INSURED RETIREMENT INSTITUTE

October 10, 2023

Submitted via SEC's Internet Comment Form at: https://www.sec.gov/cgi-bin/ruling-comments

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE, Washington, DC 20549-1090

Re: Conflicts of Interest Associated with the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers
File Number S7-12-23

Dear Ms. Countryman:

On behalf of our members, the Insured Retirement Institute ("IRI")[1] appreciates the opportunity to provide these comments to the Securities and Exchange Commission ("SEC") regarding its proposal titled, *Conflicts of Interest Associated with the Use of Predictive Data Analytics by Broker-Dealers and Investment Advisers* (the "Proposal").[2] The Proposal would, among other things, impose new rules ("Proposed Conflicts Rules") under the Securities Exchange Act of 1934 ("Exchange Act")[3] and the Investment Advisers Act of 1940 ("Advisers Act")[4] that are purportedly intended to have firms broadly review any technology used in investor interactions and to eliminate, or neutralize the effect of, certain conflicts of interest associated with broker-dealers' or investment advisers' interactions with investors through these firms' use of certain technologies. The Proposal also includes proposed amendments to rules under the Exchange Act and the Advisers Act that would require registered investment advisers ("IAs") and broker-dealers ("BDs") (together, IAs and BDs are referred to in the Proposal and herein as "Firms") to make and maintain certain records in accordance with the Proposed Conflicts Rules.

For the reasons set forth below, IRI and its members strongly oppose the Proposal and respectfully urge that it be withdrawn.

Before turning to our substantive comments, we want to note that, on August 15, 2023, IRI and a group of other financial services industry trade associations submitted a joint written request for an extension

[1] The Insured Retirement Institute (IRI) is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, broker-dealers, banks, marketing organizations, law firms, and solution providers. IRI members account for 90 percent of annuity assets in the U.S., include the foremost distributors of protected lifetime income solutions, and are represented by financial professionals serving millions of Americans. IRI champions retirement security for all through leadership in advocacy, awareness, research, and the advancement of digital solutions within a collaborative industry community.

[2] 88 Fed. Reg. 53960 (Aug. 9, 2023).

[3] 15 U.S. Code § 78.

[4] 15 U.S. Code § 80b.

of the comment period on the Proposal.[5] To date, we have received no response to this request, and we are therefore submitting this letter by the deadline specified in the Proposal. However, based on the Proposal's substantial potential impacts on our members' ability to continue to pursue investor-focused innovations, combined with the far-reaching and fundamental regulatory shifts proposed, we simply did not have enough time to formulate and develop comprehensive comments on every aspect of the Proposal. Among other things, this letter does not directly address the alternative approaches described in the Proposal, though IRI and our members do have serious and significant concerns about those alternatives. Therefore, we reserve the right to submit supplemental comments after the end of the comment period to address those aspects of the Proposal that are not covered below.

Thematic Observations on the Proposal

The SEC has presented the Proposal as an effort to protect investors against potential conflicts of interest that could result from Firms' use of artificial intelligence ("AI"), predictive data analytics ("PDA"), and similar types of technology today or in the future. In actuality, however, the Proposed Conflicts Rules would impose significantly expanded obligations on Firms, far above and beyond the standards of conduct established under existing regulations. These new obligations would apply to nearly all types of technology that could be used in nearly any type of interaction between Firms and investors.

In the financial services industry, technology is deeply ingrained in the products and services offered and standard business practices, and new innovations designed to aid investors are always in the pipeline. Whether aimed at enhancing productivity, efficiency, knowledge, connectivity, or something else, new and evolving technology brings with it the promise of a better tomorrow, including making it easier for investors to pursue their financial goals. On the flip side, we acknowledge that innovation may also come with potential risks and conflicts.

Clearly, the regulatory framework has to evolve to keep up with technological advancements. We support the SEC undertaking the effort to determine whether and how the regulatory framework should evolve to keep up with technological advancements. Guardrails may be necessary to protect against any novel dangers that could be presented by new technology, but such guardrails must be carefully designed and appropriately tailored to observed risks. In our view, existing laws and rules already provide the guardrails necessary to protect investors with respect to the use of new technology. Fear of the risks and potential conflicts that can arise from the use of new technology should not stifle innovation and progress.

Unfortunately, in crafting such a broad Proposal, it seems the SEC has disregarded the importance of fostering innovation in a misguided attempt to build an impenetrable wall around American investors. The federal securities laws were not designed or intended to guarantee favorable outcomes for all investors. Rather, in crafting those laws, Congress sought to empower investors to make informed investment decisions that align with their individual financial objectives, needs, and risk tolerance. The Proposal would impermissibly reject this core principle.

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[5] Comment letter from a coalition of sixteen industry trade associations (Aug. 15, 2023), available at: https://www.sec.gov/comments/s7-12-23/s71223-245299-541662.pdf

Even more troubling, it appears that the SEC is using its concerns about evolving technology to justify a complete overhaul of the rules, across a variety of activities covered by existing regulations, that govern the conduct of Firms and their representatives without directly proposing to amend those rules.

