Statement of Kenneth E. Bentsen, Jr.

On Behalf of the Securities Industry and Financial Markets Association

To the Massachusetts Securities Division

January 7, 2020

Good morning. I am Ken Bentsen, President and CEO of the Securities Industry and Financial Markets Association. SIFMA is a national trade association which brings together the shared interests of more than 350 large, medium and small broker-dealers, investment banks and asset managers comprising more than 75% of market share and 50% of assets under management (AUM). Our members serve millions of retail and institutional clients in every state, including Massachusetts. Virtually all of our members serving retail clients do so both as a broker-dealer under the Securities Exchange Act of 1934 ('34 Act) and as an investment advisor under the Investment Advisors Act of 1940 ('40 Act).

The U.S. securities industry proudly employs 45,000 Commonwealth residents and manages well more than $580 billion in assets in the state. In 2019, the industry underwrote more than $40 billion in municipal and corporate bonds and $13.25 billion in equity offerings - including 1.78 billion in initial public offerings - in the Commonwealth.

SIFMA appreciates the opportunity to present its views on the Division's newly proposed fiduciary conduct standard. Yesterday, we submitted a 20-page letter with detailed comments for your consideration. Today, I would like to focus on four specific concerns.

First: It is Premature for the Division to Declare that Reg BI Lacks Sufficient Protections for Retail Investors

SIFMA has long supported the creation of a federal heightened conduct standard for broker-dealers (BDs) and investment advisors (IAs). In our view, this was not a debate on whether to raise investor protection but how to modernize standards of conduct affecting retail clients in a way that wouldn't limit client access or choice.

Seven months ago, after more than a decade of careful study and analysis, the U.S. Securities and Exchange Commission adopted Regulation Best Interest. In the 14 months between the proposal and the final package, the SEC:

- Received 3000 unique comment letters from investors, consumer advocacy groups, investment professionals and others;
- Held seven investor roundtables;
- Surveyed over 1400 investors; and
- Hosted more than 200 meetings

We understand that the Division believes that Reg BI is lacking. We respectfully but strongly disagree. The SEC's final product creates a new, nationwide, heightened standard of conduct for BDs and their representatives as well as updating and enhancing requirements for IAs. Under Reg BI, a BD making a personalized recommendation to a retail customer in a brokerage account must act in the client's best interest without placing its financial or other interest ahead of the client's interest. BDs and their representatives must, among other things: (1) disclose all material facts about the scope and terms of the relationship and all material facts relating to conflicts of interest; (2) exercise diligence, care and skill, including understanding the risks, rewards and costs associated with a recommendation; (3) disclose, mitigate or eliminate conflicts of interest associated with the recommendation; and (4) establish robust policies and procedures to achieve compliance with Reg BI in its entirety.

The Division expressed concern that Reg BI does not create a single uniform standard for BDs and IAs. While the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") permitted the SEC to establish a uniform standard, it did not require the SEC to do so. After extensive review, the Commission chose not to develop a uniform rule. In Chairman Clayton's words, a "one size fits all" approach "would be a loss for our Main Street investors" and Reg BI "incorporates fiduciary principles, but is appropriately tailored to the broker-dealer relationship model and will preserve retail investor access and choice." While the SEC did not adopt a uniform standard, it effectively updated the '34 Act standard to be equivalent with the '40 Act standard, with regard to the duties and obligations owed to clients when providing investment advice.

Implementation and compliance are both a top industry priority and the law. While we have not yet fully quantified this effort, our members report that they are individually deploying significant amounts of resources to meet the June 30, 2020 compliance deadline. For example, one firm has told us that they have "several hundred" people working on Reg BI. Another has, since September, spent 3280 manhours **per week** on Reg BI compliance. A smaller firm has devoted roughly 5300 hours to date on the issue.

Given the breadth and depth of the rule and the efforts undertaken to comply, we respectfully believe that it is premature for the Division to declare Reg BI is inadequate. We encourage you to delay further state action until after Reg BI has been in place for at least 18 months and then assess whether further steps, if any, are necessary. Acting prematurely would lead to conflicting standards between the Commonwealth and the rest of the nation and would likely result in reduction of services to Commonwealth clients.

Second: The Proposal Will Likely Limit or Eliminate Retail Brokerage Services in the Commonwealth

Brokerage services represent an important, cost-conscious choice for retail consumers and provide access to affordable advice, particularly for buy-and-hold investors and investors with moderate resources. Broker-dealers and investment advisers offer different types of relationships, services and fee models. Virtually all of SIFMA's members who provide retail investment services offer both retail brokerage and investment advisory services, and often clients choose to retain both types of service. Brokerage is transaction-based whereas IA is ongoing and fee-based. Historically,

brokerage is less expensive since clients are not purchasing continual service. And in fact, the SEC has challenged IA's for imposing ongoing fees on otherwise "buy and hold" investments.

The Proposal's ongoing fiduciary duty obligation and its "avoid conflicts" and "without regard to" language blurs the line between BDs and IAs and will likely cause firms to limit or eliminate retail brokerage services in the Commonwealth. Quite simply, retail brokerage accounts – with their more limited client interaction and per transaction fee structure – do not make economic sense for firms if such accounts are going to be subject to the same duties and liabilities as fee-based advisory accounts. Consequently, clients will end up with substantially fewer brokerage products and services or will pay more for advisory services they do not want to purchase. That is exactly what the SEC sought to avoid.

