



Via electronic submission to NASAAComments@nasaa.org

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North American Securities Administrators Association, Inc. (NASAA)
Attn: Amy Kopleton, Group Chair, Broker-Dealer Market and Regulatory Policy and Review Project, Stephen Bouchard, Former Chair, Broker-Dealer Section, James Nix, Chair, Broker-Dealer Section
750 First Street, N.E., Suite 990
Washington, D.C. 20002

December 4, 2023

Re: Proposed Revisions to NASAA's Model Rule on Dishonest or Unethical Business Practices of Broker-Dealers and Agents dated September 5, 2023 (the "Proposal")

Dear NASAA, Ms. Kopleton, Mr. Bouchard and Mr. Nix:

We the undersigned trade associations appreciate the opportunity to comment on the North American Securities Administrators Association (NASAA) proposed revisions to its Model Rule on Dishonest and Unethical Business Practices of Broker-Dealers and Agents dated

September 5, 2023 (the “Proposal”).¹ We collectively represent a broad cross section of the financial services industry, and many of our members do business and serve retail investors, state and federal governments, corporations and institutional investors across the country.

Most of our associations will also be submitting separate comment letters focused on issues of specific importance to our respective members. However, we write to highlight issues of common interest and concern among our organizations as you engage in your comment review process. Moreover, for the reasons set forth below, we join together in requesting that the Proposal, as drafted, not be adopted at this time.

There are several reasons that, individually and in sum, warrant withdrawal of the proposal. Among other issues, the Proposal:

- Conflicts with the Securities and Exchange Commission’s (SEC) Regulation Best Interest (Reg BI)²;
- Conflicts with the National Association of Insurance Commissioners’ (NAIC) Suitability in Annuity Transactions Model Regulation (NAIC Model);
- Raises serious preemption concerns under the National Securities under the National Securities Markets Improvement Act (NSMIA);
- Exceeds necessary model language to incorporate Reg BI protections in state rules;
- Contributes to regulatory uncertainty and fragmentation;
- Would be harmful to investors and their financial professionals.

Overall, we believe that the Proposal, while seeking to protect investors and improve investment outcomes, will unintentionally harm investors by reducing access to, and limiting choice of, investment products and services. Our concerns rest largely on the fact that the Proposal diverges from, and materially conflicts with, existing standards governing the relationship between investors and their financial professionals.

Our organizations have supported regulations requiring that investors receive investment advice and recommendations that are in their best interests. We also believe it is essential that financial institutions and professionals provide clear disclosures regarding the nature of their services, their fees and compensation and material conflicts of interest so that investors are empowered to make informed decisions. At the same time, we believe such standards and requirements should be adopted in a way that preserves investor choice and access to a wide range of investment and financial services.

It is our view that investors are best served with a single, consistent standard across the nation, which preserves choice and access to investment service, reduces investor confusion and costs, facilitates compliance, and promotes overall investment services, advice and planning.

¹ <https://www.nasaa.org/wp-content/uploads/2023/09/Request-for-Public-Comment-on-BD-Best-Interest-Model-Rule.pdf>

² 17 CFR § 240.151-1

Such standards result in better savings and outcomes for all Americans, regardless of whether they work with a broker-dealer, investment adviser, or other financial professional.

I. The Proposal Conflicts with Regulation Best Interest

In June of 2019, the SEC adopted Reg BI and related rules and interpretations, creating a new, nationwide, heightened standard of conduct for broker-dealers and their representatives. Reg BI accomplishes our shared goal of elevating and harmonizing the standards that apply to retail investment advice and recommendations while preserving choice and access to services. Reg BI substantially raised the bar from the decades-long suitability framework for recommendations and codified meaningful new investor protections. Reg BI significantly and materially changed the way brokerage services are provided and impacts nearly every aspect of a broker-dealer's operations.

We are deeply concerned NASAA is proffering a different standard from Reg BI, even after the substantial investments and resources our members – across all our organizations – have made to ensure that they serve their clients' best interests and comply with Reg BI. Financial firms and professionals continue to fine-tune operations and compliance in light of subsequent SEC staff guidance and examinations by the SEC, Financial Industry Regulatory Authority (FINRA) and state securities regulators.

