science) in connection with the design, implementation, and modification of DEPs from the perspective of firms, retail investors, and other interested parties? How do these benefits differ depending*

The SEC also failed to gather any meaningful evidence regarding investors' use of covered technology, including what technology they want and use, why they want or use it, and how it affects them, and failed to address the many benefits that technology can provide. And yet the SEC chose to ignore these uses and benefits in its rulemaking.

Rather than taking a methodical, data-driven approach to rulemaking, the SEC's rulemaking appears to be based on unsupported speculation and academic theories.

## II. The SEC Has Failed To Conduct A Credible Cost-Benefit Analysis And Any Theoretical Benefits Cannot Outweigh The Proposal's Significant Costs And Burdens.

The SEC is required, by law, to undertake a thorough and accurate analysis of the costs that the Proposal would impose on regulated entities and the economy as a whole.[63] This economic analysis must be reasonable and substantiated, and the conclusions that the Commission draws from it must have a reasoned, rational basis in the data the Commission gathers. Guidelines issued by the SEC also mandate that the data used in this analysis be "accurate, reliable and unbiased," that it be carefully

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*upon the type of tools or methods? Do the tools and methods mitigate, or have the potential to mitigate, biases in the market that may have prevented participation by some retail investors (e.g., by lowering barriers to entry)? Please provide or identify any relevant data and other information.*

*2.13 What are the risks and costs associated with the use of the tools and methods identified above (e.g., AI/ML, predictive data analytics, cross-industry research, behavioral science) in connection with the design, implementation, and modification of DEPs from the perspective of firms, retail investors, and other interested parties? How do these risks differ depending upon the type of tools or methods used? What are the most significant investor protection concerns arising from or associated with the use of such tools and methods by broker-dealers and investment advisers in the context of DEPs? Please provide or identify any relevant data and other information.*

*2.15 Are there any particular challenges or risks associated with the use of AI/ML (including deep learning, supervised learning, unsupervised learning, and reinforcement learning), including AI developed or provided by third parties? If so, what are they and how should firms address such challenges or impediments and any risks associated with them? What model risk management steps should firms undertake? Does the use of AI/ML or retail investor data gathered in connection with DEPs raise unique issues related to financial privacy, information security, or identity theft prevention?*

*3.13 What additions or modifications to existing regulations, including, but not limited to, those identified above, or new regulations or guidance might be warranted to address investor protection concerns identified in connection with the use by broker-dealers and investment advisers of DEPs, the related tools and methods, and the use of retail investor data gathered in connection with DEPs? What types of requirements, limitations, or prohibitions would be most appropriate to address any such identified investor protection concerns?*

[63] *See, e.g.*, 44 U.S.C. § 3501 *et seq.*; 5 U.S.C. § 601 *et seq.*; 5 U.S.C. § 500 *et seq*.

reviewed by subject matter experts and appropriate levels of management, and that there be "adequate disclosure about underlying data sources, quantitative methods of analysis and assumptions used, to facilitate reproducibility of the information, according to commonly accepted scientific, financial or statistical standards, by qualified third parties."[64]

By its own admission, the SEC has failed to satisfy this fundamental statutory obligation. Here, the SEC concedes that it lacks the ability to reasonably estimate important components of the cost-benefit balance; entirely ignores other aspects of the supposed problem, such as the sufficiency of existing protections and the potential for technology to make disclosure more effective for retail investors; and provides estimates of the proposed rules' costs and burdens that are inadequate and far too low. Moreover, the costs that will be imposed by the proposed rules far outweigh any purported benefits identified by the Commission.

**A. The SEC Has Failed To Gather The Requisite Information To Conduct A Serious Cost Analysis And Instead Offers A Speculative And Incomplete Cost Assessment.**

**1. The SEC Admits That It Lacks the Data To Conduct A Complete Analysis.**

The SEC's economic analysis and numerous, multi-part requests for information are admissions that the SEC lacks critical data to estimate key components of the costs the proposed rules will impose. For example, the SEC expressly concedes the following:[65]

- "[T]he Commission is unable to quantity certain economic effects because it lacks the information necessary to provide estimates or ranges."
- "Some of the benefits and costs discussed below are impractical to quantify because quantification would necessitate general assumptions about behavioral responses that would be difficult to quantify."
- "The Commission seeks comment on any data that could aid quantification of these responses."
- "Based on Commission staff experience, the Commission believes that … third-party providers play a growing role with respect to the development of covered technologies…. Due to data limitations, we are unable to quantify or characterize in much detail the structure of these various service provider markets. The Commission lacks specific information on the exact extent to which third-party service providers are retained, the specific services they provide, and the costs for those services. We also do not have information

[64] SEC, *Final Data Quality Assurance Guidelines* (modified July 18, 2019), http://www.sec.gov/about/dataqualityguide.htm.

[65] Proposing Release, 88 Fed. Reg. at 53,997-98, 54,001.

about the market for these services, including the competitiveness of such markets."

The SEC also asks commenters to provide it with the following information that is fundamental to the rulemaking and information that the SEC should have gathered *before* issuing the Proposal so that it could provide a reasonable cost-benefit analysis:[66]

- "The Commission seeks comment on the conflicts of interest associated with the use of covered technologies. What types of conflicts of interest are associated with the use of these technologies? What costs do they impose on investors? What practices exist for eliminating, or neutralizing the effect of, these conflicts of interest? What practices exist for mitigating the effects of these conflicts of interest? What are the current costs of these methods?"
- "The Commission seeks comment on the potential costs associated with the proposed conflicts rules and proposed recordkeeping amendments. What types of costs are likely to be incurred by firms in order to comply with the proposed conflicts rules and proposed recordkeeping amendments? How might these costs vary depending on the types of technology, the business model, or the nature and extent of investor interactions used by the firms? To what extent do firms already incur these costs in order to comply with their existing obligations? What costs would there be for investors?"
- "The Commission seeks comment on the types of labor and other resources that would be required for firms to comply with the proposed conflicts rules and proposed recordkeeping amendments. What personnel would need to be involved in complying with the proposed conflicts rules and proposed recordkeeping amendments? What types of expertise would be required? How might the size and complexity of a firm impact the resources needed to comply with the proposed conflicts rules and proposed recordkeeping amendments?"
- "The Commission seeks comment on how the proposed conflicts rules and proposed recordkeeping amendments might impact a firm's or a technology provider's software development process. What changes might be necessary in order to help ensure that firms using covered technologies in investor interactions are in compliance with the proposed conflicts rules and proposed recordkeeping amendments? How might the proposed conflicts rules and proposed recordkeeping amendments impact the speed or efficiency of software development?"

With so many explicit admissions that it is either missing critical data or needs more data to complete its analysis, it is not possible for the SEC to satisfy its obligation to conduct a reasonable cost-benefit analysis.

[66] *Id*. at 54,014-15.

**2. The SEC's Analysis Also Fails To Provide A Complete Cost Estimate Because It Fails To Consider The Effect Of The Proposal On Key Groups.**

The SEC also fails to provide a complete cost estimate because it fails to fully quantify the effect of the Proposal on small firms or investors. With regard to small firms, many of these firms rely on third-party vendors for technology because they do not have the internal resources to produce or manage those technologies. Because the Proposal requires firms to go through the same exercise with covered technology from third parties, it would make it more challenging to outsource technology solutions, thereby creating barriers to entry and innovation and favoring firms that have the resources to manage technology in-house. The SEC recognizes the significant competitive disadvantages that the Proposal would create for smaller firms: "Smaller firms subject to the proposed conflicts rules could also face a competitive disadvantage compared to larger firms when negotiating with technology companies to build software that complies with the proposed conflicts rules."[67] The Proposal, however, fails to quantify any of these costs.

Similarly, the Proposal fails to quantify the costs to investors in two significant ways. First, it is undeniable that the Proposal will result in higher costs for firms and, by extension, investors. The SEC admits that investors could bear higher costs but does not even try to estimate the costs they would bear.[68] These costs could include the elimination of tools and features that retail investors take advantage of every day, like recurring investments, direct indexing, and portfolio rebalancing. The SEC, however, made no attempt to quantify the cost of losing or restricting access to these types of technologies.

And many benefits that covered technology provides are at risk of being reduced or eliminated under the Proposal. To this end, the SEC admits that a likely effect of the Proposal is for broker-dealers and advisers to reduce or eliminate certain covered technology that they provide (or could in the future provide) to investors.[69] The SEC expressly acknowledges that its Proposal will lead to firms *not providing* certain covered technology at all.[70] Also, if a firm is *too slow* in its implementation and cannot "promptly" address a potential conflict relating to a covered technology, it may eliminate the practice that gives rise to it (i.e., stop offering the technology to investors).[71] However, the SEC fails to quantify the costs to investors of this reduced access to technology. The SEC would entrench the divide between institutional investors and retail investors by making retail investors into second-class citizens by

[67] *Id*. at 54,012.

[68] *Id*. at 54,010.

[69] *Id*. at 54,012.

[70] *Id*. at 53,986.

[71] *Id*. at 53,987.

depriving them of access to technology and information because the SEC views them as incapable of understanding or participating in the securities markets.

