April 22, 2020

Ms. Faye Morton
General Counsel
Oklahoma Department of Securities
204 North Robinson Avenue, Suite 400
Oklahoma City, OK 73102

Dear Ms. Morton:

The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness ("the Chamber"), together with the State Chamber of Oklahoma, welcome the opportunity to comment on the proposal released by the Oklahoma Department of Securities ("Department") regarding standards of ethical practice for investment advisers ("Proposal").[1] While we understand that the Department has recently decided against adopting the Proposal at this time, we believe this important topic nonetheless warrants comment.

The Chamber strongly supports investors having access to quality, affordable investment advice and believes that investment professionals should be held to appropriate standards when advising retail customers. Last year, the Securities and Exchange Commission ("SEC" or "Commission") adopted Regulation Best Interest ("Reg BI") which set a strong, national standard that prohibits broker-dealers from placing their own interests ahead of their clients.[2] The SEC also issued an updated Commission-level interpretation regarding standards of conduct for investment advisers ("SEC IA Interpretation").[3]

---

[1] Proposed release under Title 660, Chapter 11 of the Oklahoma Uniform Securities Act of 2004, *available at* https://www.securities.ok.gov/Act-Rules/Rulemaking/2020/Chapter-11/660%2011-7-42%20Standards%20of%20Ethical%20Practice%20Amended.pdf (hereinafter "Proposal").
[2] Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 FR 33318 (July 12, 2019) (hereinafter "Reg BI").
[3] Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 FR 33669 (July 12, 2019) (hereinafter "SEC IA Interpretation").

These actions were the culmination of a years-long effort by the SEC to carefully develop standards that reflect the diverse needs of American investors and different business models available from investment professionals. The Chamber strongly supported the adoption of Reg BI and the SEC's IA Interpretation as we believe they establish and reinforce strong standards at the federal level for both broker-dealers and investment advisers.

However, in recent years several states have sought to implement standards for broker-dealers and investment advisers that often conflict with SEC regulations. These efforts threaten to create a patchwork of conflicting state and federal rules that would serve only to increase costs and reduce access to recommendations for investors.[4]

The Chamber has largely opposed these state efforts because they undermine critical investor protections, reduce investor choice, and make it difficult for providers to serve their clients across state lines. Our overall concern is that the definition of "best interest" (in the case of broker-dealers) and "fiduciary" (in the case of investment advisers) would become jumbled depending on what state a provider or investor happen to live in. This is not a good outcome for retail investors who deserve to benefit from strong and consistent protections, regardless of where they reside.

We appreciate efforts taken by the Department to align certain parts of the Proposal with SEC standards. However, we believe that the Department should refrain from adopting conflicting requirements for investment advisers that are already registered at the federal level. We are also concerned about provisions in the Proposal that would severely limit the use of arbitration as a resolution forum for investors.

- **The Department should clarify that the Proposal would not create new or conflicting duties for a) SEC-registered investment advisers and b) state-registered investment advisers that are already in compliance with SEC regulations.** The Proposal includes some language regarding non-applicability to SEC-registered investment advisers; however, it remains unclear as to whether there is an intent to impose any compliance requirements on these advisers under the Oklahoma Uniform Securities Act. The Proposal should be

[4] *See, e.g.,* Massachusetts (Final fiduciary standard of conduct rule adopted February 21, 2020); Nevada (Draft regulations to implement SB 383 issued January 21, 2020); New Jersey (NJ Division of Consumer Affairs proposal regarding fiduciary standard for broker-dealers and investment advisers issued April 15, 2019); and Iowa (Iowa Insurance Division Best Interest Regulation dated February 27, 2020).

clarified to explicitly state that, in accordance with federal law, it does not apply to SEC-registered investment advisers and their investment adviser representatives. In addition, we believe the Proposal should clarify that an investment adviser's compliance with the SEC investment adviser regulatory regime as most recently described in the SEC's IA Interpretation would satisfy requirements at the state level.

- **The proposed duty of loyalty requirement should not create irreconcilable differences regarding the mitigation and disclosure of conflicts of interest.** The duty of loyalty requirements under the Proposal would require investment advisers to disclose all material conflicts of interest and "make all reasonably practicable efforts" to avoid conflicts, eliminate conflicts that cannot be avoided, and mitigate conflicts that cannot be avoided or eliminated.[5] However, it is not clear what constitutes "all reasonably practicable efforts" under the Proposal. More troublingly, the Proposal also states that disclosure or mitigation alone is not sufficient to meet the duty of loyalty,[6] meaning that even if an investment adviser made "all reasonably practicable efforts" to mitigate conflicts of interest, they still may not meet the duty of loyalty requirement under the Proposal. Additionally, the Proposal's language regarding prohibitions on sales contests, implied or express quota requirements, or other special incentive programs should be clarified so that incentives related to activities such as asset gathering are not covered.[7]

- **The Department should remove provisions in the Proposal that effectively eliminate the use of arbitration agreements to fairly resolve customer disputes.** Arbitration is a fair, effective, and less expensive means of resolving disputes compared to going to court. Multiple empirical studies demonstrate that claimants in arbitration do just as well or, in many circumstances, considerably better than in court. The Proposal would further strain already overcrowded courts and deprive investors of a speedier and more effective way to resolve disputes with an investment adviser.