The Proposal directly conflicts with Reg BI in multiple ways, including four which we would like to highlight here:

- 1) The Proposal vastly and inappropriately expands the definition of “recommendation” under Reg BI (Subpart 1.d.(5)).

Subpart 1.d.(5) of the Proposal states:

*“The obligations set forth in this section do not apply to unsolicited transactions that a broker-dealer or agent execute for a customer in a self-directed or nondiscretionary account. If the broker-dealer or agent utilized **any means, method or mechanism to feature or promote** an account type, specific security or investment strategy to a retail customer, whether directly or through a third-party, 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).

This language constitutes a wholesale redefinition of what constitutes a recommendation under Reg BI and long-standing SEC and FINRA interpretations and guidance. The SEC and FINRA have always anchored the definition of recommendation to a “call to action” analysis.³ At the same time, the SEC and FINRA have also provided clear and specific examples of when a recommendation has been made and when it has not.⁴

³ Reg BI Adopting Release (“**Adopting Release**”) at pp. 79-80 and fn 164, and p. 104, <https://www.sec.gov/files/rules/final/2019/34-86031.pdf>.

⁴ See, e.g., FINRA Notice 01-23, Suitability Rule and Online Communications (Apr. 2001), <https://www.finra.org/rules-guidance/notices/01-23> (providing clear and specific examples of when a

It is difficult, if not impossible to contemplate how a firm could build a supervisory system and written supervisory procedures reasonably designed to supervise against the broad phrase “*any* means, method or mechanism” (emphasis added) that “feature[s] or promote[s]” an account type, security or strategy. This is especially so given that Reg BI requires firms to focus their policies, procedures, testing, training, supervision, and other documentation premised upon a financial advisor making an actual “recommendation” of an account type, security or investment strategy (per the current, well-understood SEC and FINRA definitions and interpretive guidance). Here, the Proposal suggests a seemingly impossible standard, i.e., determining what is in a customer’s best interest at the point in time that the firm is merely “featuring” or “promoting” an account type, security or strategy.

2) The Proposal rewrites the Conflicts of Interest Obligation under Reg BI (Subparts 1.d.(1) and (2)). The Proposal states that disclosure alone is not sufficient to meet best interest standard in Reg BI. This is in direct conflict with Reg BI, which requires firms to assess all conflicts and manage them according to their type and severity.

The Proposal contends that this revision, “is straightforward and incorporates SEC guidance from the Adopting Release (and repeated elsewhere) directly into the text of the model rule.” Clearly, had the SEC wanted to codify this guidance it could have done so, rather than include it in the Adopting Release. We do not find it compelling that in the months following Reg BI’s implementation that NASAA felt firms relied too heavily on disclosure. Reg BI includes sufficient authority to address situations in which there is an over-reliance on disclosure or where disclosure does not otherwise satisfy Reg BI’s obligations. There is no need to diverge from Reg BI when regulators have sufficient authority to enforce the Conflicts of Interest Obligations. By doing so, the Proposal invites different interpretations as a result of application, unnecessarily causing confusion for regulators, firms, advisors, and investors alike.

3) The Proposal’s treatment of “cash or non-cash compensation” (Subpart 1.d.(2)b.) and the presumption that any form of compensation other than sales charges and 12b-1 fees are not in the best interest of the customer and would therefore be prohibited.

The Proposal’s “cash or non-cash compensation” provision conflicts with Reg BI.

Subpart 1.d.(2)b. of the Proposal states:

*“The broker-dealer or agent will be presumed to have placed its financial interest ahead of the interest of the retail customer where the broker-dealer or agent participates in (i) sales contests; (ii) sales quotas; (iii) bonuses; or (iv) any other non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time, **or rewards the broker-dealer or agent with additional cash or non-cash compensation beyond the sales commission as the result of that recommendation.**” (emphasis added).*

recommendation has been made in the context of online brokerage). See also SEC FAQs on Reg BI (Jan. 2020), <https://www.sec.gov/tm/faq-regulation-best-interest#recommendation> (providing additional concrete examples of what constitutes a recommendation subject to Reg BI).