This very real harm may be the most significant cost of the Proposal. Greater access to technology has increased financial participation in the securities markets; reducing this access ultimately will push investors out of the market. The obvious outcome of the Proposal, then, is that it will result in a worse, more expensive, less informed and more intimidating investor experience. Such an outcome is anti-investor and antithetical to the SEC's mission to protect investors. It is also ignored in the SEC's cost-benefit analysis.

### B. For The Costs That It Does Quantify, The SEC Woefully Underestimates The Cost Of Compliance.

Although the Proposal purports to relate to the use of "predictive data analytics" by broker-dealers and investment advisers, the definitional triggers in the SEC's Proposal are overly broad and would capture a much broader range of communications. To illustrate the extreme burdens that would be imposed on firms, below are the steps a broker-dealer or adviser would need to take under the Proposal:

- First, a firm would need to identify all technology that could be "covered technology." This is a problem because the definition of "covered technology"[72] captures far more than the predictive AI and other advanced technologies identified as a concern by the SEC. The SEC acknowledges that the definition can capture even mundane technologies, such as spreadsheets.[73] The SEC, however, provides no guidance on the level of abstraction required to analyze a technology. To start, while internet websites and mobile applications are covered under the proposed rules,[74] every individual piece of a website or app would need to be evaluated, and, in many instances, the underlying code would need to be analyzed. It would be a significant hurdle for a firm even to undergo an initial assessment of which technologies are "covered" before it can determine which covered technologies are involved in an "investor interaction."[75]

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[72] "Covered technology" means "an analytical, technological, or computational function, algorithm, model, correlation matrix, or similar method or process that optimizes for, predicts, guides, forecasts, or directs investment-related behaviors or outcomes." Proposed Rules 15l-2(a), 211(h)(2); Proposing Release, 88 Fed. Reg. at 54,021-22, 54,023.

[73] Proposing Release, 88 Fed. Reg. at 53,972.

[74] *Id*. at 53,974.

[75] "Investor interaction" means engaging or communicating with an investor, including by exercising discretion with respect to an investor's account; providing information to an investor; or soliciting an investor; except that the term does not apply to interactions solely for purposes of meeting legal or regulatory obligations or providing clerical, ministerial, or

- Second, a firm would need to identify all covered technology that could be used—directly or indirectly—in an "investor interaction." This is again a problem because the definition of "investor interaction" is similarly over-broad. It encompasses a universe just as broad as "covered technology," from formal correspondence in person, by phone, email, or text, to any user display a customer can view or notification a customer can request on a website or app. Although intended to alleviate the burden of the expansive definition, a firm would need to assess which "investor interactions" were eligible to be excluded from the "investor interaction" definition for functions that are "solely for purposes of meeting legal or regulatory obligations or providing clerical, ministerial, or general administrative support." Additionally, the firm must consider not only its *actual* use of covered technology but also any *reasonably foreseeable potential* uses as well, requiring the firm to use a crystal ball to divine how it may in the future use a technology, even if it does not end up using the technology in that manner.

- Third, after identifying which technologies are covered technologies and which covered technologies are used in investor interactions, a firm would be required to determine whether any of those technologies involve a "conflict of interest" under the Proposal. Again, this is a problem because the definition of "conflict of interest" is also incredibly broad. It captures any technology that "takes into consideration an interest" of the firm or a natural person who is an associated person of the firm.[76] As the SEC states: "[c]onsideration of *any* firm interest would be sufficient for a conflict of interest to exist under the proposed conflicts rules."[77] And yet, it is both necessary and appropriate that firms' decisions consider the interests of their business. Taking into account those interests does not subvert the principal-agent relationship, nor does it create a true *conflict* of interest between those parties. Only through the SEC's complete re-definition of "conflict of interest" to include any consideration of a firm's interests can such a theory gain any traction. The consequence may be that every technology implemented by a broker-dealer necessarily involves a so-called "conflict of interest" because such technology could eventually lead to a transaction (even if the transaction is entirely self-directed by the customer) and thus, more business for the broker-dealer. In other words, firms will likely need to assume that every use of technology is "conflicted" and then undergo the task of attempting to identify such "conflicts."

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general administrative support. Proposed Rules 15l-2(a), 211(h)(2)-4(a), Proposing Release, 88 Fed. Reg. at 54,021-22, 54,023.

[76] Proposed Rules 15l-2(a), 211(h)(2)-4(a), Proposing Release, 88 Fed. Reg. at 54,021, 54,023.

[77] Proposing Release, 88 Fed. Reg. at 53,985.

- Fourth, the firm would be required to prove that no *actual* conflicts of interest exist when it seeks to use (or potentially use) a covered technology. Once each so-called "conflict of interest" has been identified, a firm must determine whether any conflict places the interests of the firm or an associated person ahead of the interests of investors. If the conflict places, or *could place*, an interest of the firm or its associated person ahead of the customer, then the firm must undertake to "eliminate, or neutralize the effect of" the conflict so that it "no longer places the interests of the firm ahead of the interests of investors."[78] This turns the enforcement framework on its head; rather than requiring the SEC to prove that firms have violated their obligations by failing to disclose an actual conflict of interest, the proposal would presume wrongdoing unless a firm can prove that no conflict exists.
- Fifth, each step of this laborious process is expected to be documented in a firm's policies and procedures and accompanied by onerous recordkeeping requirements that will require a firm to identify and describe each "covered technology" and its "material features," "investor interaction," use and foreseeable potential use, "conflict of interest," how a conflict of interest did or did not place the firm's or an associated person's interests ahead of a customer, and the process used to eliminate or neutralize any identified conflict that did so, and then justify (with documented support) each decision the firm made along the way.[79]
- Finally, the above steps would need to be repeated on a periodic basis and every time a firm rolls out a new technology or makes a material change to existing technology. And every year, firms would need to review and update their documentation and processes.[80]

Each of the above steps and requirements involves reading tea leaves about all the possible interpretations of what is required and what the terminology means. This process is made only more costly and burdensome where a firm seeks to use a third-party technology vendor because the firm may not have readily available access to the information that the Proposal would require. As SEC itself concedes, "the requirement to identify conflicts of interest in a technology could dissuade firms from using certain technologies when it is too difficult or costly to adequately evaluate the use of the covered technology, identify a conflict of interest, or determine whether they place the firm's or an associated person's interest ahead of an investor's."[81] This would be a bad result for markets, firms, and investors.

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[78] *Id*. at 53,986.

[79] *Id*. at 53,990.

[80] *Id.*

[81] *Id*. at 54,010-11.

Notably, the SEC makes no attempt to quantify the costs associated with the use of third-party service providers.[82] Shockingly, the SEC estimates that these laborious steps would, for a firm such as Robinhood,[83] amount to a paltry:

- 25 hours and $11,150 for initial compliance, and
- 12.5 hours and $5,575 for each year thereafter.[84]

These projections have no grounding in reality and grossly underestimate the costs associated with the Proposal. At the same time the SEC maintains that it will cost less than $6,000 to comply with the Proposal on a yearly basis, it concedes that the new process for "identifying, evaluating, eliminating or neutralizing conflicts of interest" could be challenging and, in some cases, *may not even be possible*.[85] It is not clear how the SEC can reconcile an admittedly impossible, challenging task with its anemic cost estimates.

The implementation of Reg BI is instructive on the SEC's economic analysis for the Proposal. Compliance with Reg BI involved extensive industry resources. Even though the SEC estimated initial industry costs of $5.96 billion and ongoing annual costs of $2.37 billion (split among 2,766 broker-dealers amounting to a per firm initial cost of approximately $2,154,736 and ongoing annual cost of approximately $856,833), an independent third party estimated $17 billion in initial costs and $6.25 billion in annualized costs (a per firm initial cost of approximately $6,146,059 and ongoing annual cost of approximately $2,259,581).[86]

It is no surprise that compliance with Reg BI was an expensive task—and significantly more expensive than the SEC's economic analysis suggested. For Reg BI, firms had to

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[82] *See id.* at 54,001 ("Due to data limitations, we are unable to quantify or characterize in much detail the structure of these various service provider markets. The Commission lacks specific information on the exact extent to which third-party service providers are retained, the specific services they provide, and the costs for those services.").

[83] Based on the SEC's definition of "complex covered technology firm" (i.e., firms that use machine learning or NLP algorithms or process large data sets), Robinhood has determined that it would be characterized as a "simple covered technology firm" because it does not utilize complex covered technology at this time.