---

[5] Proposal at 1.
[6] *Id.*
[7] *See id.* at 2.

Discussion

The Chamber's members rely on the investment advice, investment recommendations, and financial educational tools provided by a wide array of financial services providers. Our members and their employees have varying needs, and they enter into relationships with financial professionals based on their own unique circumstances. We have a strong interest in ensuring that our full spectrum of members have access to quality, affordable financial services that meet their needs. Critical to ensuring such access is the development and maintenance of well-crafted federal and state securities laws and regulations.

Unfortunately, we have in recent years faced significant regulatory challenges that have harmed our members and threatened their access to the services they require, most notably the U.S. Department of Labor's Fiduciary Rule ("DOL Rule"). The effect of the DOL Rule was severe even for the limited time it was in effect, especially for retirement savers with small account balances. A 2017 Chamber report estimated the damage had the DOL Rule been fully implemented: 11 million households would have seen limited or restricted investment products available to them; up to 7 million individual retirement account owners would have lost access to investment advice altogether; nearly three quarters of financial professionals would have stopped providing advice to some of their small accounts; and 35% of those professionals would have ceased serving accounts below $25,000.[8]

The SEC reached the same conclusion regarding the DOL Rule. In the preamble to Reg BI, the SEC wrote: "Our concerns about the ramifications for investor access, choice, and cost…are not theoretical. With the adoption of the now vacated [DOL 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 [citations omitted]."[9]

Regrettably, certain state-level proposals in recent years seek to emulate the DOL Rule and would effectively eliminate certain business and transaction models for which investors have demonstrated a preference. These initiatives also create potential sources of conflict with SEC regulations, which could limit access to investment products and services in some states and raise overall costs for investors. While the Proposal does not appear to be as disruptive as proposals put forward in other states,

---

[8] "The Data Is In: The Fiduciary Rule will Harm Small Retirement Savers," U.S. Chamber of Commerce, Spring 2017, *available at* https://www.uschamber.com/sites/default/files/ccmc_fiduciaryrule_harms_smallbusiness.pdf.
[9] Reg BI at 84 FR 33322.

we nevertheless urge the Department to consider a number of important factors prior to issuing a final rule.

Recommendations

The Department should clarify that the Proposal a) would not create new conduct rules for SEC-registered investment advisers, and b) would not create new or conflicting duties for state-registered investment advisers that are already in compliance with SEC regulations.

a) The Proposal includes a statement regarding its limited application to federal covered advisers. However, this statement alone is somewhat ambiguous, and the Proposal must explicitly acknowledge that the conduct rules do not apply to federal covered advisers and representatives of federal covered advisers as such provisions would be preempted by federal law. The National Securities Markets Improvements Act of 1996 ("NSMIA") added section 203A(b)(1) to the Investment Advisers Act of 1940, which unambiguously preempts states from imposing any regulatory requirements on federal registered investment advisers and their investment adviser representatives relating to their advisory activities or services. In the Rules Implementing Amendments to the Advisers Act, the SEC explained that Section 203A(b)(1), as amended by NSMIA, preempts not only a state's specific registration, licensing, or qualification requirements, but all regulatory requirements imposed by state law on SEC-registered IAs relating to their advisory activities or services, except those provisions relating to enforcement of anti-fraud prohibitions.[10]

b) The Proposal should clarify that an investment adviser's compliance with the SEC investment adviser regulatory regime as most recently described in the SEC's IA Interpretation would satisfy requirements at the state level.

The preemption issue is all the more critical given some of the notable differences between the Proposal and what has been adopted by the SEC. The Proposal uses language similar to that included in the DOL Rule regarding the

---

[10] Rules Implementing Amendments to the Investment Advisers Act of 1940, Release No. IA–1633, File No. S7–31–96, (May 22, 1997), *available at* https://www.govinfo.gov/content/pkg/FR-1997-05-22/pdf/97-13284.pdf ("On its face, section 203A(b)(2) preserves only a state's authority to investigate and bring enforcement actions under its antifraud laws with respect to Commission-registered advisers. The Coordination Act does not limit state enforcement of laws prohibiting fraud. Rather, states are denied the ability to reinstitute the system of overlapping and duplicative regulation of investment advisers that Congress sought to end." (text at nn.155-56)).

objectivity of recommendations provided to clients. The Proposal states that investment adviser recommendations and investment advice must be provided "*without regard to* the financial or any other interest of any party other than the client."[11] The SEC IA Interpretation states that "the duty of care includes a duty to provide investment advice that is in the best interest of the client, including a duty to provide advice that is suitable for the client."[12] If the preemption issues are not addressed and investment advisers have to comply with conflicting standards, the eventual effect of the "without regard to" language could largely depend on how it is enforced, creating an enormous amount of uncertainty for advisers.

