



Securities and Exchange Commission
Secretary
100 F Street NE
Washington, DC 20549

October 1, 2021

Response to Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches

(File No. S7-10-21)

The Financial Technology Association (FTA) appreciates the opportunity to respond to this request for comment (the “RFC”) on a broad range of topics involving digital engagement practices (“DEPs”), the application of emerging technologies, and growth of digital investment advisers. The breadth of topics raised underscores how technology has impacted, and, in many instances, enhanced the financial industry. Financial technology (“fintech”) is consistent with the SEC’s tripartite mission of protecting investors, maintaining fair, orderly and efficient markets, and facilitating capital formation.

In particular, fintech has had a substantial positive impact on financial markets and introduced new categories of financial services,¹ increased competition and efficiency, lowered investor costs, and expanded market participation.² The growth of fintech has helped to facilitate wealth creation for millions of Americans over the last decade, and future innovation holds substantial promise in helping to close the wealth gap in the United States.³ Allowing fintech to continue

¹ For example, digital investment advisers, also known as “robo-advisors,” pioneered the use of technology to provide investment advisory services over the Internet, services previously available only to affluent investors. Focused on long-term investment and wealth creation strategies, digital investment advisers use technology to help investors identify savings goals, such as retirement or education, and track their progress towards their financial goals.

² Other investor-centric fintech companies include those focused on micro-investing, those that allow customers to round up on purchases and invest the difference, those focused on expanding access to company equity ownership opportunities, and those pioneering investment opportunities in new asset classes and fractional shares.

³ Increased participation in equity investments has been shown to help build generational wealth and close the racial wealth gap. See McKinsey, *The economic impact of closing the racial wealth gap* (Aug. 13, 2019), available at <https://www.mckinsey.com/industries/public-and-social-sector/our-insights/the-economic-impact-of-closing-the-racial-wealth-gap>.



innovating furthers the SEC’s mission, supports economic growth, and long-term wealth creation.

To this end, FTA welcomes the Commission’s effort to begin gathering information on digital engagement practices and emerging technologies through this request. FTA respectfully cautions the Commission against regulating innovation, rather than conduct, and against penalizing digital firms relative to traditional firms. Technology-targeted regulation may fail to solve for identifiable investor harms and will limit or unnecessarily steer further innovation.

The Financial Technology Association (FTA)

The Financial Technology Association (FTA) is a nonprofit trade organization that educates consumers, regulators, policymakers, and industry stakeholders on the value of technology-centered financial services and advocates for the modernization of financial regulation to support inclusion and innovation.⁴ FTA is focused on informing tomorrow’s regulations, policy frameworks, and public understanding in order to safeguard consumers and advance the development of trusted, digital financial markets and services.

FTA is committed to advocating for the value of technology-centered financial services. As noted above, fintech innovators have made significant contributions to the financial industry by lowering costs of investment advisory services and trading services, increasing market participation of retail investors by reducing barriers to entry, introducing competition with legacy business models, and promoting capital formation.

FTA recognizes the Commission's concerns, however, that the SEC must remain vigilant in the face of behaviors that cause investor harm or undermine trust. FTA respectfully notes that this challenge is not new, and is present regardless of the communication and technology tools available to financial firms. As detailed below, the SEC has a broad range of regulatory tools that are fully capable of addressing measurable and clear investor harms, regardless of applicable technologies. FTA further notes that its members are committed to the responsible use of technology to safeguard investors, advance the development of trusted, digital financial markets

⁴ FIN. TECH. ASS’N, www.ftassociation.org (last visited Oct. 1, 2021). The FTA’s members include Afterpay, BlueVine, Betterment, Brex, Carta, Figure, Klarna, Marqeta, MX, Nium, Plaid, Quadpay, Ribbit Capital, Sezzle, Truwork, Wise, and Zest AI.



and services, and promote long-term retail investor wealth creation. The following are recommendations to ensure these critical market and public policy outcomes.

