



VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS
AND INDEPENDENT FINANCIAL ADVISORS

VIA ELECTRONIC MAIL

May 15, 2013

William Francis Galvin
Office of the Secretary of the Commonwealth
Attn: Proposed Regulations
Massachusetts Securities Division
One Ashburton Place, Room 1701
Boston, MA 02108

RE: Request for Public Comment Regarding Additional Requirement for Investment Adviser Representative Registration Applications (950 CMR 12.205(2)(d)(1))

Dear Mr. Galvin:

On March 14, 2013, the Massachusetts Securities Division (Division) gave notice of its intent to amend 950 CMR 12.205, which governs investment adviser representative applications (Proposed Rule).¹ The purpose of the Proposed Rule is to: (1) add a requirement that those seeking investment adviser representative (IAR) registration in Massachusetts file as part of their application a Criminal Offender Record Information (iCORI) Acknowledgement Form;² (2) update filing requirements with respect to Form ADV; and, (3) update certain citations and references to forms to address changes that have occurred over time.

The Financial Services Institute³ (FSI) welcomes the opportunity to provide comments in connection with the Proposed Rule. While we applaud the Division's

¹ Public Notice of Proposed Rulemaking of Massachusetts Securities Division, *available at*: <http://www.sec.state.ma.us/sct/sctiar/Request%20For%20Comment%2003142013.pdf>

² The iCORI online system allows access to Criminal Offender Record Information (CORI), which is a database of criminal offender information covering crimes committed in the commonwealth of Massachusetts.

³ The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has over 100 Broker-Dealer member firms that have more than 138,000 affiliated registered

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efforts to update Form ADV filing requirements, we have concerns about the implementation of an additional filing requirement for investment adviser representative registration that does not utilize the Investment Adviser Registration Depository (IARD) system.⁴

Background on FSI Members

The independent broker-dealer (IBD) community has been an important and active part of the lives of American investors for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD firms also share a number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; engage primarily in the sale of packaged products, such as mutual funds and variable insurance products; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered investment adviser firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial advisers are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their financial goals and objectives.

In the U.S., approximately 201,000 independent financial advisers, or approximately 64 percent of all practicing registered representatives, operate in the IBD channel.⁵ These financial advisers are self-employed independent contractors, rather than employees of the IBD firms. These financial advisers provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisers are typically "main street America" it is, essentially part of the "charter" of the independent channel. The core market of advisers affiliated with IBDs is comprised of clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisers are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other

representatives serving more than 14 million American households. FSI also has more than 35,000 Financial Advisor members.

⁴ The IARD system is an electronic filing system that facilitates investment adviser registration, exempt reporting adviser filing, regulatory review and the public disclosure information of investment adviser firms. FINRA is the developer and operator of the IARD system. The system has been developed according to the requirements of its sponsors, the Securities & Exchange Commission and NASAA, along with those of an Industry Advisory Council representing the investment adviser firms. See also <http://www.iard.com>

⁵ Cerulli Associates at <http://www.cerulli.com/>.

centers of influence.⁶ Independent financial advisers get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, these financial advisers have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisers. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is committed to preserving the valuable role that IBDs and independent advisers play in helping Americans plan for and achieve their financial goals. FSI's primary goal is to insure our members operate in a regulatory environment that is fair and balanced. FSI's advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

Comments

FSI has the following comments on the Proposed Rule.

- 1. The Proposed Changes to Form ADV Requirements Will Promote More Effective Compliance By Investment Advisers** – FSI supports efforts by state regulators to promote more uniform requirements amongst the states, as they are likely to promote more effective compliance by regulated entities. The Division's proposal to amend the Form ADV requirements in 950 CMR 12.206(6) to align with the NASAA model brochure rule and the SEC's amendments to Part 2 of Form ADV will align the rules of Massachusetts with a national uniform standard. Moreover, the current changes to the Proposed Rule will promote uniformity going forward, as the text of the rule references the instructions to Form ADV, as opposed to referencing specific items that may have to be updated by the state over time. Therefore, FSI applauds the Division for making these changes to the investment adviser regulations in Massachusetts.
- 2. The iCORI System is Not the Appropriate Solution for U-4 Verification -**
The Proposed Rule seeks to impose a new requirement on investment adviser firms seeking to register their representatives in the state. Under the current system, investment adviser representative (IAR) registrations are handled completely through the Investment Adviser Registration Depository (IARD) system. The IARD system was adopted in early 2001, allowing registered investment advisers to file their Form ADV electronically through an online

