January 7, 2020

The Honorable William Francis Galvin
Office of the Secretary of the Commonwealth
Attn: Proposed Regulations- Fiduciary Conduct Standard
Massachusetts Securities Division
One Ashburton Place, Room 1701
Boston, MA 02108
Submitted Electronically - securitiesregs-comments@sec.state.ma.us

Re: Comments on the Proposed Fiduciary Standard of Conduct for Massachusetts Broker-Dealers, Agents, Investment Advisers and Investment Adviser Representatives

Dear Secretary Galvin:

The Association for Advanced Life Underwriting ("AALU") appreciates the opportunity to comment on the revised amendments to 950 CMR 12.204, 12.205, and 12.207 (collectively, the "revised Proposal") establishing a uniform fiduciary standard for investment advisors and broker-dealers. We previously commented on the Massachusetts Securities Division's (the "Division") Preliminary Proposal to express our very significant concerns about the negative effect the Preliminary Proposal would have had on commission-based business models that are of vital importance to investors in the Commonwealth.[1]

While we offer our comments on the revised Proposal today as required by the December 13, 2019 Request for Comment, we urge the Division to extend the comment period for an additional 60 days. There are significant new issues raised by the revised Proposal, and the January 7, 2020 deadline provided only a little more than three weeks to review and comment on them. This small amount of time is insufficient to provide complete and meaningful comments. Given the importance of these issues to the citizens of the Commonwealth and the magnitude of the new changes to the Preliminary Proposal, we believe an extended review period is both appropriate and necessary.

We note that while the revised Proposal removed the unworkable "best" test for transaction-based compensation as we requested in our prior comment letter, the revised Proposal now contains new and troubling language raising a variety of new issues that cause us to believe the Proposal must be significantly modified to avoid harming the very investors it is intended to protect.

We believe that the Division has not fully considered the costs that would be imposed on investors in the Commonwealth as a result of a Massachusetts fiduciary standard that conflicts with federal regulations and other state standards. Promulgating a final rule that results in a patchwork of different and conflicting state and federal rules will lead to litigation, increased costs, and reduced access for Massachusetts consumers. Broker-dealers and other financial professionals will face significant costs to continue doing business in Massachusetts, if it makes sense for them to remain at all, and the

[1]See, AALU comment letter dated July 26, 2019, at https://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/preliminarycomments/2019-07-26-Association-for-Advanced-Life-Underwriting.pdf, last accessed on January 2, 2020.

citizens facing the most likely loss of choice and access to commission-based financial services are low-balance and beginning investors.[2]

Who We Are:

AALU is the leading organization of life insurance professionals—our more than 4,000 members are primarily producers engaged in providing life insurance planning and annuity solutions for individuals, families, and businesses nationwide. As life insurance professionals, we put our clients first every day, enabling individuals and families to maintain independence in the face of potential financial catastrophe and to build and guarantee retirement income. Many of our members are registered representatives of broker-dealers and we have significant concerns about the Proposal's attempt—despite the lack of any credible legal basis—to regulate insurance transactions. Our members are also very concerned that the likely effect of the Proposal will be restricting Massachusetts consumers' access to financial professionals utilizing the commission-based business model.

Overview:

As we explained in our prior comment letter, we believe that the Division's goals in promulgating the Proposal are achieved by the Securities and Exchange Commission's ("SEC") new Regulation Best Interest ("Reg BI") and Form CRS Relationship Summary ("Form CRS") and do not believe the Division should proceed to a final rule. At a minimum, the Division should wait until the SEC has implemented its final rules to assess their impact accurately and to inform the development of any final rule(s) contemplated by the Division.