Currently, IAs are subject to a fiduciary standard under the Advisers Act, and BDs are subject to a best interest standard under the SEC's Regulation Best Interest ("Reg BI").[6] To the extent that Firms and their representatives work with retirement plans and retirement plan participants and beneficiaries, they may also be subject to a fiduciary standard under the Employee Retirement Income Security Act of 1974 ("ERISA"). In addition, 40 state insurance regulators have adopted a similar best interest standard for recommendations of annuity products, and the remaining states are expected to follow suit in 2024. These regulatory regimes require financial institutions and financial professionals, when making recommendations, to act in the best interest of their clients without putting the interests of the Firm ahead of their clients' interests.[7] By all accounts, this robust and comprehensive regulatory framework is working. The SEC has offered no evidence that new rules are needed to effectively protect investors.

Nevertheless, the SEC has put forth the Proposal, which is built on a foundation of overbroad and far-reaching defined terms that extend its scope and reach far beyond new and emerging technologies. The Proposed Conflicts Rules would apply to even the most basic of computer hardware and software, mobile and web-based applications, and more in connection with nearly any type of interaction a Firm might have with an investor.[8] And unlike the existing regulatory framework for investment advice, the Proposed Conflicts Rules would not be limited to recommendations to investors. The Proposed Conflicts Rules would apply to interactions and communications that are intended to provide education or to increase investor awareness of basic investment concepts. Assessing the technologies used to assist with these informative activities could deprive investors of access to essential and valuable educational tools and resources.

Given this extraordinary breadth, the Proposed Conflicts Rules would drastically alter the costs of pursuing innovations on behalf of investors. Firms would have to assess whether conflicts of interest could arise and potentially harm investors as a result of any of the technologies they use, as most would likely fall within the definition of "covered technology," and then develop and implement steps to eliminate or neutralize such conflicts. For many Firms, this would apply to thousands of technologies and would take a massive amount of time and resources, not to mention the technical expertise necessary to conduct this required analysis.[9]

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[6] 17 CFR § 240.15l-1.

[7] *See* https://www.sec.gov/rules/final/2019/34-86031.pdf, Exchange Act Release No. 86031 (June 5, 2019) [84 FR 33318 (July 12, 2019)] ("Reg BI Adopting Release"); Commission Interpretation Regarding Standard of Conduct for Investment Advisers, Advisers Act Release No. 5248 (June 5, 2019) [84 FR 33669 (July 12, 2019)], at section II.C. ("Fiduciary Interpretation") (describing an adviser's fiduciary duties to its clients).

[8] Proposal, at 53972- 53977.

[9] Proposal, at 53980-53982 (discussing the testing and policies and procedures requirements, respectively, of the Proposed Conflicts Rules, which, if implemented in accordance with the proposal, would necessitate Firms' developing an understanding of the technologies they use).

Notably, the impact of the conflicts assessment requirement would not be limited to BDs and IAs. Firms commonly use technology provided by affiliated entities[10] and third-party entities,[11] and purchased from/licensed by other companies. Firms would need to communicate extensively with all these financial market players (likely their IT departments) to elicit the information needed to conduct the assessments and would rely on them considerably in determining how to eliminate or neutralize actionable conflicts associated with particular technology. Further, if the technology is deployed, there would likely be a need for ongoing information/reporting/certifications between the companies about its functioning given the post-implementation testing requirement, as well as the typical need for data/systems updates. The volume of technical detail flowing back and forth between the BDs and IAs vs. the technology providers, and the deep interdependencies that would result, would be significant.[12] These systemic burdens cannot be overstated. Moreover, they could result in less access to helpful investment tools and resources, as BDs and IAs could decide not to outsource technology due to the time and resource requirements.

In the comments below, we explain in greater detail that the Proposal must be withdrawn because it: (i) is not within the scope of the SEC's statutory authority; (ii) lacks an adequate economic analysis to demonstrate that the benefits to be achieved by the Proposed Conflicts Rules would outweigh the associated costs; (iii) fails to consider the unique and substantial adverse impact of the Proposed Conflicts Rules in the annuity and insurance space; (iv) is overreaching in applying to Firms' use of nearly all forms of technology; (v) unjustifiably disregards precedent by purporting to cover conduct other than recommendations; (vi) needlessly extends to a far broader universe of investors than existing standards of conduct; (vii) disregards the well-established meaning of "conflict of interest" in favor of a unique and far-reaching approach; (viii) rejects a core principle of the federal securities laws by disallowing disclosure as a method to address conflicts; and (ix) is unnecessary as the current regulatory framework already serves to effectively address conflicts of interest that could arise from Firms' use of technology with investors.

Substantive Comments on the Proposal

I. The SEC Lacks Statutory Authority to Adopt the Proposed Conflicts Rules.

As more fully outlined in a joint comment letter recently submitted to the SEC by IRI and a group of other financial services industry organizations, the SEC lacks the statutory authority to promulgate the

[10] For example, an insurer-affiliated BD or IA may use illustration tools provided by the affiliated insurance company.

[11] For example, registered representatives of retail-BDs may develop a recommendation with assistance from registered representatives of wholesaler-BDs who are affiliated with product issuers. In this regard, wholesaler-BD registered representatives typically offer education and support related to the products of their affiliated-company product issuers. In communicating with the registered representatives of retail-BDs, they may use their own technological tools to generate information that those registered representatives in turn rely on to support recommendations to their customers.