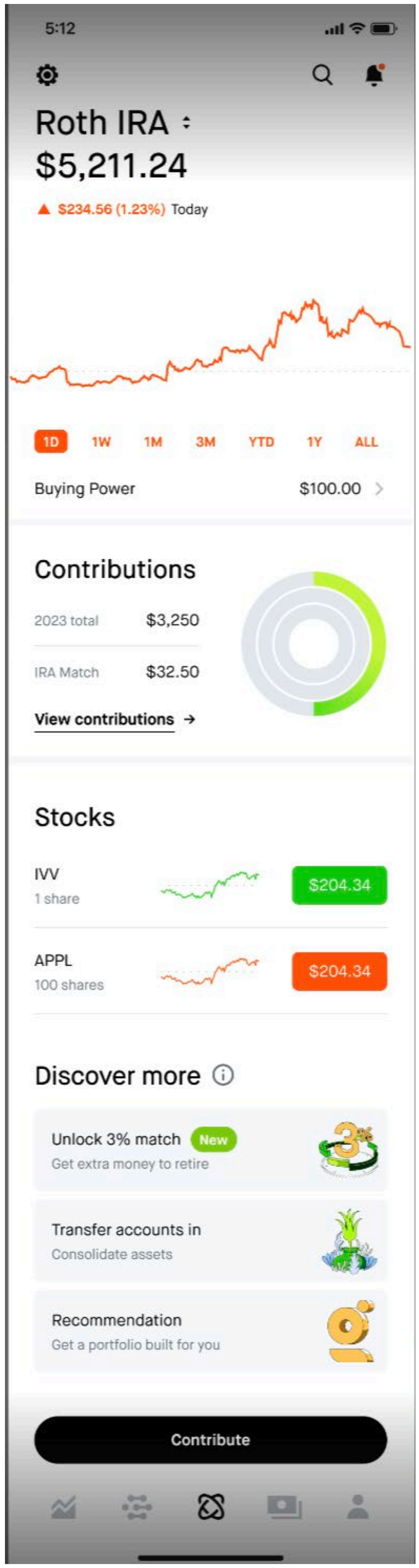
[84] Proposing Release, 88 Fed. Reg. at 54,009 tbl.2.

[85] *See id.* at 53,978 ("In certain cases, it may be difficult or impossible to evaluate a particular covered technology or identify any conflict of interest associated with its use or potential use within the meaning of the proposed rules.").

[86] *See* Deloitte & Touche LLP and SIFMA, *Regulation Best Interest: How wealth management firms are implementing the Rule Package* at 25 (Mar. 6, 2020), https://www2.deloitte.com/content/dam/Deloitte/us/Documents/regulatory/us-regulation-best-interest-survey-report.pdf ("The aggregate up-front costs for the industry are estimated at approximately $17.07 billion, while the aggregate annualized spend is estimated at approximately $6.25 billion. These aggregates are across people, process and technology.").

establish cross-functional teams with stakeholders across the business to complete a comprehensive analysis of all customer communications that could involve a recommendation and then take steps to comply with Reg BI general standards and obligations. Additionally, firms needed to operationalize future compliance by establishing controls for when products, services, or compensation plans changed.

Unlike Reg BI, the Proposal does not stop at customer communications involving recommendations. Now, the SEC would require broker-dealers and investment advisers to undertake a similar process to examine not only customer communications but also any investor interaction that involves covered technology and take steps to eliminate or neutralize the effect of any identified conflict that place the firm's interest ahead of investors' interests. Yet the SEC's estimated costs are *significantly less* than its estimated costs of Reg BI. This makes no sense. To illustrate how onerous this process would be, we offer a sample analysis of a relatively simple mobile app interaction—the IRA page of the Robinhood App.


5:12
Roth IRA
$5,211.24
$234.56 (1.23%) Today
1D
1W
1M
3M
YTD
1Y
ALL
Buying Power
$100.00
Contributions
2023 total
$3,250
IRA Match
$32.50
View contributions
Stocks
IVV
1 share
$204.34
APPL
100 shares
$204.34
Discover more
Unlock 3% match
New
Get extra money to retire
Transfer accounts in
Consolidate assets
Recommendation
Get a portfolio built for you
Contribute

Starting at the top of the page and pointing out only the most obvious uses of technology,[87] we would need to review:

- the appearance of a red dot to signify the customer has a notification;
- the inclusion of "Gold 3%," which is Robinhood's subscription product that includes larger matches on contributions; larger instant deposits; Level 2 stock data; Morningstar research reports; and 4.9% interest on uninvested cash in the customer's account;
- the use of the color gold with "Gold 3%" box;
- the use of colors to depict price movement—green is up and red is down;
- the font type and size of the numbers representing the total value in the account;
- how the total value of the account changes;
- disclosing "Buying Power";
- disclosing the amount of "Contributions" for this year;
- the button "Contribute";
- the use of "Find investments," which lets customers search for stocks and ETFs by different categories;
- the use of "Discover More"; the three prompts underneath: "Have an old 401(k)?," "Consolidate IRAs," and "Options trading"; and the graphics next to each prompt; and
- the icons that are static at the bottom of the page.

Arguably, each feature described above would need to be analyzed under the Proposal. If the customer decides to purchase a security, this exercise would involve reviewing every step the customer must take, from the landing page through the decision on what order type to use and the eventual submission of the order by "swiping up."

To undertake this analysis, a cross-functional team would need to be able to evaluate and understand any code, technology, computation, or algorithmic functions that underlie or determine what is displayed to customers. Each function will largely fall into one or more buckets: (1) features that make understanding an investment account easier ("ease of use"); (2) informational; (3) educational; and (4) promotional. Then, the firm would need to assess whether these technologies take into account an interest of the firm and whether the firm is placing its own interests ahead of those of investors. There is no clear or easy way for firms to evaluate these

[87] This list is not intended to be exhaustive. We expect that this analysis could require reviewing additional elements not listed here that may be drawn in by the expansive definition of "covered technology" upon further review.

interests under the Proposal. Firms will shoulder the burden of establishing a consistent approach only to be subject to second-guessing at every turn during a regulatory examination or inquiry.

For “ease of use” features, one would think that the firm is not placing its interests ahead of investors because the purpose of those features is to make it easier for customers to invest—the exact reason they have come to Robinhood and downloaded our App. We at Robinhood think investors having easy access to the capital markets is a good thing. However, it could be argued that any “ease of use” feature benefits the firm because it makes it easier for investors to place trades or contribute money to their accounts—both of which benefit the firm by increasing the firm’s revenues. The same analysis could apply to informational or educational features. Again, one could argue both the investor and the firm benefit from these features. But what if interests are aligned but result in customers trading more or depositing more into their account? When does the firm’s profit motive outweigh the benefits that investors receive from features like educational tools designed to teach investors important financial skills?

Conversely, would all promotional features, such as including the “Gold 3%” box to promote Robinhood’s Gold offering, put the firm’s interest ahead of the investor’s interest? The Proposal would muddy at what point the benefits an investor receives for taking advantage of this offering outweigh the firm’s own interests.

These are just a small sample of the questions that Robinhood would need to consider in evaluating whether conflicts of interest exist that would need to be addressed under the Proposal. Although how to perform the analysis is not clear, it is clear that this first step of the analysis will involve significant time and resources to perform.

Once we have decided a “conflict of interest” exists where the firm’s interests are placed ahead of an investor’s interests, if it is even determinable, we would need to eliminate or neutralize the effects of the conflict. Having to eliminate/neutralize a promotional conflict would mean that the firm likely could not include references to other products and services the firm offers. Likewise, if an ease of use, informational, or educational feature was deemed to place the firm’s interest ahead of the investor’s (i.e., investors trade more, and the firm makes more money), it would need to be eliminated or at the least heavily restructured. For example, would “green” and “red” need to be eliminated and replaced with “black” and “white?” Would using black and white be sufficient to eliminate or neutralize the effect of a conflict associated with using colors? Would graphics need to be eliminated? What about the use of buttons to contribute to accounts, transfer funds or place trades? Is “swiping up” to place a trade out?

Finally, all the above identification and consideration would need to be documented in the firm’s books and records.

One screen down ... thousands to go.

As stated above, the Proposal estimates that a "simple" covered technology firm would incur initial costs of $11,150 and annual costs of $5,575. It appears that Robinhood would largely be considered a simple covered technology firm because of its limited use of artificial intelligence and machine learning to back office or compliance functions. Given the above examples and how many times this process would need to be repeated, the Proposal's estimate strains credulity.

While Robinhood does not currently have an estimate of how many times the above example assessment would need to be completed per year, the ongoing assessment of $5,575 is nowhere near an accurate assessment. Robinhood estimates that it makes tens of thousands of coding changes each year to the Robinhood App and website related to brokerage, and during the last 12 months, Robinhood released 50 iOS and 50 Android updates. Arguably, each brokerage code update, whether it involves technology underlying the user interface or a change visible to customers in the App or website would need to be reviewed to understand the impact, whether the change resulted in a "conflict of interest" and whether the change was placing the firm's interest ahead of customers' interests. Completing an assessment of each of the tens of thousands of changes would require a dedicated team of employees spending thousands of hours each year conducting the review and creating and maintaining the records required under the Proposal.

Even assuming the ongoing review of coding changes, the rollout of new products and changes to existing products would require Robinhood to hire the equivalent of five full time employees in legal, compliance, product management, engineering, and operations (a hypothetical, conservative estimate to demonstrate how far off base the SEC's estimate truly is). Using the SEC's blended rate of $446 per hour for personnel required to conduct the necessary reviews,[88] the annual costs of these five employees would be over $4.8 million, a far cry from the $5,575 for ongoing annual costs to simple covered technology firms, or even $78,050 per year for complex covered technology firms. And if we add the tens of thousands of dollars in outside legal fees that Robinhood would accrue in reviewing and developing its process, the SEC's underestimate is even more egregious.