We attributed the Division's original dismissal of the impact of Reg BI and Form CRS to the fact that the Division published the Preliminary Proposal only a few days after Reg BI and Form CRS were released and therefore had no real opportunity to review and address them. Unfortunately, in the new Request for Information accompanying the revised Proposal, the Division incorrectly characterizes key requirements of the new SEC rules. For example, the Division writes in the Request for Comment that it was compelled to proceed to protect Massachusetts investors in part because Reg BI permits conflicts to be addressed through disclosure alone.[3] In fact, the SEC agrees disclosure is not enough, and therefore Reg BI "…require[s] broker-dealers to…identify and mitigate any conflicts of interest… that create an incentive for a [representative] to place the interest of the broker-dealer, or [representative] ahead of the interest of the retail customer…we do not believe that disclosure alone sufficiently reduces the potential effect that these conflicts of interest may have on recommendations made to retail customers."[4]

We are very concerned that the Division is moving too quickly given its stated understanding of the new SEC rules. The Division writes that, "…the time to establish a true uniform fiduciary standard…is now, before industry habit and practices harden around Reg BI and form a barrier to further improvements."[5] In our view, failing to provide adequate time for public comment on significant revisions to the Preliminary Proposal is not consistent with the legal obligations and intent of the regulatory process, and will not produce results in the best interest of the Commonwealth.

In the event the Division does proceed, we offer the following specific comments on the Proposal, summarized here and described in more detail below. These address our serious concerns that the Proposal will make it very difficult for commission-based recommendations to remain a market choice available to investors in the Commonwealth. Reducing investor choice in this way will be harmful to the very investors the Proposal is intended to protect. Specifically:

- The Division must remove the overly broad and vague language in Sec. 12.207(2)(d) that could sweep common and appropriate compensation methods into a presumption of a breach of the duty of loyalty intended for sales contests. The broad and undefined terms including "express or implied quota" go well beyond any reasonable description of inappropriate sales contests of the kind the Division intends to prohibit, and could be read to

---

[2] *"With the adoption of the now vacated Department of Labor ('DOL') Fiduciary Rule, there was a significant reduction in retail investor access to brokerage services, and we believe that the available alternative services were higher priced in many circumstances." Securities and Exchange Commission Release No. 34-86031; File No. S7-07-18, "Regulation Best Interest: The Broker-Dealer Standard of Conduct" at pgs. 20-21, accessed on January 2, 2020 at https://www.sec.gov/rules/final/2019/34-86031.pdf.*

[3] *See, Request for Comment, December 13, 2019, at 2 and at 3 at https://www.sec.state.ma.us/sct/sctfiduciaryconductstandard/Request-for-Public-Comment.pdf last accessed on January 2, 2020.*

[4] *Securities and Exchange Commission Release No. 34-86031 at 325-326.*

[5] *Request for Comment, at 5.*

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, D.C.: 101 Constitution Avenue, N.W. | Suite 703 East | Washington, D.C. 20001 | 202.742.4638
www.aalu.org

include almost any commission-based arrangement compensating a financial professional. An "express or implied quota" can be read to include basic measures of profitability, routine contract terms establishing compensation grids, or qualification for employee benefits by statutory employees. Combining a presumption of a breach with undefined and vague terms creates a significant risk for financial professionals that will serve to increase costs and reduce the availability of commission-based services for Massachusetts consumers.

- The Division should remove the Proposal's unfounded assertion of authority over insurance. There is no credible legal basis for the Division's claim to regulate insurance transactions and conduct. The Division can't claim jurisdiction over financial products and services that are not securities. The Division's authority to deny or revoke securities registration for specifically listed types of misconduct--including committing any felony, committing postal fraud, having a securities license revoked in a Canadian territory, or dishonest insurance activity--does not grant it the authority to regulate the underlying felonious conduct, postal fraud, Canadian securities markets, or insurance transactions.