[12] The complexity would be compounded, for example, if the technology at issue includes one or more component features licensed from yet another firm. In this scenario, the BD and IA would have to deal with multiple intermediary companies to accomplish the conflicts analysis for a single tool, as well as the ongoing requirements in the event the technology is deployed.

sweeping changes contemplated by the Proposed Conflicts Rules under either the Advisers Act or the Exchange Act.[13] In particular, we emphasize a few key points below.

The expansive nature of the Proposal is inconsistent with the narrowly tailored authority granted by Congress to the SEC under Sections 211(h) of the Advisers Act and 15(l) of the Exchange Act. These provisions were promulgated under Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act[14] in connection with the delegation of authority to the SEC to adopt harmonized standards of conduct for BDs and IAs when providing investment advice to retail investors. Congress could have clearly granted broad authority for the SEC to regulate the business of Firms, but Section 913 did not go anywhere near that far.

Moreover, the Proposal includes an unworkably vague definition of conflict of interest that has no basis in the federal securities laws and is incompatible with existing definitions of the term under other existing SEC regulations.

In sum, the SEC simply cannot regulate the entirety of the business of Firms as contemplated by the Proposal without a clear delegation of such authority by Congress.

II. The SEC's Cost-Benefit Analysis Is Insufficient to Support the Proposal.

Section 23(a)(2) of the Exchange Act requires the SEC to consider the impact that any rule promulgated under that Act would have on competition and to include in the rule's statement of basis and purpose "the reasons for the [SEC's] . . . determination that any burden on competition imposed by such rule or regulation is necessary or appropriate in furtherance of the purposes of [the Exchange Act]."[15] The D.C. Circuit has viewed these provisions, together with the requirement under the Administrative Procedure Act that SEC rulemaking be conducted "in accordance with law," as imposing on the SEC a "statutory obligation to determine as best it can the economic implications of the rule."[16] Similarly, the court has found certain SEC rules arbitrary and capricious based on its conclusion that the SEC failed adequately to evaluate a rule's economic impact.[17]

IRI and a group of other financial services industry organizations recently submitted a joint comment letter that highlights the inadequacy of the SEC's cost-benefit analysis of the Proposed Conflicts Rules.[18]

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[13] Comment letter from a coalition of sixteen industry trade associations (Sept. 12, 2023), available at: https://www.sec.gov/comments/s7-12-23/s71223-258279-605062.pdf ("There is no data in the economic analysis to support the "preliminary" beliefs expressed in it. Similarly, there is no justification for what the proposal's authors say "could" result. Supporting information is needed on the shortcomings (if any) in current law, on whether investors currently lack confidence in firms using the covered technology or are actually being harmed – or likely to be harmed - by the use of any covered technology, and on the potential impacts of the proposal on investor decisions.").

[14] *Dodd-Frank Wall Street Reform and Consumer Protection Act*, Pub. L. No. 111-203, § 913, 124 Stat. 1376, 1824 (2010) (codified at 15 U.S. Code § 78o and 15. U.S. Code § 80b-11)

[15] 15 U.S. Code § 78w.

[16] *Chamber* I, 412 F.3d at 143.

[17] *See, e.g., Business Roundtable*, 647 F.3d at 1148 (finding that the Commission had failed "adequately to assess the economic effects of a new rule").

[18] Comment letter from a coalition of six industry trade associations (Sept. 19, 2023), available at: https://www.sec.gov/comments/s7-12-23/s71223-261319-615782.pdf

As more fully discussed in such letter, this defect in the Proposal makes it vulnerable to vacatur as arbitrary and capricious by the courts.[19]

A more robust and comprehensive economic analysis would have clearly demonstrated that the Proposal will have a harmful effect on low and middle-income investors by making it far more expensive and far more difficult, if not impossible, to access the essential tools, educational information, and resources they need to achieve their financial goals. We understand that other industry groups have conducted their own economic analyses of the Proposal and will be sharing their findings with the SEC in their respective comment letters. We urge the SEC to review and consider the results of these economic analyses carefully and objectively before determining whether and how to proceed with respect to the Proposal.

III. The Proposal Fails to Consider the Unique and Substantial Impacts of the Proposed Conflicts Rules in the Context of Variable Annuities and Other Insurance Products.

Insurance companies that issue annuities and other insurance products may provide technology tools to affiliated Firms, and unaffiliated third-party Firms that sell their products. To the extent that a Firm uses insurer-provided technology in "investor interactions," the Firm may require assistance from the insurer to meet its obligations to conduct the conflicts assessments and other compliance requirements under the Proposed Conflicts Rules. For example, a Firm may request information, reports, or ongoing certifications that the technology is functioning as represented (if the technology is deployed).