### C. The SEC Has Failed To Quantify Any Benefits To The Proposal.

In the absence of any demonstrable regulatory gap and given the significant costs and burdens that would be associated with the Proposal, the SEC's burden for substantiating the benefits of the Proposal is high. The SEC does not meet this burden because any potential benefits of the Proposal that are cited by the SEC are unclear and speculative at best.

The SEC's economic analysis fails to quantify any benefits of the Proposal, or even identify any clear benefits. The SEC repeatedly states that the proposed rules "*could*" or "*might*" generate unspecified benefits for investors, but there is no attempt to

[88] Proposing Release, 88 Fed. Reg. at 54,016 tbl.3.

describe or quantify these benefits.[89] The SEC itself states: "the Commission is unable to quantify certain economic effects because it lacks the information necessary to provide estimates or ranges" and that "[s]ome of the benefits and costs discussed below are impracticable to quantify because quantification would necessitate general assumptions about behavioral responses that would be difficult to quantify."[90] It also admits that the incredibly costly undertakings it requires may often prove totally unnecessary, since "[i]n the case of many covered technologies, it may be readily apparent that, while the technology may take into account an interest of the firm, it does not result in the firm's interests being placed ahead of investors' interests."[91] The Proposal seems to suggest this reflects the rule's reasonableness—remedial measures often won't be required. But in fact, this is a foundational problem of the rule—it requires a costly, no-stone-unturned search for hypothetical conflicts that in "many" cases don't exist. The Commission cannot adopt this rule without properly estimating how frequently, in the costly enterprise it is requiring, actual problems will be unearthed.

The SEC also alludes to the Proposal enhancing "investor protection" and "investor confidence" without describing how the Proposal would produce these abstract benefits.[92] In that discussion, the SEC necessarily assumes that investors are not adequately protected by existing regulations and do not currently possess sufficient confidence in the markets to support their participation (a proposition that flies in the face of the significant growth of retail investing we have had in recent years). However, the SEC does not identify *which* investors currently exhibit these characteristics and would benefit from the Proposal. The Proposing Release is littered with conclusory statements about how technology can influence customer trading behavior, even where recommendations or investment advice are not provided, and how investors could not possibly understand the technologies being used and the conflicts such technologies create. But the SEC does not delve into whether these technologies do, in fact, have that effect, or even whether any effects are harmful for investors. There is no effort to test these academic hypotheses and almost no support cited by the SEC. Instead, the SEC caveats or couches in uncertain terms the potential benefits that it thinks the Proposal could generate. In several cases, the SEC also casts doubt on the likelihood that these potential benefits will materialize.[93] The level of uncertainty in the SEC's own description of the Proposal's benefits should mean that they are taken with a massive grain of salt or simply discarded. The SEC

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[89] *See, e.g.*, *id.* at 53,998 (generally disclaiming quantification of likely economic effects of the Proposal because the SEC "lacks the information necessary" or it is "impracticable" or "difficult" to do so).

[90] *Id*.

[91] *Id*. at 53,983.

[92] *See, e.g.*, *id.* at 54,006-08.

[93] *See, e.g.*, *id*. at 54,011-12.

has not met its burden to justify the costs of the Proposal with commensurate benefits.

At the end of the day, the costs of this rule are clear—and clearly immense. The benefits are dubious and speculative. Such a rule cannot legally be adopted.

**D. The SEC Has Failed To Consider The Sufficiency Of Existing Regulations In Its Cost-Benefit Analysis.**

Related to its failure to quantify any "benefits," the SEC's cost-benefit analysis is also incomplete because the SEC has failed to identify any problematic practices relating to the use of covered technology that could not be addressed by existing SEC and FINRA regulations. This failure renders the SEC's cost-benefit analysis meaningless. Without any such assessment, it is impossible to estimate the expected benefits from the proposed rules. If there is no need for those rules, there can be no benefits to outweigh the billions of dollars in costs.

Notably, the one real example of a problematic practice involving covered technology that the Commission identifies proves our point that existing regulations are more than adequate.[94] In that case, the SEC brought an enforcement action against a robo-adviser for marketing that its "no fee" portfolios were determined through a "disciplined portfolio construction methodology" when they allegedly were pre-set to hold a certain percent of assets in cash because the adviser's affiliate was guaranteed revenue at these levels.[95] There, existing regulations were more than adequate to allow the SEC to successfully bring and settle an enforcement action. In the case of the Proposal, the SEC's failure to identify a real example of a harmful practice that cannot be addressed by existing regulations necessarily means that there is no need for the Proposal and any speculative benefits cannot outweigh the very real costs. This lone example illustrates another point as well because the alleged practice would have been easy to describe in a disclosure. A central premise of the Proposal is that the (imaginary) conflicts arising from technology are so complex they cannot be addressed by disclosure. Mostly, these conflicts are merely imagined.[96] But in the rare instance where the Commission gives actual evidence—an example—of what might occur, it is an issue that a disclosure could have simply described.

This reflects a peculiar (and legally unsustainable) feature of the Proposal: it uses the imaginary, speculative nature of the harm it addresses as a basis to mandate an especially onerous solution. First, the Proposal imagines future conflicts of interest

[94] *Id*. at 53,968.

[95] *Charles Schwab & Co*., Exchange Act Release No. 95,087 (June 13, 2022).

[96] *See, e.g*., Proposing Release, 88 Fed. Reg. at 53,965 (speculating that "[f]irms' nascent use of AI *may already* be exposing investors to these" risks, and types of risks," and expressing "concern[ ] that firms *will* . . . take their own interest into account" in developing AI) (emphasis added).

that it does not concretely identify or describe, and then—having conjured these unidentified behaviors—imagines that they are so complex, they cannot effectively be described in a disclosure. Under the law, however, a dearth of facts is not a reason to impose a burdensome rule. It is a reason to shelve this costly, speculative Proposal until appropriate study has been done.

## III. The SEC Lacks The Authority To Adopt The Proposal.

In addition to being unjustified, the Proposal would exceed the Commission's statutory authority and violate the First Amendment.

### A. The Proposal Exceeds The SEC's Statutory Authority, As Illustrated By The Plain Language Of The Provisions On Which The Commission Relies.

Like other federal agencies, the Commission "literally has no power to act … unless and until Congress authorizes it to do so by statute."[97] Moreover, the Commission's authority must be read narrowly in the circumstances here to avoid triggering the "serious constitutional problems" the Proposal raises.[98]

The Commission offers the Proposal under its "authority under section 211(h) of the Advisers Act and section 15(l) of the Exchange Act."[99] The Proposal exceeds this authority in multiple ways.

*First*, the Commission's authority is limited to prohibiting or restricting "certain" conflicts of interest that the Commission has "examine[d]"; the Commission cannot just regulate "*all* conflicts of interest" without specification. *Second*, the Commission's authority to "prohibit[]" or "restrict[]" conflicts of interest is a negative power; the Commission can bar certain arrangements that involve competing interests; it cannot force broker-dealers and investment advisers to develop procedures to identify "*any* conflict of interest," even if the Commission itself has not identified it. *Third*, the Commission may regulate "conflicts of interest," not any interaction with an investor in which the broker-dealer or investment adviser "takes into consideration" an interest of its own. *Fourth*, and finally, the Commission's authority is limited to addressing practices that are "contrary to the public interest and the protection of investors"; using technology to facilitate affordable access to investment services is anything but.

#### 1. The Proposal Exceeds The SEC's Authority To Bar "Certain" Conflicts of Interest.

The Commission's authority is limited to prohibiting or restricting "*certain*" conflicts of interest. Sections 15(l)(2) and 211(h)(2), enacted as part of Section 913 of Title IX

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[97] *Franciscan All., Inc. v. Becerra*, 47 F.4th 368, 378 (5th Cir. 2022) (quoting *Fed. Election Comm'n v. Cruz*, 142 S. Ct. 1638, 1649 (2022)).

[98] *See Edward J. DeBartolo Corp. v. Florida Gulf Coast Bldg. & Const. Trades Council*, 485 U.S. 568, 575 (1988); Section III.C, *infra*.

[99] Proposing Release, 88 Fed. Reg. at 53,971.

of the Dodd-Frank Act, are identical: each authorizes the Commission to "examine and, where appropriate, promulgate rules prohibiting or restricting *certain* sales practices, conflicts of interest, and compensation schemes for brokers, dealers, and investment advisers."[100] The Proposal does not simply restrict or prohibit "certain" conflicts of interest, however. Instead, the Proposal requires broker-dealers and investment advisers to, with respect to "covered technologies," identify and address "*all* conflicts of interest."[101] "Certain" does not mean "all."[102] It is the *Commission's* responsibility to "examine" and, "where appropriate," prohibit or restrict "certain" conflicts of interest—not to command regulated parties to themselves go out and identify "*any* conflict of interest" that might arise from the use of a covered technology.[103] The Commission has not undertaken such an examination here, despite the SEC Staff's recommendation to do so in the GameStop Report.[104]

The Commission itself recently rejected the very authority it claims here. In its final order adopting regulations governing private fund advisers, the Commission "agree[d] that 'certain,'" in section 211(h)(2), "indicates that [the statute] does *not* apply to all sales practices, conflicts of interest and compensation schemes, but rather only those that, after examination, the Commission deems contrary to the public interest and protection of investors."[105] The Proposal here—which reaches "*all* conflicts of interest,"[106] rather than any specifically identified conflict of interest—is inconsistent with the Commission's own reading of its authority.