⁶ These "centers of influence" may include lawyers, accountants, human resources managers, or other trusted advisers.

system.⁷ The system is a uniform system allowing both state and SEC registered advisers (RIAs) to utilize one method to make filings. An IAR registration component was added in March 2002, allowing RIAs to register their IARs online through FINRA's Web CRD system. One of IARD's goals is to provide investment advisers with an "efficient automated filing system."⁸ Unfortunately, the Proposed Rule undermines this goal of the IARD system.

The implementation of the Proposed Rule, in its effort to verify the U-4 filings of IARs through the iCORI system, disrupts the uniformity and efficiency inherent in the IARD/CRD system. The Proposed Rule imposes another compliance and administrative burden and cost on RIAs and IARs – requiring them to complete, sign, notarize and file an additional form manually – in addition to their U-4 filing through the FINRA CRD system. In addition to the compliance and administrative burdens on regulated firms, there is also the administrative cost and burden to the Division in devoting staff to manually processing these additional forms and insuring they are filed promptly. Furthermore, the iCORI system has the major shortcoming of being limited to only covering criminal records from Massachusetts, limiting its effectiveness in protecting investors.

While FSI and its members support the efforts of the Division to verify the criminal history of IARs on U-4 filings, we do not believe the method proposed by the Division is the best way to carry out this activity. FSI proposes exempting from the iCORI requirement IARs that are dually registered as registered representatives of a broker dealer (Dual-registrants). In addition, FSI encourages the Division to pursue the adoption of a fingerprinting statute in Massachusetts to allow more effective nationwide background checks to be performed.

The Division Should Provide an Exemption for Dual-Registrants From The iCORI Background Check Requirement

Dual-registrants are already required to undergo a mandatory fingerprinting and background check through the CRD/IARD system under SEC and FINRA rules.⁹ Under the Proposed Rule, Dual-registrants would be subject to duplicative requirements, having to submit to a background check by the FBI to verify their

⁷ *Electronic Filing For Investment Advisers on IARD: What is IARD?*, Securities & Exchange Commission, available at: <http://www.sec.gov/divisions/investment/iard/about.shtml>;

⁸ *Investment Adviser Registration Depository, What is IARD?*, available at: <http://www.iard.com/WhatIsIARD.asp>

⁹ See FINRA, *What to Expect from the U4 and U5 Filing Process*, FINRA "What to Expect" Webcast Series, pg. 4, available at: <http://www.finra.org/web/groups/industry/@ip/@edu/documents/education/p018907.pdf> ("SEC rules require FINRA to send [fingerprints submitted with U-4] to the FBI For a criminal history search"); see also SEC Rule 17f-2.

U-4, then another background check through the Massachusetts iCORI system. This duplication would provide little investor benefit given that the FBI system has much more extensive coverage than the iCORI system.¹⁰ As evidence of the large pool of Dual-registrants among investment adviser and broker dealer firms, FINRA has indicated that, "approximately 88 percent of all registered advisory representatives are also registered representatives of a broker-dealer."¹¹ Given the duplicative nature of this background check on Dual-registrants, in addition to the burdens and costs imposed on firms and the Division in performing it, FSI believes the Proposed Rule should be amended to exempt these individuals from having to provide a signed iCORI form with their IAR registrations.