The new bold italicized language above directly conflicts with not only Reg BI's regulatory requirements, but also Reg BI's overall compensation framework, which is designed to, and in fact does, promote retail investors' access to products, services, and best interest investment advice. This new provision would create a rebuttable presumption that the broker-dealer is placing its financial interest ahead of the customer if the broker-dealer receives *any* compensation beyond basic sales commissions.

By going beyond the requirements of Reg BI and creating a presumption of non-compliance, the Proposal would effectively prohibit broad categories of variable compensation programs which are otherwise structured to comply with Reg BI. For example, a firm that compensates representatives, in part, based on aggregate net flows of assets into customer accounts would need to overcome a presumption that this form of product-neutral compensation somehow presents a conflict of interest. In addition, firms would need different compensation models for the states that have adopted different versions (or no version) of the Proposal thereby making compensation disclosure highly confusing and most likely incomprehensible to customers.

Additional conflicts between Reg BI and the Proposal, include but are not limited to the expansion of customer profile information and inconsistency regarding the definition of "retail customer" demonstrate that the proposal materially differs from Reg BI in ways that suggest NASAA very carefully weigh the implications of adopting the Proposal.

4) The Proposal's "reasonably available alternatives" test directly conflicts with the Care obligation under Reg BI

Subpart 1d(3)(b) would require consideration of reasonably available alternatives that is inconsistent with the reasonably available alternatives test in Reg BI:

To satisfy this care obligation, a broker-dealer or agent shall make reasonable inquiry regarding lower-cost and lower-risk securities and investment strategies that are reasonably available to the broker-dealer or agent, as well as products or services available if the agent is also [licensed or registered] in other capacities such as an investment adviser representative or insurance agent.

Unlike the Proposal, Reg BI requires a lengthy and nuanced analysis that cannot be "simplified" into a choice merely between two products or one based solely on cost and risk. The Reg BI analysis must incorporate such factors as the investor's need for liquidity (or, presumably, lack thereof) and the potential benefits, risks and compatibility of the recommended security with the investor's profile. In fact, Reg BI *prohibits* a broker-dealer from limiting its evaluation to the cost and risk of any particular security or investment strategy. While the Proposal asserts that Subpart 1d(3) holds itself out as codifying a simplified form of the SEC's lengthy analysis, it in fact directly conflicts with Reg BI and would result in limiting the investment choice of products and services that may provide portfolio diversification and better achieve an investor's objectives.

II. The Proposal Conflicts with the NAIC Best Interest Model Rule

We also have serious concerns about creating a new standard that goes well beyond, and conflicts with, the enhanced updates to the Suitability in Annuity Transactions Model Regulation⁵ approved by the National Association of Insurance Commissioners (“NAIC”) in early 2020 (“NAIC Model”).⁶ The NAIC Model has already obtained widespread acceptance, with 40 states having adopted it as of December 1, 2023, in a substantially uniform manner.

Similar to Reg BI, the NAIC Model requires insurance producers to act in the best interest of the consumer under the circumstances known at the time a recommendation is made, without placing the producer’s or the insurer’s financial interest ahead of the consumer’s interest. In addition to the enhancements to the applicable standard of conduct and supervisory requirements, the revised model also reflects important adjustments to the training provisions and the FINRA safe harbor included in the prior version of the model.

The objectives of the NAIC Model and Reg BI are aligned, and the NAIC Model integrated Reg BI principles into the insurance regulatory framework (while creating a safe harbor for firms and agents that were complying with Reg BI). The NAIC spent many years on a robust process that considered feedback from multiple stakeholders while working through various issues. The NAIC was clearly committed to a transparent, inclusive process when working through these amendments. As a result, very clear policy decisions were made about what the standard should be. Adding a contradictory model to the regulatory landscape, such as the Proposal, would be inconsistent and problematic.