Registered representatives of wholesaler BDs[20] may also use technology sponsored by affiliated insurance companies to assist retail BD registered representatives in understanding and identifying products to recommend to customers. Due to the overbroad definitions of "covered technology" and

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[19] *See Chamber of Commerce v. SEC*, 412 F.3d 133, 143-144 (D.C.Cir.2005) ("The [Securities and Exchange] Commission also has a 'statutory obligation to determine as best it can the economic implications of the rule.' . . . Indeed, the Commission has a unique obligation to consider the effect of a new rule upon 'efficiency, competition, and capital formation,' . . . and its failure to 'apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation' makes promulgation of the rule arbitrary and capricious and not in accordance with law." *See also* Memorandum to Staff of the SEC Rulewriting Divisions from the SEC Division of Risk, Strategy, and Financial Innovation, and the SEC Office of the General Counsel re: Current Guidance on Economic Analysis in SEC Rulemakings (Mar. 16, 2012), available at: https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf ("Recent court decisions, reports of the U.S. Government Accountability Office and the SEC's Office of Inspector General, and Congressional inquiries have…recommended improvements to various components of the Commission's economic analysis in its rulemaking, including: (1) identifying the need for the rulemaking and explaining how the proposed rule will meet that need; (2) articulating the appropriate economic baseline against which to measure the proposed rule's likely economic impact (in terms of potential benefits and costs, including effects on efficiency, competition, and capital formation in the market(s) the rule would affect); (3) identifying and evaluating reasonable alternatives to the proposed regulatory approach; and (4) assessing the potential economic impact of the proposed rule and reasonable alternatives by seeking and considering the best available evidence of the likely quantitative and qualitative costs and benefits of each.").

[20] In the annuity and insurance space, a wholesaler BD is a Firm that acts as an intermediary between the product issuer and the retail Firm. Wholesaler BDs generally do not have direct contact with investors. Rather, they provide behind-the-scenes support for retail Firms to help them better understand the products and how they could align with the needs of certain investors. Some wholesaler BDs are owned by or affiliated with particular insurance companies, while others are independent.

"investor interaction," such technology could be in scope under the Proposed Conflicts Rules, in which case, the wholesaler BD and the retail BD would need to coordinate to ensure compliance requirements are met, with the retail BD bearing the responsibility for compliance. The amount of technical detail flowing back and forth between these market players, and the deep interdependency that would result, would be significant.

The costs and burdens associated with the potential application of the Proposed Conflicts Rules in these circumstances would be substantial and, in our view, would far outweigh the minimal and theoretical benefits to investors. The Proposal fails to acknowledge or address these circumstances.

In addition, many insurance companies offer proprietary products that are only available through certain retail BDs. Proprietary products can also offer unique benefits for investors. For example, registered representatives of Firms that offer proprietary products may have more experience working with those products and may have received additional training or support with respect to those products. As a result, such registered representatives could be especially well-suited to assessing whether a proprietary product would be a good fit for a particular client.

Unfortunately, the expansive definition of "conflict of interest" under the Proposal appears to prohibit Firms from using covered technology that could lead to or support a recommendation of a proprietary product, as the sale of a proprietary product can arguably be viewed as being more beneficial to the Firm than a sale of a non-proprietary product. Given that the SEC has not acknowledged or addressed the impact of the Proposal on this business model, it is unclear whether or how a Firm could eliminate or neutralize the effects of the potential conflict of interest presented by proprietary products. Likewise, the SEC has offered no evidence that disclosure and informed consent would be insufficient to effectively protect investors with respect to the potential conflicts associated with proprietary products. Nevertheless, the Proposal would effectively place an unnecessary barrier on investors' ability to access proprietary products by making it nearly impossible for Firms to use covered technology in connection with investor interactions involving such products.

IV. The Sprawling Definition of "Covered Technology" Reaches Far Beyond AI and PDA, Bringing Virtually All Forms of Technology Under the Proposed Conflicts Rule.

In the Introduction to the Proposal, the SEC asserts that "the current regulatory framework should be updated to help ensure that Firms are appropriately addressing conflicts of interests associated with the use of PDA-like technologies." Improving technology governance is a worthy regulatory objective. AI, PDA, and similar emerging technologies present potential opportunities and benefits, as well as potential costs and risks. IRI believes policymakers at all levels of government should continue to educate themselves about these new forms of technology and how they could be used and abused before undertaking to develop appropriate measures to effectively protect consumers without unduly impeding innovation. The SEC and its fellow regulators should not, however, rush to put overly prescriptive, one-size-fits-all rules in place out of fear that new technology might possibly be used in a manner that could potentially harm investors. Unfortunately, in issuing the Proposal, this is precisely what the SEC has done.

The Proposed Conflicts Rules are comprised of two primary components. First, Firms would be required to identify and assess whether the use or reasonably foreseeable potential use by the Firm or its

associated persons of "covered technology" in connection with "investor interactions" could present a "conflict of interest," either currently or in the foreseeable future. Second, if a Firm determines that any covered technology would present any such potential conflicts, the Firm would be required to "eliminate or neutralize the effect" of such conflicts. The concept of "covered technology" lies at the core of the Proposed Conflicts Rules, and its vastness is among the most significant and fundamental defects in the Proposal.

Under the Proposed Conflicts Rules, "covered technology" would mean "an analytical, technological, or computational function, algorithm, model, correlation matrix, or similar method or process that optimizes for, predicts, guides, forecasts, or directs investment-related behaviors or outcomes." In effect, this sweeping definition would encompass nearly all forms of technology, ranging from the most complex AI and PDA to simple, everyday business software such as Microsoft Excel spreadsheets, calculators, and online educational materials.