Comments on the Commission’s RFC

FTA welcomes the opportunity to begin engagement on the many questions raised in the RFC. For purposes of this request, FTA offers the following comments:

1. Regulation should be technology neutral

Regulation of conduct, rather than the mode of communication, should be the focus of the Commission’s regulatory inquiry. Any efforts to regulate the forms of technology employed by financial firms may unintentionally hamper new innovation, unfairly target digital innovations relative to traditional analog forms for investor engagement, and fail to solve for the underlying firm conduct that presents investor risk.

At the most basic level, digital engagement practices are merely communication tools. Many DEP activities used by broker-dealers and investment advisers represent technological improvements on long-standing customer engagement and education practices. Blunt regulatory approaches aimed at DEPs may constrain retail investors to a more limited and static set of investing tools relative to more affluent investors, decreasing their market participation and hampering investor education.

Digital design features can be used to shape investor behavior and outcomes in a variety of ways, and can be a powerful force for good. Investor-centric fintechs design DEPs to incentivize long term thinking and positive outcomes for clients. For example, “On-track / Off-track”, a DEP employed by digital investment advisers, shows an investor their progress towards a particular financial goal, helping them focus on long-term savings as opposed to short-term market movements. These progress reports are based on the investor’s goal time horizon, expected deposits, and asset allocation. DEPs designed with the clients’ best interest in focus, like “On-track / Off-Track,” do not drive investors to take action in response to stock prices and short-run market volatility.

Other investor-centric DEPs incorporate behavioral nudges to allow people to invest even if they may not feel they have enough funds, time, or appetite to take a more active role, by starting



small and counting on those savings to eventually add up. Behavioral nudges, like rounding up, or tax impact preview screens that cause an investor to pause and evaluate costs of a withdrawal during periods of market instability, use behavioral science to drive positive client outcomes.

FTA recognizes that, just as tools can be used for good, issues can also arise when firms' business models lead them to deploy DEPs in ways that may be contrary to investors' interests. Fortunately, as the Commission outlines in the RFC, there are a number of existing regulatory requirements that govern the behavior of broker-dealers and investment advisors that enable the Commission to enforce against improper conduct.

For example, anti-fraud provisions, which cover manipulative and deceptive trade practices, requirements to provide disclosures and material information to investors, Reg. BI, conflicts rules, and advertising restrictions already serve as effective enforcement authorities for pursuing egregious misconduct, both from traditional and digital broker-dealers and investment advisers.⁵ As the Commission states in the RFC, the use of a DEP by a broker-dealer may constitute a recommendation for purposes of Reg. BI, and FTA agrees that the Commission can apply existing conduct standards and disclosure obligations to the use of DEPs rather than create additional technology-targeted regulation. Blanket technology-targeted regulation would fail to solve for identifiable harms and would either box-in or unnecessarily steer further innovation.

Lastly, the RFC asks whether there are actions or regulations the Commission can pursue to foster educational engagement. The Commission can promote innovations in investor education materials by highlighting and encouraging their use. For example, digital investment advisers and other investor-centric financial firms use platform design and DEPs to provide educational engagement for retail investors in a variety of ways: tooltips explain complicated financial terms; pop-out modals provide additional context about a particular service; goal recommendation questionnaires help investors identify common savings goals; investment calculators help investors quantify goals and understand the assumptions that drive long-term returns; and push notifications alert investors when something requires attention. Educational engagement can also be presented via cross-links in the platform to blog posts, frequently asked questions and

⁵ Securities and Exchange Commission, *Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology to Develop and Provide Investment Advice*, issued Aug. 27, 2021, pp. 31-37, available at <https://www.sec.gov/news/press-release/2021-167>.



answers, and product disclosures that explain aspects of financial services in plain English and in more digestible, accessible formats as compared to regulatory disclosure documents.