We are concerned that the Proposal’s significant departures from Reg BI and the NAIC Model would cause unnecessary confusion and compliance difficulties for dual registrants (state securities registered and insurance producers) offering annuities. The confusion and challenges can be exacerbated by the fact that annuities in some states are regulated as insurance products and in some states as securities.

III. The Proposal Raises Issues of Federal Preemption

In 1996 Congress passed the National Securities Markets Improvement Act (NSMIA)⁷ with the purpose of eliminating both duplicative and inconsistent regulations affecting the

⁵ See NAIC’s Suitability in Annuity Transactions Model Regulation (#275), available here: <https://content.naic.org/sites/default/files/model-law-275.pdf>.

⁶ While the official name of the NAIC Model refers to a suitability standard, the 2020 version replaced the suitability standard imposed under prior versions with a best interest standard that aligns with the standard established under Reg BI. The NAIC intentionally decided not to change the official name of the NAIC Model in order to avoid any uncertainty with respect to the requirements of Section 989J of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”). Under Section 989J of the Dodd-Frank Act, certain annuities are treated as exempt from the Securities Act of 1933 if, among other things, the NAIC Model (or a successor regulation that meets or exceeds the requirements of the version that was in effect when the Dodd-Frank Act was enacted by Congress) has been adopted by the state in which the annuity is issued or by the state of domicile of the insurance company that issues the annuity.

⁷ 15 U.S.C. § 78o(i)(1) (“No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall establish . . . making and keeping records . . . requirements for brokers, dealers, municipal

national securities markets and Investment Advisers and Broker-Dealers operating across state lines. Congress' stated objective in NSMIA was to preclude a "patchwork quilt of state regulation" on top of extensive federal securities laws and comprehensive SEC rules.

Congress determined that "dual Federal and state securities regulation resulted in a degree of duplicative and unnecessary regulation" that in many instances was "redundant, costly, and ineffective." (Conference Report) The Senate referred to this relationship as "confusing, conflicting, and involv[ing] a degree of overlap that may raise costs unnecessarily for American investors and the members of the securities industry." (Senate Report)

While our organizations continue to review the implications of the Proposal, it appears that at a minimum, it is inconsistent with the intent of NSMIA to the extent that the Proposal diverges from and exceeds Reg BI.

Additionally, many states regulate variable annuities as non-securities insurance products due to the preemptive nature of the McCarran—Ferguson Act, raising some questions about the scope and applicability of the Proposal with regard to those products. Finally, we have preemption concerns under ERISA and the Investment Advisers Act.

We note also that the provisions of Revision Set #2 of the Proposals are put forward as a list of options to be adopted in whole, in part, or not at all. Contrary to the assertion that the standardized options "promot[e] uniformity," we expect these provisions to have the opposite effect. As such, these provisions and all the deviations from Reg BI undermine the intent not only of NSMIA and the NAIC Model, but of the Uniform Securities Act itself.

IV. The Majority of the Proposal is Unnecessary to Incorporate Reg BI into State Securities Regulations

The Proposal goes far beyond what is necessary for states in order to align with Reg BI. We are deeply troubled that despite periodic dialogue by some of our organizations with NASAA leadership and the Broker-Dealer Section, it was only upon release of the Proposal that we learned that this NASAA initiative was also looking to address "significant changes that have occurred in the financial services industry in recent years, including the blurring of brokerage and advisory service models and the emergence of fintech and other digital investing platforms."

We strongly encourage NASAA to limit the scope of the Proposal to aligning states with Reg BI. Broader issues, including fintech and digital investing platforms, are the subject of current SEC rulemaking and NASAA proceeding at this time would risk a misalignment of regulation that could be extremely disruptive. Notably, NASAA members have been able to successfully pursue enforcement matters related to digital engagement, suggesting that there is no urgency to move forward ahead of the SEC and without more meaningful dialogue with stakeholders.