- The Division should remove the Proposal's barriers limiting access to commission-based financial services. There are four primary areas of concern in this regard:

    1. The Proposal contains internally contradictory duty of loyalty provisions in which one provision requires conflict mitigation efforts for commission-based business models, while another deems mitigation insufficient for compliance, making it impossible to know whether the standard has been met;
    2. Though the Division removed the "best" test, the Division must also rescind the troubling enforcement policy described in the Request for Comment in which very similar policies will be enforced against commission-based compensation despite the change;
    3. The imposition of ongoing investment monitoring requirements that are not appropriate or feasible for commission-based, episodic recommendations; and
    4. The use of certain titles for non-securities activities should not trigger ongoing monitoring obligations for unrelated securities activities.

- The Division should provide for an 18-month implementation period in any final rule to minimize costs and disruption facing consumers.

- The Division should recognize that federal law is likely to preempt many of the requirements of the Proposal, and the ensuing litigation, delays, and confusion will not serve the interests of Massachusetts investors.

Overly Broad and Undefined Terms Would Create a Presumed Breach of Loyalty for Common and Appropriate Business Models Unrelated to Prohibited Sales Contests:

The Division seeks to prohibit sales contests, quotas, or other incentives that "…provide no benefit to the customer or client, and are therefore repugnant to the principle of loyalty."[6] Unfortunately, the Proposal's overly broad and vague language would do much more than that, potentially sweeping into its presumed breach a wide array of legitimate and appropriate compensation methodologies. We urge the Division to remove the presumption of a breach and to instead clearly define prohibited compensation in a manner that is administrable and consistent with its stated goal.

The Proposal's new Sec. 12.207(2)(d) reads, " It shall be presumed to constitute a breach of the duty of loyalty…to recommend any investment strategy…type of account, or the purchase, sale, or exchange of any security, commodity, or insurance product, if the recommendation is made in connection with any sales contest, implied or express quota requirement, or other special incentive program. [emphasis added]"

The combination of a presumption of a breach and vague, undefined terms creates significant unintended consequences for financial professionals receiving common and appropriate compensation. Undefined terms such as "sales contest," "express or implied quota" and "special incentive" make it possible to argue—with a presumption against the financial professional—that many types of appropriate compensation are actually prohibited. This lack of clarity benefits no one.

---

[6] *"Id at 9.*

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, D.C.: 101 Constitution Avenue, N.W. | Suite 703 East | Washington, D.C. 20001 | 202.742.4638
www.aalu.org

The risk in the current language is that it is impossible to tell where the line is drawn. "Implied quota" can be read to include basic measures of profitability for representatives—if representatives are not engaging in sufficient activity they will be let go. Statutory employees (such as life insurance sales agents) qualify for health and retirement benefits based on their production levels—is this an express quota? Many representatives are compensated at progressively higher levels based on productivity throughout the year—is this a special incentive? Can a bonus be awarded to representatives who are more successful than others, or is this a special incentive?

The Division states that "The Proposal does not prohibit compensation, revenue, or profit…[it] requires simply that those conflicting interest cannot motivate or influence the advice or recommendations provided."[7] Unfortunately, the presumption of a breach for vaguely defined compensation standards may do exactly that—the duty of loyalty is presumed to be breached absent any showing that the compensation had any influence on the recommendation. This overbroad provision will make it very difficult for commission-based financial professionals to understand and comply with the law. What the Division appears to have intended it not what this provision does, and it must be significantly modified in order to best serve the needs of Massachusetts investors.

The Division Has No Legal Authority to Regulate Insurance:

Massachusetts state law specifically defines the term "security," listing what it includes and what it does not include. The statute does not include insurance products in its affirmative list of securities—in fact, it expressly excludes insurance products, reading "…'Security' does not include any insurance or endowment policy or annuity contract under which an insurance company promises to pay money either in a lump sum or periodically for life or some other specified period."[8]

Despite this clear definition excluding insurance policies and annuity contracts from its jurisdiction, the Division nonetheless attempts to regulate insurance as if it were a security. To support this effort, the Division argues that it has a "strong interest" where insurance is sold by persons who are also registered with respect to securities.[9] The Division then claims that the statute grants it the authority to regulate the insurance conduct of persons who also hold a securities license because doing so is "…consistent with Section 204(a)(2)(G) and is necessary to protect investors."[10]