2. Testing of DEPs should treat digital and traditional firms equally

As the Commission considers how firms oversee and manage DEPs, it is important to avoid imposing unequal or greater requirements on digital engagement that would discourage beneficial practices. For example, technology-forward financial firms often incorporate digital testing methods to gauge how products and messaging are received by customers. This testing, while more structured than the natural feedback loop a human adviser might incorporate into marketing decisions, is also quantitative and more likely produces results that show whether a product, service, or communication is demonstrably fit for its purpose. Quantitative testing through software is also less prone to certain subjective biases that may affect human decision-making. DEPs, as technology-based forms of customer engagement practices, are subject to relevant existing internal oversight, testing, and compliance frameworks focused on proper customer engagement.

The Commission should not penalize fintech firms with heightened testing requirements as compared to traditional firms simply because of the digital medium of their messaging, and should treat digital and legacy financial firms equally. Digital financial firms test products and marketing, including DEPs, to ensure they bring engaging, informative, user-friendly investing experiences to customers. This innovation and iteration through testing is critical to promoting greater market participation and investor education, and should not be discouraged or disadvantaged.

3. Digital advisers expand market access and promote responsible investing behavior

FTA believes the growth of digital investment advisory models has expanded market access for retail investors,⁶ and that the Commission should recognize the benefits of digital investment advisers as a way for investors to pursue long-term investing goals in a cost-effective and user-

⁶ According to reports, direct-to-consumer robo-advisor platforms in the U.S. reached \$257 billion at the end of 2018 and are projected by some to have assets under management of \$4.6 trillion by 2022. See Insider Intelligence, *Top robo advisors in 2021: Performance reviews, returns, and comparisons* (July 20, 2021), available at <https://www.insiderintelligence.com/insights/best-robo-advisors/>; U.S. Digital Investment Management Market Monitor, Q2 2019 (May 2019), available at <https://aite-novarica.com/report/us-digital-investment-management-market-monitor-q2-2019>.



friendly manner. Digital investment advisers are overall a relatively small size in the market, they reduce human error and biases, and their advantages over legacy models calls for regulation to be applied in a way that fosters their further development.⁷

The RFC seeks comment on the use of technology by digital investment advisers to develop and provide investment advice. In the RFC, the Commission recognizes advantages of robo-advisor models, such as lowering the costs of advisory services, offering user-friendly features, and reducing barriers to entry. The RFC acknowledges that digital advisers may provide clients more customized advice by using AI-based software that benefits from analysis of more (or more types of) information, and that AI-tools may substantially enhance information processing, reduce asymmetries, and contribute to market efficiency and stability.

However, the RFC also notes potential unique risks given digital advisers' reliance on algorithms and AI/ML engagement with customers, which may include portfolio recommendations and selections. The RFC states that a robo-advisor may rely on limited data or information provided by the customer, and may not include the ability to speak to a human, including during times of market stress.⁸ Further, the RFC states that technologies utilized by digital investment advisers may pose systemic risks, due to potential interconnectedness across the financial system and dependence on certain models.

As a threshold matter, it is important to contextualize digital models relative to the status quo and legacy business models. For example, digital firms, through the use of aggregation technology, are able to link external client accounts and draw complete financial data, which can be updated and analyzed in real-time, allowing for ongoing tracking of the client's financial position.⁹ Legacy models, which rely on manual processes, may be prone to certain information gaps. Legacy models rely on a client remembering his or her accounts, sharing that information, and manually updating that information. Legacy advisor models may also lack the internal capability to fully integrate customer financial data and use it to make more appropriate recommendations or investment allocations.

⁷ Philipp Maume, *Regulating Robo-Advisory*, 55 TEX. INT'L L. J. 49 (2019).

⁸ RFC, p. 51.

⁹ Data aggregators have identified robo-advisors as natural partners in enhancing investor experiences and outcomes. See, e.g., Plaid Whitepaper on Robo-Advisors, <https://plaid.com/tearsheet-whitepaper>.