The Proposal explains that this new term is intended to broadly cover "design elements, features, or communications that nudge, prompt, cue, solicit, or influence." [21] However, the SEC offers little more than mere speculation to justify the breadth of this concept, asserting that "[t]his broad proposed definition is designed to help ensure that, as innovation and technology evolve and firms expand their reliance on technologies to provide services to, and to interact with, investors, our rules remain effective in protecting investors from the harmful impacts of conflicts of interest."[22]

We acknowledge the SEC's desire to establish an evergreen regulatory framework capable of evolving in real time alongside the development of innovative technologies. In this context, however, evergreen rules already exist in the form of Reg BI, the Advisers Act fiduciary standard, and the corresponding standards of conduct adopted by the Department of Labor and state insurance regulators. Those rules apply regardless of whether existing or new technology is utilized in connection with a particular recommendation. The mere fact that innovative technology may be involved in the development or presentation of a recommendation does not create a need for new rules.

In sum, the broad definition of covered technology in the Proposal serves not to effectively establish guardrails for the future as intended but to paralyze and cast a shadow on the present. Despite its acknowledgement that the Proposed Conflicts Rules would apply to existing and relatively well-understood technology, the SEC makes no effort in the Proposal to explain why it is necessary to require Firms to expend the time and resources to assess whether simple, everyday technology such as Excel spreadsheets could be used, either intentionally or inadvertently, to nudge an investor into a transaction based on the interests of the Firm to the detriment of the investor.

V. The Inclusion of Non-Recommendations in the Expansive Definition of "Investor Interaction" Represents an Unnecessary and Inappropriate Paradigm Shift.

The Proposal represents a significant, problematic, unnecessary, and inappropriate expansion upon and deviation from the scope of BD activities subject to the best interest standard of conduct established

[21] Proposal, at 53972

[22] Id.

under Reg BI. Consistent with decades of precedent,[23] the best interest standard, including the conflict of interest obligation incorporated therein, is triggered when a "recommendation" has been made to a retail customer.[24] By contrast, the Proposed Conflicts Rules would be triggered by the use of covered technology in any "investor interaction," a vague, ill-defined, and overbroad new term invented by the SEC for purposes of the Proposal.

Adding to the confusion, the Proposal describes "investor interactions" as any use of covered technology by a Firm that could "nudge, prompt, cue, solicit, or influence investment-related behaviors or outcomes from investors."[25] These terms are unfamiliar, vague, imprecise, and generally unhelpful, and actually undercut the traditionally understood meaning of recommendation, which is anchored on a "call to action," an objective standard that requires both intent on the part of the Firm or agent that that the customer take specific action and a reasonable belief on the part of the customer that the agent intends them to act. Moreover, determining whether covered technology has been used in a way that nudges, prompts, cues, solicits, or influences an investor's behavior would require an assessment of the investor's subjective interpretation of the circumstances, which would be extremely difficult for agents to apply. "Recommendation" and "call to action" are objective and well-understood concepts; rejecting these in favor of subjective and vague terms like nudge, prompt, cue, solicit, and influence would be inconsistent with historical precedent, create significant challenges for the establishment and implementation of effective compliance policies and procedures; and likely produce different results for different investors based solely on their individual state of mind.

In the text of the Proposed Conflicts Rule, "investor interaction" is defined to mean "engaging or communicating with an investor, including by exercising discretion with respect to an investor's account; providing information to an investor; or soliciting an investor…"[26] The Proposal acknowledges that such definition goes well beyond investment advice and recommendations, noting that the Proposed Conflicts Rule would apply to any use of covered technology in connection with any of the following activities, all or most of which are already subject to regulatory oversight under FINRA Rule 2210 (Communications with the Public) for BDs and under the Advisers Act for IAs:

- Correspondence, dissemination, or conveyance of information to or solicitation of investors in any form;
- Communications that take place in-person, on websites; via smartphones, computer applications, chatbots, email messages, and text messages; and other online or digital tools or platforms;
- Engagement between a firm and an investor's account on a discretionary or non-discretionary basis;

[23] For more than 80 years prior to the adoption of Reg BI, BDs were subject to a suitability standard. As with Reg BI, the suitability standard applied only when making recommendations to retail investors.

[24] SEC Adopting Release: Regulation Best Interest: The Broker-Dealer Standard of Conduct, 17 CFR Part 240 Release No. 34-86031; File No. S7-07-18 ("Reg BI Adopting Release").

[25] Proposal, at 53972.

[26] Proposal, at 54021.

- Advertisements, disseminated by or on behalf of a firm, that offer or promote services or that seek to obtain or retain one or more investors;
- Firms' use of research pages or "electronic libraries" to provide investors with the ability to obtain or request research reports, news, quotes, and charts from a firm-created website;
- Emails to investors as part of a firm-run email communication subscription that investors can sign up for and customize, and which alerts investors to items such as news affecting the securities in the investor's portfolio or on the investor's "watch list;"
- Circulating a link to a digital platform that includes features designed to prompt investors to trade along with the annual delivery of Form ADV;
- Providing individual brokers or advisers with customized insights into an investor's needs and interests;
- Game-like prompts or marketing that "nudge" investors to take particular investment-related actions on digital platforms; and
- Solicitations, including when a firm uses covered technology that scrapes public data, which the firm, in turn, uses to solicit clients through broadcast emails.[27]

The breadth and depth of this non-exclusive list is astonishing and unprecedented. Never before has the SEC or any other regulatory body sought to impose such onerous requirements on such a wide array of activities. In fact, in the Reg BI adopting release, the SEC expressly stated that Reg BI applies only to recommendations[28] and intentionally opted not to formally define the term "recommendation," instead choosing to rely on the existing framework under which the determination of whether a recommendation has been made is based on the particular facts and circumstances. To that end, the SEC noted that:

> Factors considered in determining whether a recommendation has taken place include whether the communication "reasonably could be viewed as a `call to action'" and "reasonably would influence an investor to trade a particular security or group of securities." The more individually tailored the communication to a specific customer or a targeted group of customers about a security or group of securities, the greater the likelihood that the communication may be viewed as a "recommendation." We continue to believe this general framework regarding what is a recommendation is appropriate…[29]

Based on this framework, the SEC has clearly stated that:

> The treatment of certain communications as "education" rather than "recommendations" is well understood by broker-dealers. We generally view the following types of communications as not being recommendations:
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> - "General financial and investment information, including:

[27] Proposal, at 53974-53975.

[28] Reg BI Adopting Release, at 33338-33340 (

[29] Reg BI Adopting Release, at 33335.

  - basic investment concepts, such as risk and return, diversification, dollar cost averaging, compounded return, and tax deferred investment,
  - historic differences in the return of asset classes (e.g., equities, bonds, or cash) based on standard market indices,
  - effects of inflation,
  - estimates of future retirement income needs, and
  - assessment of a customer's investment profile;
- Descriptive information about an employer-sponsored retirement or benefit plan, participation in the plan, the benefits of plan participation, and the investment options available under the plan;
- Asset allocation models that are:
  - based on generally accepted investment theory,
  - accompanied by disclosures of all material facts and assumptions that may affect a reasonable investor's assessment of the asset allocation model or any report generated by such model, and
  - in compliance with FINRA Rule 2214 (Requirements for the Use of Investment Analysis Tools) if the asset allocation model is an "investment analysis tool" covered by FINRA Rule 2214; and
- Interactive investment materials that incorporate the above."[30]

All or most of these educational activities are already subject to regulatory oversight under FINRA Rule 2210 (Communications with the Public) for BDs and under the Advisers Act for IAs. In light of this existing regulatory framework, the SEC intentionally excluded these already-regulated educational activities from the scope of Reg BI, noting that Reg BI "should not stifle investment education as a means to encourage financial wellness, or otherwise restrict broker-dealers from disseminating information about, for example, retirement plans, and the approach we are taking to what is or is not considered a "recommendation" achieves this goal."

The overlap between the types of activities that are out of scope under Reg BI but in scope under the Proposed Conflicts Rules is stark. There is simply no way to reconcile the notion that a BD's use of interactive investment materials that incorporate assessments of customer investment profiles is not subject to the best interest standard under Reg BI, but using covered technology to provide an individual brokers or advisers with customized insights into an investor's needs and interests is subject to the Proposed Conflicts Rules. These positions are incompatible and would produce inconsistent outcomes.

Consider, for example, two scenarios in which a registered representative of a broker-dealer meets with a client to discuss potential investment opportunities.

[30] Reg BI Adopting Release, at 33337-33338.

In the first scenario, the registered representative prepares for the meeting by reviewing a hard copy of the client's investment profile and determines, based on that review, that she should explore variable annuity options with the client. She opens her desk drawer, finds hard copies of prospectuses for several different variable annuity products, and reviews them prior to the meeting. During the meeting, the registered representative explains how annuities work and the key benefits, features, and differences among the specific products to the client. Based on the subsequent discussion, she expressly recommends that the client purchase one particular product.

In this scenario, the registered representative has made a recommendation and is therefore subject to the best interest standard imposed under Reg BI, including the component conflict of interest obligation. However, she made no use of any covered technology in connection with this interaction, and therefore, the Proposed Conflicts Rules would not apply. As a result, the registered representative would be required to comply with her firm's policies and procedures to disclose and mitigate, or in some cases, eliminate, any conflicts of interest she may have. She would not, however, be required to eliminate or neutralize the effects of any such conflicts of interest.

The second scenario is the same as the first, except that the registered representative uses modern technology to conduct a more thorough and advanced analysis of the client's investment profile, and determines, based on that analysis, that the client could benefit from the features of certain variable annuity products but first needs to be provided with basic education on variable annuities and how they differ from other investments. The registered representative then uses her firm's internal database and other tools to identify educational materials that would be helpful to the client, and to produce illustrations to make it easier for the client to understand the costs, features, benefits, and risks of particular products that could help meet the client's needs. As in the first scenario, based on the subsequent discussion, she recommends that the client purchase one particular product.

Once again, Reg BI will apply because the registered representative has actually made a recommendation to her client, and she would therefore have to disclose and mitigate, or in some cases, eliminate, any conflicts she may have. She would also have to comply with policies and procedures implemented by her Firm, including Firm-level controls to prevent conflicts from influencing the registered representative's recommendation as required by Reg BI (e.g., by compensating her the same regardless of the product recommended).

However, because she utilized technology in several ways in advance of and throughout the interaction with the client, the Proposed Conflicts Rules – if adopted in its current form – would also apply. In theory, one of those technologies might have somehow taken the interests of the Firm into consideration when identifying potentially valuable educational resources and/or products that could meet the client's needs. Firms would recognize, however, that registered representatives may either not be aware of the firm-level conflict and related mitigation controls or, if aware, may not have the technical expertise to meaningfully assess that risk. Therefore, having adopted and instilled a culture of compliance throughout their organizations, Firms may decline to make such technology available to their registered representatives.