That the Proposal extends only to conflicts of interest associated with "any use or reasonably foreseeable potential use of a covered technology" is immaterial to the

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[100] 15 U.S.C. §§ 78o(l)(2), 80b-11(h)(2) (emphasis added).

[101] Proposing Release, 88 Fed. Reg. at 53,978 (emphasis added).

[102] *The Am. Heritage Dictionary of the English Language* (5th ed. 2022) (defining "certain" as "[a]n indefinite but limited number; some"), https://tinyurl.com/yc7dsxyj; *see El Al Israel Airlines, Ltd. v. Tsui Yuan Tseng*, 525 U.S. 155, 173 (1999) ("Inclusion of the word 'certain' in the [Warsaw] Convention's title . . . accurately indicated that 'the [C]onvention is concerned with certain rules only, not with all the rules relating to international carriage by air.'" (quoting *Sidhu v. British Airways plc*, [1997] 1 All E.R. 193, 204) (second alteration in original)).

[103] Proposing Release, 88 Fed. Reg. at 53978 (emphasis added).

[104] *See* GameStop Report at 43-44.

[105] *Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews*, 88 Fed. Reg. 63,206, 63,216 (Sept. 14, 2023) (codified at 17 C.F.R. Part 275) (emphasis added); *see also id.* ("There are other examples of sales practices, conflicts of interest and compensation schemes in the private fund industry that are not addressed in this rulemaking, some of which we do not currently view as rising to the level of concern set forth in section 211(h).").

[106] Proposing Release, 88 Fed. Reg. at 53,978 (emphasis added).

statutory analysis.[107] A conflict of interest is defined by two competing interests at stake, not by the setting in which that competition may arise. In other words, the Commission's authority to prohibit certain conflicts of interest is limited to outlawing specific scenarios involving competing interests that the Commission believes harm the public interest, not issuing a blanket regulation on any and all competing interests that happen to arise while using technology.[108]

#### 2. The Proposal Does Not Merely "Prohibit" Or "Restrict" Conflicts Of Interest.

The Proposal also goes beyond "*prohibiting or restricting*" conflicts of interest.[109] The words "prohibiting and restricting" unambiguously impart only a negative power—the power to restrain certain specific scenarios involving competing interests.[110] Those words immediately precede, and modify, the phrase "certain … conflicts of interest," thus making clear that the Commission may only "ban" existing conflicts.[111] The Proposal goes well beyond this. It requires broker-dealers and investment advisers to independently undertake an onerous, detailed process to "[e]valuate any use" of a covered technology, "identify" any conflict of interest, as defined by the Proposal, "[d]etermine" whether that use gives rise to a conflict of interest that place's the firm's or an associated person's interests ahead of an investor, and "[e]liminate, or neutralize the effect of," those conflicts, and to "adopt, implement, and maintain[/adopt and implement] written policies and procedures" to do the same.[112]

The Commission does not have the authority to require this. When Congress wants to authorize the Commission to go beyond restricting or prohibiting a particular practice—it says so. Under the statute that Congress enacted, the Commission can ban "certain" conflicts that it has identified and then "examine[d]," but the Commission cannot use this limited authority to require broker-dealers and investment advisers to establish and undergo a highly prescriptive process to identify and address all conflicts of interest for themselves.

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[107] *Id*. at 53,971, 54,021–24.

[108] The Proposal's broad application is even too much for the SEC's own economists, who had difficulty with assessing the costs and benefits of the Proposal because the Proposal's application of "conflicts of interest" is broader "than how economists usually define 'conflicts of interest,' such as in the context of the principal-agent problem. *Id*. at 53,998 n.232.

[109] 15 U.S.C. §§ 78o(l)(2), 80b-11(h)(2) (emphasis added).

[110] *See Webster's Third New Int'l Dictionary* 1813 (1961) (defining "prohibition" as "a declaration or injunction forbidding an action"); *id.* at 1937 (defining "restrict" as "to set bounds or limits to").

[111] *See Nat. Res. Def. Council, Inc. v. U.S. Consumer Prod. Safety Comm'n*, 597 F. Supp. 2d 370, 387 n.10 (S.D.N.Y. 2009) ("'Prohibition' and 'ban' have the same meaning in everyday use.").

[112] Proposed Rule 15l-2(b), Proposing Release 88 Fed. Reg. at 54,022.

### 3. The Proposal Does Not Regulate "Conflicts Of Interest."

The Proposal also does not regulate "conflicts of interest" within any recognizable meaning of that term. The Commission adopts what it modestly calls a "broad definition of conflict of interest."[113] According to the Proposal, a conflict of interest arises whenever a broker-dealer or adviser "takes into consideration an interest" of its own.[114] That stretches the concept of "conflict of interest" beyond recognition. "Conflict of interest" is a term of art. A "conflict of interest" arises in the context of a "principal-agent relationship"[115]; it is a "real or seeming incompatibility between one's private interests and one's public or fiduciary duties."[116] By contrast, a conflict of interest has never been understood to encompass (as the Commission now claims) *any* decision that considers "*any* firm-favorable information,"[117] whether there is an actual divergence of interest between the broker-dealer or adviser and its customer or not, and whether that divergence concerns a duty of the broker-dealer or adviser. Participants in the marketplace legitimately and properly consider their own interests regularly and in countless ways; their doing so is no proxy, or close approximation, to the far narrower range of circumstances where a "conflict of interest" arises because one party's interests conflict with another's *and* the party is to be acting as the agent for the other.

Yet here, for example, the Proposal would regulate as a "conflict of interest" a technology that alerted customers to the risk of a potential margin call, on the ground that the broker-dealer has an interest in the customer having sufficient funds in his or her account. But that is not a conflict; the customer *also* has an interest in having sufficient funds in his or her account. The fact that a broker-dealer or adviser *has* an interest does not mean that the interest conflicts with that of its customer, and even if it does, that does not mean that the conflicting interests have anything to do with the duties of the broker-dealer or adviser.

The immediate statutory context further undermines the Commission's overbroad conception of "conflict of interest." The statutory provisions on which the Commission relies in Section 15(l) of the Exchange Act and Section 211(h) of the Advisers Act grant rulemaking authority to restrict "sales practices, conflicts of interest, and compensation schemes."[118] Under the interpretive principle of *noscitur*

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[113] Proposing Release at 53,982.

[114] *Id.* at 53,981.

[115] Regulation Best Interest, 84 Fed. Reg. at 33,319.

[116] *Conflict of interest*, *Black's Law Dictionary* (11th ed. 2019).

[117] Proposing Release, 88 Fed. Reg. at 53,982.

[118] 15 U.S.C. §§ 78o(l)(2), 80b-11(h)(2).

*a sociis*, "words grouped in a list should be given related meanings."[119] Here, the phrases "sales practices," "conflicts of interest" and "compensation schemes" refer to structural incentives, generally operating at the point of sale, such as sales contests, that may encourage a broker-dealer or investment adviser to push an investor into an unsuitable transaction.[120] The words cannot reasonably be read to reach *any* "communicat[ion]" with an investor, or the provision of *any* "information to an investor,"[121] no matter how related (or not) the communication or information is to a proposed transaction.

#### 4. The Proposal Is Contrary To The Public Interest And The Protection Of Investors.

The Proposal exceeds the Commission's authority in a final way: it is contrary to the "public interest and the protection of investors."[122] The Commission provides no support for its blanket assertion that alleged "conflicts" associated with technology currently present any special threat to investors. In fact, as discussed elsewhere in this comment, the Commission's Proposal will discourage technology and innovation, stifle competition, and ultimately disempower investors.[123]

### B. The Statutory Structure And Context Confirm That Congress Did Not Intend To Grant The Commission The Authority It Claims.

What the statute's text shows, its structure and context confirm: Section 15(l)(2) is not a plausible source of authority for the Commission's attempt to regulate a broker-dealer's use of virtually any form of technology in any investor interaction.

Section 15(l)(2) was enacted as a part of the Dodd-Frank Act, which required the Commission to "conduct a study to evaluate" the existing standards of care for broker-dealers and identify "legal or regulatory gaps" in the governing framework relating to the provision of "personalized investment advice about securities to retail

[119] Antonin Scalia & Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts* 195 (2012) (quoting *Third Nat'l Bank in Nashville v. Impac Ltd., Inc.*, 432 U.S. 312, 322 (1977)).

[120] *See, e.g.*, Regulation Best Interest, 84 Fed. Reg. at 33,454 (And the SEC at the time understood the limitations of its rulemaking authority under Section 15(l)(2). In a section titled "Elimination of Certain Sales Practices," the SEC required broker-dealers only to "establish, maintain, and enforce written policies and procedures reasonably designed to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sale of specific securities or specific types of securities within a limited period of time," because "the conflicts of interest associated with these practices [] may create high-pressure situations for the associated persons of the broker-dealer to recommend a specific security over another").