Sec. 204(a)(2)(G) authorizes nothing of the kind. Sec. 204 as a whole governs the authority of the Secretary of the Commonwealth (therefore, the Division) regarding the "Denial, Revocation, Suspension, Cancellation, and Withdrawal of Registration" for securities purposes. Sec. 204(a) provides a long list of activities for which the Division may take action against the registration of a person or entity, many of which are unrelated to securities. Nothing in the statute grants authority to the Division or to the Secretary to regulate the underlying non-securities activity itself—it merely grants the authority to control whether the person or entity is registered to sell securities in Massachusetts.

The limit of this authority is clear when viewed in context of the list of items from which the Division plucked 204(a)(2)(G). That list also includes:

- Denial, suspension, or revocation of a securities license by any other state, any Canadian province or territory, or the SEC (Sec. 204(a)(2)(F)(i));
- Postal fraud (Sec. 204(a)(2)(F)(iii));
- Denial, suspension, or revocation of registration by the Commodities Futures Trading Commission ("CFTC") (Sec. 204(a)(2)(F)(v));
- Conviction of "any felony" (Sec. 204(a)(2)(C)); and
- Unethical or dishonest conduct in insurance or commodities (Sec. 204(a)(2)(G));

The Division no more has the authority to regulate insurance than it does to regulate securities in other US states or Canada, postal fraud, the CFTC, or general criminal law. The Division can't decide what constitutes postal fraud—pursuant to the statute but, it can deny, revoke, or suspend the registration of the recipient of a fraud order issued by the Unites States Postal Service within the last five years. Similarly, the Division cannot regulate the insurance activities of a producer simply because that producer may also be registered for securities purposes. Yet that is exactly what the Division attempts to do.

---

[7] *Id.*

[8] *M.G.L. c. 110A, § 401(k)*

[9] *Request for Comment at 5.*

[10] *Id at 6.*

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, D.C.: 101 Constitution Avenue, N.W. | Suite 703 East | Washington, D.C. 20001 | 202.742.4638
www.aalu.org

In the Proposal at Sec. 12.207(1)(a), the Division attempts to define the "unethical or dishonest conduct" referenced in the statute at Sec. 204(a)(2)(G) to include, "Failing to act in accordance with a fiduciary duty…when providing investment advice or recommending an investment strategy, the opening of or transferring of assets to any type of account, or the purchase, sale, or exchange of any…insurance product. [emphasis added]" This not "consistent with Section 204(a)(2)(G)" as the Division asserts—it is contrary to it. State law does not allow the Division to define and regulate the non-securities conduct of a security registrant as a condition of securities registration. It certainly doesn't allow the Division to impose an entirely different standard of care on an insurance transaction validly conducted under state insurance law and regulation simply because the producer is also registered for securities purposes. The Division's authority is limited to denying someone who violates insurance law the ability to engage in securities activity—it does not allow the Division to decide what insurance law should be.

The Division Should Remove the Proposal's Barriers Limiting Investors' Access to Commission-based Financial Services:

As we explained in our prior comment letter on the Preliminary Proposal, it is imperative that any final rule not limit investor access to commission or transaction-based business models. Depending on the needs of investors, such as the frequency with which they will make changes to their investments, or the type of investment product serving the consumers' needs, a fee-based model of compensation may cost significantly more while providing no additional advice or assistance. That is why we are very concerned about four specific types of barriers that remain in the revised Proposal. While the Proposal may not technically prohibit commission-based compensation, without modification these barriers would have the practical effect of effect reducing or eliminating this important option for investors. We urge the Division to address the following four issues:

1. Contradictory Duty of Loyalty Provisions Cannot Reasonably Be Met by Commission-Based Financial Professionals

   The new requirements under the duty of loyalty provisions are internally contradictory and cannot be met regardless of good faith compliance efforts by commission-based financial professionals.