The Proposed Conflicts Rules, if adopted as proposed, would call into question the continued viability of the second scenario despite the fact that the client in the second scenario would clearly benefit from the use of technology by the registered representative. The client would be presented with opportunities to

become more educated and informed about the types of products being considered as well as the specific products that could be recommended. A more educated client will be able to engage in a more meaningful dialogue with the registered representative, and together, they will be able to make a more informed decision about whether and how to proceed. If the SEC moves forward with the Proposal, however, many clients would likely lose access to these benefits, as helpful technology designed and intended to produce better client experiences and outcomes would no longer be available to the registered representative.

Would the client in the second scenario be better served and protected if the Proposed Conflicts Rules are adopted? In our view, clearly not.

And would the client in the second scenario face greater risk and likelihood of harm if the Proposed Conflicts Rules are not adopted? We do not believe so, and the SEC has offered nothing more than mere speculation to support the assertion that the Proposed Conflicts Rules are necessary to effectively protect investors from the theoretical risks that could be associated with certain types of technology. Disclosure in the second scenario would have sufficed to inform the client about the conflict and provided the client with an opportunity to ask questions and decide whether to accept the registered representative's recommendation, but the draconian approach reflected in the Proposal makes clear that disclosure and informed consent would not satisfy the requirements of the Proposed Conflicts Rules.

The inclusion of activities related to marketing and business development within the scope of "investor interaction" is troubling for different reasons. Historically and appropriately, the SEC and FINRA have imposed rules designed to ensure that marketing materials are fair and balanced, not materially misleading, inaccurate, or incomplete. Now, however, the SEC asserts that the use of covered technology to support legitimate efforts to grow a Firm's business somehow requires the imposition of an obligation to put the investors' interests ahead of the Firm's when pursuing such efforts. The SEC states in the Proposal that, "[w]e recognize that many investor interactions could have the sole goal of encouraging investors to open a new account, and that firms may use covered technologies for this purpose. The proposed conflicts rules would not require conflicts of interest that exist solely due to a firm seeking to open a new investor account to be eliminated or their effects neutralized. Even though opening an account would likely be in the interest of the firm, the proposed conflicts rules are not designed to limit firms' abilities to attract clients and customers." However, even this seemingly broad exclusion from the conflicts analysis requirement is unclear and vague due to the inclusion of "solely." Without clarifying exactly which specific investor interactions involving covered technology used by Firms to attract new clients or customers fall within this exclusion, Firms that, in good faith, determine, a particular investor interaction was used or foreseeably could be used "solely" for such purposes, could find themselves having to defend such determination if questioned by the SEC.

VI. The Definitions of "Investor" Are Needlessly Overbroad.

Under the Proposal, the term "investor" would be defined in the BD context as "a natural person, or the legal representative of such a natural person, who seeks to receive or receives services primarily for

personal, family, or household purposes."[31] For IAs, "investor" would mean "any prospective or current client of an investment adviser or any prospective or current investor in a pooled investment vehicle (as defined in § 275.206(4)–8) advised by the investment adviser."[32] In both cases, the Proposal would needlessly apply far more broadly than existing standards of conduct.

The inclusion of prospective clients in the definitions of "investor" is a significant departure from long-standing precedent under the federal securities laws and is problematic for many of the same reasons outlined above with respect to the applicability of the Proposed Conflicts Rules to non-recommendations. Prospective clients are entitled to receive the Firm's Form CRS, and in the IA context, prospective clients are also protected by the Advisers Act's antifraud rules.[33] The SEC has provided no evidence that prospective clients are in need of any further protections, nor has it offered any other meaningful justification for the application of the Proposed Conflicts Rules unless and until a prospective client opens an account or uses any services provided by a Firm.

Moreover, the federal securities laws have, for decades, recognized that not all investors are alike, and in some cases, it is appropriate to loosen rules of general applicability in the context of those who are better positioned to protect their own interests. For example, advice provided to institutional investors has historically not been subject to the conflicts of interest rules imposed under the Advisers Act. Such investors were recognized as having a heightened level of knowledge, experience, and analytical resources, and thus less in need of the protection afforded to retail investors under the Advisers Act conflict rules. The SEC has offered no rationale in support of the proposed inclusion of institutional investors in the definition of "investor" as applied to IAs, and therefore represents another example of the extensive overreach of the Proposal.

VII. The Proposal Disregards Decades of Regulatory and Judicial Precedent by Incorporating a New, Unique, and Far-Reaching Definition of Conflict of Interest.

Sixty years ago, the Supreme Court established that, under the Advisers Act, a conflict of interest must be disclosed or eliminated when it "might incline the [Adviser] – consciously or unconsciously – to render advice that is not disinterested."[34] The SEC has applied the same concept to BDs under Reg BI, noting in the Reg BI Adopting Release that BDs must "disclose all material facts relating to conflicts of interest associated with the recommendation that might incline a broker-dealer to make a recommendation that is not disinterested."[35]

By contrast, under the Proposed Conflicts Rules, a conflict of interest would exist when a Firm uses a covered technology in investor interactions that takes into consideration any interest of the Firm or its associated persons. In effect, this substantially lowers the threshold for determining whether a conflict

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[31] Proposal, at 53973-53974.