The Division Should Seek Passage of a Fingerprinting Statute to allow Electronic Submittal of Fingerprints by Firms And More Effective Background Checks

In lieu of the use of the iCORI system for those who are not Dual-registrants, FSI proposes that the Division encourage the state legislature to adopt a fingerprinting statute to allow it to properly verify the fingerprints of prospective IA representatives through the CRD system or a Division-approved fingerprint vendor. FSI and its members are happy to assist the Division in this effort by actively committing resources to this endeavor. Passage of a fingerprint statute would allow the Division to obtain fingerprints of IAR applicants from the CRD/IARD system. If the Division does not wish to use the CRD/IARD system, they could also request fingerprints of IAR registrants through a livescan electronic fingerprinting vendor. Many other states have implemented this solution. The Division could then use these fingerprints to run a criminal background check against either the FBI or Massachusetts State Police database, rather than through the limited iCORI system. This approach would have the added benefit of allowing the Division to carry out a *more effective and*

¹⁰ FSI contacted the Massachusetts Department of Criminal Justice Information Service (DCJIS) and inquired as to whether FBI background checks would cover similar information as that in the iCORI system. DCJIS staff indicated that the FBI background check would likely be more extensive given it covers all fifty states, as opposed to just Massachusetts. They also indicated that the iCORI system does not include access to sealed records, whereas the FBI background check, with fingerprints being provided, would provide access to such records. This suggests an FBI background check is just as sufficient, if not more effective, in detecting erroneous and/or fraudulent information on the U-4 filings of Dual-registrants; See also Press Release, "Governor Patrick Signs Legislation to Close Loophole in Existing Background Checks Law and Increase Protections for Children Across the Commonwealth," January 11, 2013, available at:

<http://www.mass.gov/governor/pressoffice/pressreleases/2013/0111-background-checks-legislation.html>

¹¹ See FINRA Letter to SEC, *Commission Study on Enhancing Investment Adviser Examinations Mandated by Section 914 of the Dodd-Frank Wall Street reform and Consumer Protection Act of 2010*, November 2, 2010, pp. 3, available at:

<http://www.finra.org/web/groups/industry/@ip/@reg/@guide/documents/industry/p122404.pdf>

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comprehensive criminal background check, as these databases would include criminal background information nationwide. In contrast, the iCORI system only covers crimes that were carried out within Massachusetts. The Massachusetts Governor and Legislature have recognized the limitations of the iCORI system, recently signing a law (MA-H4307) requiring the Department of Early Education and Care (EEC) and Massachusetts school districts to conduct fingerprint-supported national criminal history background checks on all teachers, school employees and early education providers in Massachusetts.¹² FSI believes that the citizens of Massachusetts should receive the same level of protection when it comes to verifying the criminal background of the fiduciaries with which they entrust their personal and retirement savings.

In addition to the more effective background checks that may be performed by the Division without using the iCORI system, this approach would provide greater efficiencies in costs and manpower to the Division. Implementation of the Proposed Rule would result in the Division having to dedicate funding and staff resources to manually approve and verify the iCORI forms of IAR registrants. Implementation of a fingerprinting statute and a national background check would not only reduce this burden on the Division, but would also make investors in Massachusetts safer, by conducting a nationwide search of past criminal charges by potential IAR registrants.

FSI urges the Division to provide an exemption for Dual-registrants from the requirement to submit the iCORI form with their IA representative registrations, due to the duplicative nature of the background check being provided. FSI also encourages the Division to adopt a more effective background check regime, with a nationwide scope, through the passage of a fingerprinting statute in the Commonwealth. This approach will allow the Division to more effectively verify the criminal background of potential IAR registrants and provide better protection for Massachusetts investors, while at the same time reducing the compliance burdens on firms. We look forward to working with the Division going forward on this issue and are willing to provide assistance in achieving a legislative solution to better protect investors in Massachusetts.

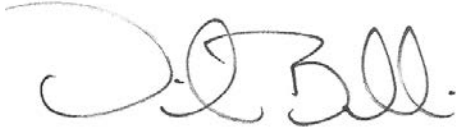
Conclusion

We remain committed to constructive engagement in the regulatory process and welcome the opportunity to work with state regulatory agencies to seek greater uniformity with their rules.

¹² Press Release, "Governor Patrick Signs Legislation to Close Loophole in Existing Background Checks Law and Increase Protections for Children Across the Commonwealth," January 11, 2013, available at: <http://www.mass.gov/governor/pressoffice/pressreleases/2013/0111-background-checks-legislation.html>

Thank you for your consideration of our comments. Should you have any questions, please contact me directly at (202) 803-6061.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "D. T. Bellaire". The signature is fluid and cursive, with a large initial "D" and "T" followed by "Bellaire".

David T. Bellaire, Esq.
Executive Vice President & General Counsel