   The new standard in the Proposal's Sec. 12.207(2)(b) is conceptually similar to the SEC's Reg BI in that it requires disclosure of material conflicts of interest, and requires mitigation or elimination of those conflicts. There are some differences in the specific language used—under the Proposal broker-dealers and others must "make all reasonably practicable efforts" to avoid or eliminate conflicts of interest, and to mitigate conflicts that cannot be avoided. The Division correctly "…acknowledges that some conflicts cannot reasonably be avoided or eliminated."[11]

   According to Sec. 12.207(2)(b), where a conflict cannot reasonably be avoided or eliminated, then it is the duty of the financial professional to take "all reasonably practicable steps" to mitigate the conflict. While this standard is somewhat vague, and therefore likely to give rise to many requests for guidance clarifying the Division's meaning, the next provision causes direct conflict. Sec. 12.207(2)(c) reads that "disclosing or mitigating conflicts alone does not meet or demonstrate the duty of loyalty. [emphasis added]" This directly contradicts Sec. 12.207(2)(b)—(2)(b) requires mitigation of an unavoidable conflict, but (2)(c) states that mitigation doesn't meet the requirement.

   As a result, commission-based compensation methods the Division says it intends to permit are cast in doubt. In the Request for Comment, the Division writes, "The duty of loyalty does not prohibit the payment or receipt of transaction-based compensation. However, this form of compensation creates a conflict that must be addressed and managed in accordance with the Proposal."[12]

   Because the Division takes the view that commissions represent an unavoidable conflict that therefore must be mitigated, even if the financial professional has made all reasonably practicable efforts to mitigate conflicts in accordance with the Proposal, the financial professional cannot be sure she has met the new duty

[11] *Id at 9.*

[12] *Id at 11.*

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, D.C.: 101 Constitution Avenue, N.W. | Suite 703 East | Washington, D.C. 20001 | 202.742.4638
www.aalu.org

of loyalty. We urge the Division to revise the duty of loyalty to provide a clear and reasonable path for compliance for commission-based financial professionals.

2. Enforcement Policy Remains Despite Removal of "Best" Test

   The Division removed the operative language in the Preliminary Proposal establishing a "best" test with regard to commissions and other transaction-based compensation. Under that test, an impractical standard which was not consistent with a fiduciary duty, a financial professional would have to show that the commission method was the "best" of the reasonably available alternatives. We, however, are troubled by the language in the Request for Comment discussing the Division's intention to enforce against commission-based compensation on similar grounds, despite the change to the regulatory text.

   Specifically, in the Request for Comment the Division writes, "…the Division intends to pursue enforcement action for breach of the duty of loyalty if transaction-based compensation is paid or received for a recommendation or advice, and other options were available which would have been less remunerative… The omission of these examples from the Proposal does not indicate that they will not apply. [emphasis added]"[13]

   In other words, despite the omission of the "best" test, the Division intends to enforce the duty of loyalty in the Proposal based on an analysis of whether commission-based compensation is more or less "remunerative" compared to other available options. This enforcement policy is not consistent with the intent of the Proposal, as explained in our previous letter. The client should come first, and the Division should rescind an enforcement policy that would view this recommendation as a violation of the duty of loyalty.

3. Ongoing Monitoring Requirements are Inconsistent with Episodic Recommendations

   The Proposal imposes an ongoing duty to monitor investments under a number of conditions. This ongoing duty is generally inconsistent with the typically episodic nature of recommendations made by commission-based financial professionals. In particular, we urge the Division to remove Sec. 207(1)(b)(4), which imposes an ongoing monitoring obligation if the financial professional receives "ongoing compensation." Many investment products provide trailing or other types of deferred compensation for what was clearly understood by the client and the financial professional to be an episodic recommendation, not an ongoing arrangement. The issue of whether there is an ongoing monitoring agreement or a reasonable expectation of ongoing recommendations has nothing to do with the timing of payments. We further note that Congress rejected an ongoing monitoring requirement for broker-dealers in the Dodd-Frank Act even as it asked the SEC to consider a uniform fiduciary standard.[14] We urge the Division to remove this language in any final rule.