[121] Proposing Release, 88 Fed. Reg. at 54,023.

[122] 15 U.S.C. §§ 78o(l)(2), 80b-11(h)(2).

[123] *See supra* Section I.A; *infra* Section IV.

customers."[124] The Dodd-Frank Act then authorized the Commission to promulgate rules setting a standard of conduct for broker-dealers and—in a subsection entitled "Other Matters"—prohibit certain sales practices, conflicts of interest, and compensation schemes.[125] The Commission's implementation of the Dodd-Frank Act ultimately culminated in the adoption of Reg BI, which requires broker-dealers to "act in the best interest of the retail customer at the time the recommendation is made."[126]

If Section 15(l)(2) were as broad as the Proposal claims, the statute's charge to study, assess, and promulgate rules concerning a standard of conduct would be superfluous—the Commission could promulgate those same rules as regulations of conflicts of interest. The statute should not be read in such a self-defeating way.[127] Rather, the only interpretation that harmonizes these distinct rulemaking powers is the one that accords with its plain meaning. Section 15(l)(2) targets specific conflicts of interest that the general standard could not address directly.

Reg BI is a perfect example of this interplay. After relying on the Commission's authority under Section 913(f) of the Act to set the general standard of conduct for disclosing conflicts of interest, it then (invoking authority under Section 15(l)(2)) requires broker-dealers to "eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time."[128] These are *specific* types of harmful sales practices and conflicts that could not be spelled out by the overarching standard. In contrast, the Proposal would cover *any* conflict of interest implicated in the use of technology and effectively create a new general standard of conduct, which Section 15(l)(2) does *not* authorize.

Moreover, if the authority granted in Section 15(l)(2) were broad enough to cover all conflicts of interest—including all conflicts touching on almost every technology that is used by a broker-dealer or investment adviser in any interaction with retail investors—Congress surely would not have tucked the provision away in a subsection unassumingly entitled "Other Matters."[129] Courts presume that Congress will "speak clearly" if it wants to delegate issues of major political or economic significance to

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[124] Pub. L. No. 111-203, § 913(b)–(d), 124 Stat. 1376, 1824–27 (2010).

[125] Pub. L. No. 111-203, § 913(f)–(g), 124 Stat. at 1827–29.

[126] 17 C.F.R. § 240.15l-1(a)(1).

[127] *See Food & Drug Admin. v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133 (2000) (quoting *FTC v. Mandel Brothers, Inc*., 359 U.S. 385, 389 (1959) (statutes must be construed to "fit, if possible, all parts into an harmonious whole")).

[128] 17 C.F.R. §§ 240.15l-1(a)(1), 240.15l-1(a)(2)(iii)(D).

[129] 15 U.S.C. § 78o(l).

administrative agencies like the Commission.[130] Congress has given no indication whatsoever here that it intended this "ancillary" provision—whose own title suggests it is meant to be a "gap filler"—to vest the Commission with power to regulate the use of almost every form of technology in the securities industry that provides inputs into an investor interaction (and all conflicts of interest as they arise in that sphere).[131]

### C. The Proposal Violates The First Amendment.

Statutory authority aside, the Proposal violates the First Amendment. Broker-dealers such as Robinhood have a First Amendment right to communicate with their customers, but the Proposal impermissibly burdens that right based on the content of the broker-dealer's speech. Before the broker-dealer can "interact[]" (i.e., speak) with its customers through virtually any form of technology, the broker-dealer must, under the Proposal, adopt and implement onerous procedures. The First Amendment does not allow the Commission to constrain speech in this way.

Strict scrutiny applies here. The Proposal would adopt "content-based" and "speaker-based" restrictions on speech.[132] It applies to broker-dealer's interactions with their customers and turns in large part on the content of that speech—whether the broker-dealer is "optimiz[ing] for, predict[ing], guid[ing], forecast[ing], or direct[ing] investment-related behaviors or outcomes," for example, by "providing information to [the] investor," "soliciting [the] investor," or "providing … general administrative support."[133]

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[130] *West Virginia v. Env't Protection Agency*, 142 S. Ct. 2587, 2605 (2022).

[131] *Id.* at 2610; *Whitman v. American Trucking Ass'ns, Inc.*, 531 U.S. 457, 468 (2001) (Congress "does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions—it does not, one might say, hide elephants in mouseholes.").

[132] *Sorrell v. IMS Health Inc.*, 564 U.S. 552, 565–66 (2011).

[133] Proposed Rule 15l-2(a), Proposing Release, 88 Fed. Reg. at 54,023. The Proposal's application similarly turns on the speaker. Specifically, it targets the speech of those who communicate over digital platforms and not those who communicate through more traditional forms of communication used by broker-dealers and financial advisers—such as financial publications that routinely publish lists or information about the most active stocks or other widely traded securities. The selective burdening of those who communicate digitally is subject to strict scrutiny. *See infra*, Section IV.C; *Reed v. Town of Gilbert, Ariz.*, 576 U.S. 155, 170 (2015) ("Because speech restrictions based on the identity of the speaker are all too often simply a means to control content, we have insisted that laws favoring some speakers over others demand strict scrutiny when the [law's] speaker preference reflects a content preference." (internal citations and quotation marks omitted)).

The Proposal cannot survive strict scrutiny. It is not narrowly tailored to promote a compelling government interest.[134] And there are less restrictive alternatives that would serve the Commission's purposes anyway.[135]

First, in the First Amendment context, the government cannot "rest on 'speculation or conjecture.'"[136] It needs evidence. And, here, the record lacks any evidence that the Proposal would in fact further a compelling government interest. On the investor-protection front, however, the Commission has not come close to meeting its burden. The Commission has not shown that broker-dealers' use of technology is somehow hurting investors; in fact, the record shows that the opposite is true.

Moreover, the Proposal is anything but narrowly tailored. This is not like the Commission's ordinary disclosure requirements. Rather than require the simple disclosure of true and factual information, the Proposal *prohibits* the communication of true and factual information pending the creation of costly policies and procedures and, in other instances, the elimination of conflicts of interest. And to the extent there is an "actual [investor protection] problem in need of solving"[137]—which there is not—the Proposal sweeps in far too many innocent and protected interactions (including those involving a simple spreadsheet or the communication of a change in stock price) to be "the least restrictive alternative that can be used to achieve" the Commission's asserted interests.[138]

The Commission cannot proceed with the expectation that a lesser degree of First Amendment scrutiny will apply here, as it could in the case of so-called "professional speech." Even if this *were* professional speech, and professional speech is a "difficult category to define with precision," the Supreme Court has held that the "ordinary First Amendment principles" discussed above apply anyway.[139] The Proposal would not survive even a lesser level of constitutional scrutiny. Under intermediate scrutiny, the Proposal fails because the Commission has not shown why less-restrictive alternatives, such as disclosure, would be inadequate.[140] Moreover, as discussed elsewhere in this letter, the Proposal is far more extensive than necessary to serve the Commission's purpose.[141] Thus, under even lesser scrutiny, the Proposal fails because it is "unjustified," "unduly burdensome," and "broader than reasonably

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[134] *See Nat'l Inst. of Family & Life Advocates v. Becerra*, 138 S. Ct. 2361, 2371 (2018).

[135] *See id.* at 2376.

[136] *Nat'l Ass'n of Mfrs. v. Sec. & Exch. Comm'n*, 800 F.3d 518, 526 (D.C. Cir. 2015).

[137] *Brown v. Ent. Merch. Ass'n*, 564 U.S. 786, 799 (2011) (internal quotation marks omitted).

[138] *Ashcroft v. Am. C. L. Union*, 542 U.S. 656, 666 (2004).

[139] *Nat'l Inst. of Family & Life*, 138 S. Ct. at 2375.

[140] *Nat'l Ass'n of Mfrs.*, 800 F.3d at 555-56.

[141] *Id.*

necessary."[142] Simply put, under any standard, the Proposal cannot survive First Amendment scrutiny and, accordingly, should be withdrawn.

## IV. Beyond The Issues With The SEC's Lack Of Authority And Basis For The Proposal, The Proposal Is Bad Policy That Is Unlawful For A Multitude Of Other Reasons.

The Proposal is arbitrary and capricious because it contradicts the SEC's recently adopted Reg BI and Fiduciary Interpretation, including the longstanding tradition of relying on a disclosure-based framework to address conflicts of interest. It is also ill-advised policy because it would disempower investors and discourage technology and innovation. The Proposal contradicts the SEC's rulemaking mandate because it would discourage efficiency, competition, and capital formation.[143] Not only does the SEC fail to identify any credible benefits of the Proposal, but it also acknowledges that the Proposal has the potential to impose significant costs and burdens on market participants and investors. Such a rulemaking is not necessary, appropriate, or in the public interest.

### A. The Proposal Cannot Be Squared With The SEC's Recently Adopted Reg BI Or The SEC's Longstanding Tradition Of Relying On A Disclosure-Based Framework To Address Conflicts Of Interest For Broker-Dealers.