The RFC also expresses concern about the potential lack or reduction of direct human interaction between the digital adviser and the client. As an initial matter, not all retail investors may want to interface with a human and the market for investment advisory services should support investor choice, whether it be for digital advice, traditional human advice, or a hybrid approach. The low-cost availability of digital options provides many retail investors with the ability to access investments in the first place, when they may otherwise not be able to afford any advice. Additionally, to the extent a client would like to speak with a human, many digital advisers offer this capability by providing the option to consult a financial advisor or other support personnel.¹⁰

Beyond reducing cost and increasing market participation, digital investment advisory models are built to reduce the risk of idiosyncratic or biased human behavior. The risk of an investor or advisor making emotional or bias-driven decisions, especially during periods of high volatility, are well-documented.¹¹ Digital investment advisory models reduce these risks and typically adhere to grounded, quantitative analyses in order to maximize returns and mitigate risks given particular client profiles and market conditions. And despite the RFC's concern that technologies utilized by digital investment advisers may pose systemic risks, digital investment advisers do not pose systemic risks given their nature, investment approach, and overall small size in the market.

Digital advisory models, like traditional firms, are subject to the same requirements under the Advisers' Act to act in clients' best interests, and thus have personnel, policies, and procedures in place governing their investment selections and monitoring of client portfolios, including any use of software. Indeed, most digital advisory models that rely on algorithms are simple, transparent, and based on quantitative research of empirical market data that, for a given investor profile, seeks to maximize returns, reduce risk, and lower fees. One comprehensive study of the digital advisory space found that most models are based on well-accepted Modern Portfolio Theory or other known methodologies.¹² Digital investment advisers are also independent from

¹⁰ For example, Betterment offers one-on-one professional guidance through scheduled 45- and 60- minute telephone calls with a Certified Financial Planner (<https://www.betterment.com/advice-packages/>).

¹¹ Cerulli Associates, *Mitigating the Impact of Advisors' Behavioral Biases* (2019), available at <https://investmentsandwealth.org/getmedia/dea8bde8-2399-4534-b97f-541dd7e46123/Cerulli-whitepaper-Mitigating-the-Impact-of-Advisors-Behavioral-Biases-002.pdf>.

¹² Beketov, Mikhail; Lehmann, Kevin; Wittke, Manuel 2018, *Robo Advisors: quantitative methods inside the robots*, Journal of Asset Management Palgrave Macmillan, vol. 19(6), pages 363-370 (October 2018), available at https://ideas.repec.org/a/pal/assmgt/v19y2018i6d10.1057_s41260-018-0092-9.html.



the products they recommend, and thus have fewer potential conflicts than other models. On the other hand, the investment selection and decision-making process of a human advisor is often opaque, may be prone to subjective biases of the advisor, and may not be reviewed by other neutral personnel.

Absent concrete identification of investor harm, FTA cautions against targeted regulation of digital investment advisers relative to legacy investment advisory models. The Commission should instead consider more principles-based approaches, as it did in the 2017 Division of Investment Management published guidance on Robo-Advisers. Digital advisory models promote responsible investing behavior and access to markets in a cost-effective and user-friendly manner. Digital investment advisers have helped to facilitate wealth creation for millions of Americans over the last decade, and are innovating to help individuals and families plan and save for their futures, through long-term goals like education and retirement.

Conclusion

FTA appreciates the opportunity to comment on the RFC and begin engagement on the topics of DEPs, emerging technologies, and digital investment advisory models. New technologies and approaches to customer engagement offer significant benefits in terms of customer education and long-term investment outcomes. FTA recognizes that as with any new tools, there is also the potential for actors to engage in activities that are not in the best interest of customers. To this end, the SEC has ample existing authorities to pursue such activity. As the Commission continues to explore this space, FTA stands ready to serve as a resource.

Sincerely,

A handwritten signature in black ink that reads "Penny Lee". The signature is written in a cursive, flowing style.

Penny Lee

CEO

Financial Technology Association