With regard to amending NASAA's model rules to Reg BI, we believe amendments are unnecessary because states already have the ability to protect investors and enforce Reg BI. We would not oppose, however, a revision that simply incorporates Reg BI by reference.

securities dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this chapter.").

V. Inconsistent Rules Lead to Regulatory Uncertainty

As noted above, firms and financial professionals have invested significant financial and other resources to ensure they are serving their clients' best interests and are otherwise complying with Reg BI., which became effective June 30, 2020. Subsequent to Reg BI's adoption, the SEC issued three separate staff bulletins to provide guidance, the most recent of which was released April 20, 2023, just seven months ago. Reg BI examinations conducted since adoption of Reg BI have helped guide firms as they adjust compliance to ensure they meet regulators' interpretations expectations.

This process – which is expected when implementing a major new regulation – has led to greater clarity, improved compliance, and greater investor protection. The process should be allowed to continue without the conflict and confusion that would arise from states adopting related rules that diverge from Reg BI.

Aside from the Proposal, investors are also facing the prospect of massive disruption that could come from the recent DOL-proposed “Retirement Security” rulemaking⁸ and the recent SEC proposal on predictive data analytics⁹ overlapping Reg BI and stretching its conflicts of interest obligation, even as firms are continuing to adjust operations and compliance in response to regulators' Reg BI interpretations and examinations. Further, the SEC has recently proposed changes to forms for variable annuities like RILAs.¹⁰ Now is not the time to add further regulatory changes that may result in inconsistencies and potentially conflicting or overlapping obligations.

VI. The Proposal Would Have a Negative Impact on Investors

Notwithstanding other significant disruptions and costs to firms that would result from the Proposal, we are genuinely concerned about the impact on investors. We believe the regulatory conflicts of the Proposal would negatively impact retail investors by limiting their choice of brokerage products and services and reducing their access to brokerage accounts, including self-directed brokerage accounts. The proposal suggests a presumption that the Broker-Dealer owes a fiduciary duty and characterize many routine client interactions as triggering such a duty. It would therefore likely accelerate the move from brokerage to fee-based accounts, thus raising the cost of providing advice and limiting investment choice, depriving small investors of the same opportunities for attaining their investment goals as institutional and large retail investors.

8 DOL Proposed Retirement Security Rule (Oct. 24, 2023), <https://www.dol.gov/sites/dolgov/files/ebsa/temporary-postings/retirement-security-rule-definition-of-an-investment-advice-fiduciary.pdf>.

9 Conflicts of Interest Associated With the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers, SEC Release No. 34-97990

10 SEC Proposal for a RILA Registration Form (Proposed rule: Registration for Index-Linked Annuities; Amendments to Form N-4 for Index-Linked and Variable Annuities (sec.gov))

Many investors would likely lose access to brokerage accounts which represent an important, cost-conscious choice for retail investors and provide access to affordable advice, particularly for smaller, buy-and-hold investors.

In short, we expect the Proposal would lead to diminished access to services and products that small investors need to help build wealth and save for retirement.

VII. Conclusion

The undersigned associations appreciate NASAA's goal of improving investor protection by incorporating Reg BI standards into state rules. However, insofar as the Proposal exceeds, conflicts with and diverges from Reg BI, it can unintentionally harm investors in addition to imposing unnecessary and difficult burdens on financial firms professionals. Therefore, we respectfully request that NASAA withdraw the Proposal at this time.

We appreciate the opportunity to comment on the Proposal and for and your consideration of our views.

Sincerely,

American Council of Life Insurers (ACLI)
American Securities Association (ASA)
Coalition for Business Development
Defined Contribution Alternatives Association (DCALTA)
Defined Contribution Real Estate Council (DCREC)
Financial Services Institute (FSI)
Finseca
Florida Securities Dealers Association (FSDA)
Institute for Portfolio Alternatives (IPA)
Insured Retirement Institute (IRI)
National Association of Insurance and Financial Advisors (NAIFA)
Nareit
Ohio Chamber of Commerce
Securities Industry & Financial Markets Association (SIFMA)
The Real Estate Roundtable
US Chamber of Commerce