As we discuss above, throughout its history including as recently as Reg BI, the SEC has allowed market participants to rely on disclosure to cure conflicts of interest. Congress, the SEC, and the SROs have deemed disclosure sufficient to address conflicts of interest in a variety of contexts, including complex products.[144] The SEC would cast aside years of developed policy that is grounded in real statutory authority and the product of significant study and real-world application to establish a new and costly framework that applies only to the use of technology on the basis of highly speculative potential benefits.

The SEC recognizes that broker-dealers "are currently subject to extensive obligations under Federal securities laws and regulations, and … rules of [SROs (in particular, FINRA)], that are designed to promote conduct that, among other things, protects investors … from conflicts of interest."[145] Advisers similarly do not need specific new rules to govern their use of technology. As the SEC recognizes, advisory relationships with clients are governed by fiduciary duties, and the existing antifraud provisions of the Advisers Act and the rules thereunder provide a protective overlay on an adviser's

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[142] *Nat'l Inst. of Family & Life*, 138 S. Ct. at 2377.

[143] *See* 15 U.S.C. §§ 78c(f); 78w(a)(2); 80b-2(c).

[144] *See, e.g.*, Section 17(b) of the Securities Act, Section 15D of the Exchange Act; Exchange Act Rules 10b-10, 15c1-5, 15c1-6, 17g-5, 17g-7, Reg BI, Form CRS, Regulation AC, Regulation NMS Rules 606 and 607; FINRA Rules 2210, 2241, 2242, 2262, 2269, 5121, 5122; Municipal Securities Rulemaking Board Rules G-22 and G-42 (relating to broker-dealer conflicts of interest).

[145] Proposing Release, 88 Fed. Reg. at 53,965-66 (footnote omitted).

relationships with clients and fund investors.[146] The SEC's sticking point is that these firms do not have a specific obligation to address conflicts of interest resulting from technology in every investor interaction. But these firms do not need specific obligations with respect to the use of technology—they currently have rules that govern their conduct irrespective of their use of technology in appropriate circumstances. The primary basis for addressing them is, and historically has been, disclosure.

Without articulating why technology would pose such a significant risk of investor harm, the SEC now would depart from this decades-long standard not just where there has been recognition of heightened risks (such as a recommendation under Reg BI) but in *any* investor interaction. As discussed above, this departure has no basis in law or fact, and it would deprive investors of valuable information and tools to plan for their financial well-being and future.

**B. The Proposal Disempowers Investors.**

The Proposal smacks of contempt for the ordinary person, who under the SEC's apparent world view is incapable of thinking for himself or herself. Robinhood customers have made a conscious decision to be self-directed investors—they don't necessarily *want* someone else taking investment decisions or information relevant to such decisions out of their hands. Many of these customers also want the ability to choose more than one model to meet their investment needs, for example, a managed account or full-service brokerage account along with the ability to make their own investment decisions through self-directed platforms. Others are unable to access full-service brokerage or advisory services, due to factors like cost or geography. Investors want access to technologies that give them more useful choices, tools, and information, not regulation that would seek to take those choices, tools, and information away.

The SEC's rejection of disclosure as a means to cure potential conflicts of interest is the worst example of demeaning paternalism. The requirement to "eliminate or neutralize the effect of" a conflict of interest associated with the use of technology rather than disclose potential conflicts tells investors one thing: *we think we know better than you*. Instead, the SEC would remove retail investors' ability to use the same technologies that institutional investors use. And those retail investors would have to pay more for using lesser technologies because of the additional costs introduced by the Proposal.

**C. The Proposal Is Blatantly Anti-Technology, Anti-Innovation, And Anti-Commerce.**

The Proposal purports to be "principles based" and "technology neutral," but in reality it is highly prescriptive and broadly anti-technology. The Proposal also purports to address "predictive data analytics" but goes far beyond that. The SEC's

[146] *Id*.

overly broad approach will impact technologies that are mundane as well as the more advanced technologies, like AI, NLP, and machine learning, that the Proposal is ostensibly designed to address. However, even if the Proposal were specifically targeted at those more advanced technologies, the Proposal would make it too costly and burdensome for firms to use those technologies for the benefit of their customers and clients. The SEC would stifle innovative ideas and uses of technology that could lead to significant cost savings, improve the overall investor experience, and continue to open the markets to more investors. This approach is not only bad for business, markets, and investors, but also contrary to the SEC's own mandate. The SEC and SEC officials have recognized the promise that innovative new technologies can have in the marketplace countless times and have demonstrated a commitment to fostering innovation.[147] It would be antithetical to the SEC's mission and its own historical approach to the use of technology to proceed with the Proposal.

Multiple times in the Proposing Release, the SEC recognizes the potential harm that the Proposal could generate by undermining the use of technology by broker-dealers and investment advisers: "Not only could this harm the firm and investors due to, for example, foregone cost savings, lack of tailoring of recommendations to individual investors, or unimplemented user experience improvements, but it also could slow down technological innovation and progress more broadly."[148] The SEC also acknowledges that capital formation could be hindered "to the extent that the costs of the technology are too high and firms avoid using certain covered technologies that benefit investors" or the Proposal "deter[s] firms from using covered technologies in investor interaction."[149] (It is ironic the Commission evidently believes it's sufficient to "disclose" such fatal flaws, rather than "eliminating" the problems by totally re-writing or abandoning the Proposal.) These are serious concerns that we think are likely, if not absolutely certain, to transpire. And they are not offset by the speculative benefits that the SEC believes the Proposal might offer. The Proposal instead would delay and deter U.S. broker-dealers and investment advisers from implementing technology across their businesses. It would put the U.S. securities industry at a significant disadvantage to other industries and to financial institutions in other

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[147] Press Release, SEC, *SEC Announces Office Focused on Innovation and Financial Technology* (Dec. 3, 2020), https://www.sec.gov/news/press-release/2020-303; Press Release, SEC, *SEC Launches New Strategic Hub for Innovation and Financial Technology* (Oct. 18, 2018), https://www.sec.gov/news/press-release/2018-240; SEC Strategic Plan Fiscal Years 2018-2022, https://www.sec.gov/files/SEC_Strategic_Plan_FY18-FY22_FINAL.pdf; Kara M. Stein, Comm'r, SEC, *Supporting Innovation Through the Commission's Mission to Facilitate Capital Formation* (Mar. 5, 2015), https://www.sec.gov/news/speech/innovation-through-facilitating-capital-formation; Paul S. Atkins, Comm'r, SEC, *Speech by SEC Commissioner: Remarks at Vanderbilt University* (Oct. 20, 2006), https://www.sec.gov/news/speech/2006/spch102006psa.htm.

[148] Proposing Release, 88 Fed. Reg. at 54,011.

[149] *Id*. at 54,012.

jurisdictions. The SEC's approach is not only bad for U.S. markets and investors, but also it is at odds with the approach that other U.S. government agencies are taking, which is to recognize and embrace the benefits of technology.[150]

The Proposal combines the SEC's unsubstantiated suspicion of technology with a hostility toward commerce that is entirely misplaced in a regulator charged with overseeing markets and furthering capital formation. The Proposal seemingly rejects the notion that a broker-dealer is a person who is "engaged in the business" of effecting securities transactions or buying and selling securities by requiring a broker-dealer to jump through hoops any time it seeks to consider the "business" in its interactions with customers. As a business, a broker-dealer has obligations to its own investors and stakeholders as well as its customers. Accordingly, every decision a broker-dealer makes is a *business* decision and takes into account the interests of the firm. The Proposal would characterize the natural workings of a business as a malignant conflict of interest that is harmful to investors.[151] However, the Proposal fails to consider that having something work from a business perspective is a prerequisite to any customer offering—otherwise, the business would not be able to support any of its customers for long. The Proposal would make it harder for firms to make necessary, day-to-day business decisions by requiring them to perform an onerous calculus any time they make a customer-facing change. The Proposal's subversive treatment of normal business processes is unbecoming of a regulator that is intended to regulate the financial system and antithetical to a society that values commerce and entrepreneurship.

### D. The Proposal Will Reduce Efficiency, Stifle Competition, And Deter Capital Formation.

The Exchange Act and Advisers Act require the Commission to determine whether a rulemaking will "promote efficiency, competition, and capital formation."[152] The Proposal fails to achieve any of these objectives and, in fact, will have the opposite effect.

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[150] *See, e.g..,* David Vergun, *DOD Will Deploy AI-Enabled Detection System to Monitor D.C. Airspace*, DOD NEWS (Aug. 28, 2023), https://www.defense.gov/News/News-Stories/Article/Article/3507329/dod-will-deploy-ai-enabled-detection-system-to-monitor-dc-airspace/; IRS, IR-2023-166, *Agency Focus Will Shift Attention to Wealthy from Working-Class Taxpayers; Key Changes Coming to Reduce Burden on Average Taxpayers While Using Artificial Intelligence and Improved Technology to Identify Sophisticated Schemes to Avoid Taxes* (Sept. 8, 2023), https://www.irs.gov/newsroom/irs-announces-sweeping-effort-to-restore-fairness-to-tax-system-with-inflation-reduction-act-funding-new-compliance-efforts.