The proposed duty of loyalty requirement should not create irreconcilable differences regarding the mitigation and disclosure of conflicts of interest.

The Proposal requires investment advisers to disclose all material conflicts of interest and to "make all reasonably practicable efforts" to avoid conflicts, eliminate conflicts that cannot be avoided, and mitigate conflicts that cannot be avoided or eliminated. While the Chamber agrees that robust regulation and disclosure regarding conflicts of interest are important components of investor protection, it is not entirely clear how the Department intends to apply this standard in practice. We encourage the Department to engage in further discussion with regulated entities to address appropriate strategies that would meet the "reasonably practicable efforts" threshold for potential conflicts.

Additionally, the Proposal states that "disclosing or mitigating conflicts alone" would not allow an investment adviser to meet the duty of loyalty. This means that even if an adviser had made "all reasonably practicable efforts" to mitigate conflicts that cannot be avoided or eliminated, they still may not meet the duty of loyalty. In other words, the current language in the Proposal could make it impossible in some instances for an adviser to comply with the duty of loyalty. The Proposal provides no further guidance on what an investment adviser should do if they have mitigated a conflict that can't be avoided or eliminated – the above-referenced language implies that what they have done is not enough. We urge the Department to amend these contradictory provisions and provide clear guidance for investment advisers as to how they are able to fulfill the duty of loyalty under the Proposal.

---

[11] Proposal at 1.
[12] SEC IA Interpretation at 84 FR at 33672.

We also believe that the language broadly prohibiting investment advisers engaging in any "sales contest, implied or express quota requirement, or other special incentive program" should be amended to clarify that activities such as asset gathering would not be covered. Compensation tied to asset gathering – the practice of bringing in new client assets or additional assets from existing clients – is not tied to the sale of any specific investment product and therefore does not meet the type of incentive that the SEC and other regulators have tried to eliminate.

The Department should remove provisions in the proposal that effectively eliminate the use of arbitration agreements to fairly resolve customer disputes.

The Proposal also states that it would be a breach of fiduciary duty for an investment adviser to enter into a contract or renew a contract with a client when such contract provides for arbitration as the means to resolve a client dispute that may arise during the course of a relationship.

Arbitration is a highly effective process that involves neutral third-party review of the facts and circumstances of a case in order to apply an appropriate resolution. Arbitration avoids the often lengthy and costly process of courtroom litigation which typically benefits plaintiffs' lawyers more than investors or consumers.

Many of the criticisms of arbitration are based upon the flawed premise that alternative mechanisms – such as litigating through the courts – provide better outcomes for consumers and investors and give them a meaningful and realistic option for resolving a dispute. In fact, the opposite is true. Litigation typically involves enormous costs, delays, and – in the case of class actions – the majority of cases result in little to no recovery at all for members of the class. In fact, according to the American Arbitration Association, from 2011-2015 delays in the court system cost consumers up to $13.6 billion.[13]

In addition, the Federal Arbitration Act ("FAA")[14] has protected the enforceability of arbitration clauses since 1925 and preempts contrary state law. The U.S. Supreme Court has recognized that state efforts to limit the enforceability of arbitration clauses are preempted by the FAA including state attempts to disfavor contracts that contain arbitration provisions.[15] If the arbitration-related language in

[13] "Measuring the Costs of Delays in Dispute Resolution," American Arbitration Association, *available at* http://go.adr.org/impactsofdelay.html.
[14] 9 U.S.C. 1, *et seq.*
[15] *See* Kindred Nursing Centers, Ltd. v. Clark, 137 S. Ct. 1421 (2017).

the Proposal was ultimately promulgated, it would likely be challenged and ultimately invalidated.

We strongly urge the Department to remove the Proposal's provisions related to arbitration so that investors can continue to use this critical process when resolving disputes.

Conclusion

The Chamber and our members share the Department's stated goal of protecting investors, but we strongly urge the Department to adopt the recommendations outlined in this letter to avoid creating confusion and costs for investors. Strong and efficient regulation would be undermined by a patchwork of conflicting state regulations that differ materially from one another and that conflict with federal regulations.

We are happy to discuss these comments further with you and the Department, and we are pleased to answer any questions.

Sincerely,

Tom Quaadman
Executive Vice President
Center for Capital Markets Competitiveness
U.S. Chamber of Commerce

Chad Warmington
President & CEO
State Chamber of Oklahoma