The Division states that it does not believe that its Proposal will have a negative impact on investor choice. Our prior experience, however, demonstrates otherwise. As firms started working towards implementation of the now vacated U.S. Department of Labor Fiduciary Rule, we saw:

- Firms directing millions of clients to an internet or a call center option where they would receive execution only services; and

- Firms narrowing the platform of investment products available to retirement investors, which excluded common investment options such as index funds.

Indeed, a 2017 U.S. Chamber of Commerce report found that, if the DOL Fiduciary Rule had been fully implemented, 71% of advisers would have stopped providing advice to at least some of their small accounts, and 92% of firms were considering limiting or restricting investment products for their customers.

We believe, based on preliminary conversations with member firms, that the Division's Proposal as currently drafted will result in similar outcomes. This would be a major disservice to the many Massachusetts consumers who choose to hold BD accounts today and who want to continue to receive episodic brokerage advice under a transaction-based compensation model.

The Division minimizes the value of choice by declaring it "illusory" if it "means preserving the option to choose opaque, poorly-understood products that are sold via heavily conflicted advice." There are vastly more brokerage accounts than managed accounts in the U.S. today, and again, our members provide both services and customers choose the service they wish to purchase. Further, the industry is extremely competitive, and customers can and do vote by moving their assets. To suggest that all brokerage is "illusory" or bad is not supported by the facts or by customer demand.

Moreover, as our members interpret Reg BI – with its duty of loyalty, duty of care, disclosure obligations, compliance framework and requirements to mitigate or eliminate certain conflicts – we believe any potential for nefarious activity the Division is concerned about is addressed without negatively impacting retail investor access or choice.

Third: The Proposal Would Negatively Impact the State's Municipal and Corporate Markets

As drafted, the Division's Proposal could restrict the ability for firms to conduct principal transactions with retail BD clients, impacting the ability to efficiently satisfy retail investor demand for Commonwealth municipal and corporate offerings.

In a principal transaction, the BD, acting for its own account in order to facilitate client transactions, buys a security from, or sells a security to, the account of a client. In the municipal bond market, trades done on a principal basis are the most common form of trading. Principal transactions also cover underwriting activities where a BD is part of an underwriting syndicate for municipal or corporate bond offerings or for equity offerings (including IPOs).

Principal transactions would not appear on their face to satisfy the Proposal's requirement that BDs "avoid conflicts" and act "without regard to" their own financial interest. At a minimum, a BD engaged in principal transactions leaves itself open to the challenge that it is taking its own financial interest into account in violation of the Proposal. Yet these types of transactions are beneficial to a BD's clients and to the companies and municipalities who benefit from these bond issuances.

Many municipal issuers, including many in Massachusetts, require underwriters to give preference to local retail investors through a so-called retail order period. This provides a steady investor base to the issuer, and efficient pricing to the investor.

Without further clarification, many BDs acting as an underwriter may not be able to distribute such offerings to retail Commonwealth clients as an underwriter but rather will only satisfy client interest through an agency transaction. This will likely depress Commonwealth issuers' access to a broad retail investor base affecting the price of their securities while increasing the cost to such investors.

We urge the Division to exempt principal transactions from the Proposal's purview or at the very least to agree that compliance with the Investment Advisers Act and the SEC's rulemaking on principal trading would be a safe harbor for compliance with the rule.

Fourth: The Proposal Raises Substantial Legal Questions and Concerns

We believe this Proposal raises a variety of pre-emption and other legal issues.

For example, NSMIA preempts all regulatory requirements imposed by state law on SEC-registered advisers, except those relating to enforcement of anti-fraud prohibitions. We believe that the current Proposal attempts to recognize this but lacks an express declaration that SEC-registered advisers are excluded. We likewise ask for confirmation that the Proposal does not apply to investment adviser representatives ("IARs") of federal covered advisers, as mandated by NSMIA While the IAA permits states to set licensing, registration and qualification requirements and to bring enforcement actions with respect to fraud or deceit, this is substantially different from imposing substantive conduct requirements on employees or persons of federally covered advisors.

NSMIA also precludes states from imposing new books and records requirements on BDs and their representatives. The Proposal clearly imposes extensive new and different standards. BDs would need to develop new supervisory systems and procedures to address these new standards and make and keep substantial new records to document compliance. This is true despite the Proposal's provision stating that the rule shouldn't be construed as imposing any requirements that differ from or are in addition to NSMIA.

In addition, the Proposal seeks to impose investment advisory requirements on broker-dealers that are in conflict with both federal and state law. The ongoing fiduciary duty requirement is inconsistent with the "solely incidental" prong of the BD exclusion from the federal definition of investment adviser and with the language in Dodd-Frank that broker-dealers should not be required to have a continuing fiduciary duty. Moreover, the Proposal's ongoing duty requirement contravenes Massachusetts law which expressly excludes a registered BD or BD agent from the definition of investment adviser.

We appreciate the opportunity to comment and your consideration of our views. We believe Reg BI has meaningfully raised the bar for financial professionals and includes many important investor protections while preserving investor choice. We are very concerned that the Proposal exceeds the state's authority, will diminish investor access to advice, products and services and will increase investor costs. We respectfully suggest that you delay any decision making until after Reg BI is fully implemented and the SEC, FINRA, and the Division and other state regulators have the chance to examine firms for compliance.