[151] The Proposal presumes that broker-dealers are inherently conflicted and have no incentive to manage their conflicts. The opposite is true—broker-dealers are incentivized to manage and mitigate conflicts of interest and not engage in activity that would cause a negative customer experience. That would be bad for retaining customers and bad for business.

[152] 15 U.S.C. §§ 78c(f), 80a-2(c), 80b-2(c).

### 1. The Proposal Will Negatively Affect Competition.

With regard to competition, the Proposal will make it harder for new broker-dealers and investment advisers to break into the industry by introducing new and additional costs and making it harder and more expensive to rely on third-party technology service providers. This problem hits close to home for us at Robinhood. We began as a startup company with an innovative idea for an app that would make investing more accessible. The Proposal would have stifled Robinhood's own growth and now threatens to do the same to future innovators.

Moreover, many smaller firms rely on third-party vendors for technology because they do not possess the internal resources to produce or manage those technologies. The Proposal would make it more challenging to outsource technology solutions, creating barriers to entry and innovation and favoring larger incumbents who have the resources to manage technology in-house.

By introducing significant new costs associated with the use of technology, the Proposal would erect barriers that make it harder for new, innovative solutions to reach investors. While purportedly trying to put guardrails in place, the SEC instead would create a two-tiered system of broker-dealers and investment advisers—one with the resources to use complex technologies and the other without.

Indeed, the SEC concedes that the effects of the Proposal will be harmful to competition:

- "The proposed conflicts rules could also result in costs that could act as barriers to entry or create economies of scale, potentially making it challenging for smaller firms to compete with larger firms utilizing covered technologies—as firms continue to increasingly rely on covered technologies for investor interactions."[153]
- "Ensuring compliance with the proposed conflicts rules would require additional resources and expertise, which could become a significant barrier to entry, potentially hindering smaller firms from entering the market or adopting new technologies."[154]
- Larger firms "may have a competitive advantage over smaller firms because they may be better able to spread the (fixed) cost of the proposed conflicts rules across their clients, or more effectively negotiate with third party providers to obtain compliant technology externally."[155]
- "Smaller firms subject to the proposed conflicts rules could also face a competitive disadvantage compared to larger firms when negotiating with

[153] Proposing Release, 88 Fed. Reg. at 54,012.

[154] *Id*.

[155] *Id*.

technology companies to build software that complies with the proposed conflicts rules."[156]

The so-called "positive" effects on competition that the SEC identifies are speculative and unconvincing: (1) investors could have greater confidence in interactions with firms using covered technology and therefore be more likely to participate in financial transactions; and (2) investors will put additional weight on fees and execution quality. Putting aside the fact that these effects have nothing to do with increasing competition among securities firms, the SEC has failed to quantify them or set forth any compelling evidence that they are real problems in need of regulatory solutions. Investors are already focused on fees and execution quality and receive extensive information about fees and execution quality today. The Proposal will not affect the way that fees and execution quality are presented to investors, so it is nonsensical to cite this as a potential effect of the Proposal.

**2. The Proposal Will Negatively Affect Efficiency.**

The Proposal would negatively impact efficiency by making it more difficult for firms to use technology when communicating with investors because of the new, onerous obligations that would be imposed on firms using technology. This is contrary to what Congress envisioned when it established the SEC in 1934 with the instruction to maintain fair, orderly, and efficient markets, when it directed the establishment of a national market system linked through technology in 1975, and when it embarked on modernizing securities regulation at the dawn of the Internet Age and enactment of the Dodd-Frank Act. The SEC concedes the Proposal could negatively impact technology in its economic analysis: "The proposed conflicts rules could negatively affect efficiency by impeding the use of technology in several ways."[157] The SEC then proceeds to identify numerous real ways that the Proposal could negatively impact efficiency:

- "First, the compliance costs of the proposed conflicts rules could dissuade some firms from using covered technologies in investor interactions. For example, a firm might decide that using a chatbot technology that provided investment advice would be too costly because of the obligations imposed by these rules, and instead opt for human alternatives. To the extent that the chatbot technology was more efficient at providing support to investors, the efficiency of the firm's ability to provide advice would be decreased."[158]
- "Second, certain types of technology might be too difficult or costly to evaluate, or to modify to comply with the rules, and firms could avoid using these technologies.... In these cases, firms and investors would not enjoy any

[156] *Id*.

[157] *Id.* at 54,011.

[158] *Id*.

of the efficiency gains that the covered technology might have yielded, or have yielded if already implemented."[159]

- "Third, the costs and requirements could slow down the frequency or overall rate of technological updates to existing covered technologies and exploration of new covered technologies, as well as make the technology itself less efficient... Not only could this harm the firm and investors due to, for example, foregone cost savings, lack of tailoring of recommendations to individual investors, or unimplemented user experience improvements, but it also could slow down technological innovation and progress more broadly."[160]

Notably, the SEC identifies only a single way that the Proposal could positively impact efficiency: investors might have "greater confidence regarding the conflicts of interest associated with the use of covered technologies that they interact with."[161] Putting aside the fact that this potential outcome has nothing to do with the efficiency of the securities markets, this statement is wholly speculative, and the SEC fails to provide any credible support for it.

**3. The Proposal Will Negatively Affect Capital Formation.**

The SEC again identifies very real, negative effects of the Proposal on capital formation. Specifically, the SEC acknowledges that the costs associated with the Proposal could "result in increased fees for investors or deter firms from using covered technologies in investor interaction," which would hinder capital formation.[162] The SEC admits that this "could be particularly problematic for smaller firms who may struggle to absorb these additional costs."[163] Finally, the SEC concedes that because the Proposal will impose additional costs on firms' use of technology, firms could "avoid using certain covered technologies that benefit investors" and, as a result "capital formation could be hindered."[164]

Flagrantly disregarding its mandate, the Proposal fails to account—as it must—for the adverse impact it would have on capital formation, by deterring trading activity. An animating belief of the Proposal, albeit unsupported by the facts, is that technology is making it "too easy" for broker-dealers to reach investors, too easy to inform them of trades that might be of interest, and too easy to execute those trades. The Commission is sorely mistaken to view these aspects of technology as a problem. But in proposing a rule that is designed to complicate and, in some cases, "restrict" or

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[159] *Id*.

[160] *Id*.

[161] *Id*. .

[162] *Id*. at 54,012.

[163] *Id*.

[164] *Id*.

"eliminate" these interactions, a central obligation of the Commission is to explain what the consequences will be for the markets and capital formation. Simply, the Commission cannot set out with the purpose of making it harder to market securities, without carefully documenting the impact on capital formation.

Notably, the SEC identifies only one way that capital formation could be positively affected: "the elimination or neutralization of the effects of certain harmful conflicts of interest … could enhance capital formation if the quality of services is improved or investment performance or execution quality is improved, and investors … invest more as a result."[165] Putting aside the fact that there is no support or basis for these statements, they are nonsensical because they contradict other statements by the SEC. The quality of services provided to investors will not be improved because the Proposal will make it more expensive and difficult for firms to provide beneficial technology to customers, as the SEC admits. And it is nonsensical to claim that the Proposal could improve execution quality; the Proposal has nothing to do with how securities transactions are executed,[166] and the SEC admits that the Proposal could make investing more expensive for retail customers through higher fees, which logically would lead to worse execution quality and less investment.

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Robinhood appreciates the opportunity to comment on the Proposal. The Proposal is a blunt instrument that would seek to regulate a wide swathe of broker-dealer and investment adviser conduct without any nuance. Although it purports to regulate the use of PDA and PDA-like technologies, the Proposal would extend far beyond that, applying to nearly any technology—even basic technologies—that could be used in an interaction with an investor. The SEC does not appreciate the significant costs and burdens the Proposal would impose on firms or the benefits that investors would stand to lose if the Proposal were adopted. Nor does it sufficiently consider the other rules that overlap and may conflict with the Proposal's requirements—creating a compliance nightmare for firms trying to figure out how to apply this framework. Instead, the Proposal takes a regressive, hostile view of the use of technology by firms without articulating a basis for or undergoing a data-driven analysis to support the need for the Proposal. The result would be an unmitigated disaster for retail investors, who will be sidelined from full and fair participation in the U.S. financial markets, while institutional investors not impacted by the Proposal continue to have access to important investment tools. The Commission's authority to adopt the Proposal also rests on shaky ground—not only is the Proposal outside of the SEC's statutory authority and inconsistent with the Commission's mandate to promote efficiency, competition, and capital formation, but the Proposal also presents significant constitutional issues that call into question its legitimacy.

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[165] *Id*.

[166] And, in fact, the SEC excludes back-office execution and trade processing functions from the proposed rules. *See id*. at 53,974.

For all these reasons, the Commission should withdraw the Proposal.

Please contact Robinhood's Deputy General Counsel, Lucas Moskowitz, at lucas.moskowitz@robinhood.com if you have any questions or comments.

Sincerely,

DocuSigned by:

Dan Gallagher

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Daniel M. Gallagher

Chief Legal and Corporate Affairs Officer

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