4. Use of Certain Titles in Non-Securities Activities

   In the new Sec. 12.207(1)(c), the Proposal imposes an ongoing monitoring requirement if a financial professionals uses "…a title, purported credential, or professional designation containing any variant of the terms 'adviser,' 'manager,' 'consultant,' or 'planner,' in conjunction with any of the terms 'financial,' 'investment,' 'wealth,' 'portfolio,' or 'retirement,' or any terms of similar meaning or import…"

   As our members are insurance professionals engaged in providing life insurance planning and annuity solutions for individuals, families, and businesses, most of their activities fall outside the jurisdiction of the Division. However, our members also may be registered representatives of broker-dealers. Our members may therefore use an appropriate title in connection with life insurance planning activities that they do not use in connection with securities activities. Using a title in a non-security activity that may meet the definition in the list in 207(1)(c) should not result in any monitoring obligation in a securities transaction in which the title is not used.

   We ask that the Division clarify that Sec. 207(1)(c) only applies to titles used in connection with securities transactions.

---

[13] *Id at 10.*

[14] *See., 15 U.S.C 78o(k)(1) "…Nothing in this section shall require a broker or dealer or registered representative to have a continuing duty of care or loyalty to the customer after providing personalized investment advice about securities."*

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, D.C.: 101 Constitution Avenue, N.W. | Suite 703 East | Washington, D.C. 20001 | 202.742.4638
www.aalu.org

Federal Preemption is Likely Absent Material Modifications:

Despite the inclusion of the Proposal's new Secs. 12.207(4) (addressing fiduciaries under the Employee Retirement Income Security Act) and 12.207(5) (addressing the National Securities Markets Improvement Act of 1996 ("NSMIA")), the Division must recognize that the Proposal likely will be challenged as being preempted by Federal law. We believe these challenges are likely to prevail, given the interaction of the Proposal with rollover recommendations to ERISA plan participants, and given the implicit new burdens it places on broker-dealers. Compliance will require keeping records and taking other actions beyond those required by Federal law. This includes the financial obligation of purchasing insurance coverage as a fiduciary that goes beyond the standard errors and omissions coverage required of a broker-dealer that is not a fiduciary. As we explained in our prior comment letter, we also do not believe that this is a simple anti-fraud statute of the type that might not be preempted by NSMIA. Fraud is already illegal under Massachusetts law, and the Proposal addresses conduct that is not fraudulent.

Rather than promulgating a standard that conflicts with federal laws and regulations, increasing the cost and confusion facing investors and engendering years of litigation, the Division should coordinate any final rule with federal standards after Reg BI and Form CRS are fully implemented.

Reasonable Implementation Deadline:

The Proposal would result in sweeping changes across a wide array of financial service providers, and would require new agreements and contracts with Massachusetts investors. Given the magnitude of these changes, including the need to develop new policies, procedures, and training programs, and implement that training for personnel, we believe an 18-month implementation period is necessary. To rush compliance would unnecessarily increase costs and confusion for investors.

Conclusion:

Our members put their clients first every day, and we support regulation that protects investors while preserving their access to, and choice of, service models. Unfortunately, the Proposal does not achieve these goals, and will harm investors by reducing choice and increasing costs. We urge the Division to wait until the SEC has fully implemented Reg BI and Form CRS before revising the Proposal or issuing a final rule.

We appreciate the opportunity to comment, and appreciate your consideration of our concerns. We are always happy to answer any questions.

Sincerely,

Marc Cadin
President and CEO
AALU

Virginia: 11921 Freedom Drive | Suite 1100 | Reston, VA 20190 | 703.641.9400
Washington, D.C.: 101 Constitution Avenue, N.W. | Suite 703 East | Washington, D.C. 20001 | 202.742.4638
www.aalu.org