[32] Id.

[33] See Fiduciary Interpretation, footnote 42 (noting that, "with respect to prospective clients, investment advisers have antifraud liability under section 206 of the Advisers Act, which, among other things, applies to transactions, practices, or courses of business which operate as a fraud or deceit upon prospective clients, including those regarding investment strategy, engaging a sub-adviser, and account type.").

[34] *SEC v. Capital Gains Research Bureau, Inc.*, 375 US 180 (1963).

[35] Reg BI Adopting Release, at 33321.

of interest may exist. Under this formulation, a conflict would exist and the requirement to eliminate or neutralize would be triggered if even the slightest interest of the Firm is taken into account in any way, even if that Firm interest does not override the investor's interest.

As with so many other elements of the Proposal, the SEC has provided no substantive arguments or evidence to support disregarding sixty years of Supreme Court jurisprudence and its own rules to establish a new, broader definition of "conflict of interest" for purposes of the Proposed Conflicts Rules.

VIII. By Requiring More Than Disclosure to Address All Conflicts of Interest, the Proposal Rejects a Core Principle of the Federal Securities Laws.

In the Proposal, the SEC suggests that the rapid acceleration of PDA-like technologies in the investment industry presents additional challenges associated with identifying and addressing conflicts of interest resulting from the use of covered technologies. Therefore, the SEC proclaims "disclosure may be ineffective in light of…the rate of investor interactions, the size of the datasets, the complexity of the algorithms on which the PDA-like technology is based, and the ability of the technology to learn investor preferences or behavior."[36] The Proposal asserts that these factors could result in lengthy, highly technical, and variable disclosures, which could cause investors difficulty in understanding the disclosure. Based on its perception of the "inherent complexity and opacity of these technologies as well as their potential for scaling," the SEC has proposed that disclosure and consent are insufficient to protect investors and that Firms should instead be required to eliminate such conflicts or neutralize their effects.[37]

This posture, which is based on unsubstantiated speculation about the inadequacy of disclosure, is inconsistent with well-established federal securities laws and the SEC's own disclosure regimes, which are premised on the notion that informed investors can and should be permitted to decide whether to consent to conflicts that have been fully and fairly disclosed. [38]

Under sections 211(h) of the Advisers Act and section 15(l) of the Exchange Act, the SEC is explicitly directed to facilitate the provision of "simple and clear disclosures to investors regarding the terms of their relationships with brokers, dealers, and investment advisers" including any material conflicts.[39] Rather than facilitate simple and clear disclosures, the Proposal would impermissibly and unjustifiably abandon this disclosure framework and establish a new conflict resolution regime inconsistent with the statutory text, legislative intent, and prior SEC positions in the standards of conduct for Firms.

IX. The Proposed Conflicts Rules Are Unnecessary Because Existing Standards of Conduct Fully and Effectively Protect Investors from Technology-Related Conflicts.

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[36] Proposal, at 53967.

[37] Id.

[38] *See, e.g.,* 17 C.F.R. § 240.15c1-5 (requiring disclosure of control); 17 C.F.R. § 240.15c1-6 (requiring disclosure of interest in a distribution); 17 C.F.R. § 240.15c2-5 (requiring disclosure when extending or arranging credit in certain transactions); FINRA Rules 2241 and 2242 (requiring disclosure of conflicts in research reports); FINRA Rule 2262 (disclosure of control relationship with issuer); FINRA Rule 2269 (disclosure of participation or interest in primary or secondary distribution).

[39] Supra note 11.

Historically, BDs and their registered representatives were held to a suitability standard when making recommendations to retail investors, while IAs and their investment adviser representatives have been held to a fiduciary standard. In 2010, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act, under which the SEC was directed to study whether these standards should be harmonized and authorized to pursue rulemaking based on the results of the study.

The SEC staff study completed in 2011 recommended harmonization, but the SEC did not pursue rulemaking in this space until 2018. Following the vacatur of the Department of Labor's 2016 fiduciary rule, the SEC adopted Reg BI, which established a best interest standard for BDs and registered representatives, and Form CRS, which requires all BDs and IAs to provide standardized disclosures about their services, fees, and material conflicts of interest. The SEC has since issued guidance on Reg BI's care and conflict of interest obligations, as well as the application of Reg BI to account-type recommendations. The SEC and FINRA have been actively and aggressively enforcing Reg BI and Form CRS over the past two years. Reg BI and Form CRS are supplemented by requirements imposed under ERISA and regulations adopted by the state insurance departments under which financial institutions and financial professionals are required, when making recommendations, to act in the best interest of their clients without putting the interests of the Firm ahead of their clients' interests. By all accounts, this robust and comprehensive regulatory framework is working. The SEC has offered no evidence to suggest that new rules are needed to effectively protect investors.

Nevertheless, the SEC has issued the Proposal while at the same time acknowledging that these existing standards of conduct apply to conflicts arising from the use of covered technology. Specifically, the Proposed Conflicts Rules require a Firm to take steps that the SEC claims are in addition to, but not in conflict with, the standard of conduct that applies when it is providing advice or making recommendations.[40] According to the Proposed Conflicts Rules, neutralization is included as an additional method of addressing conflicts of interest thereunder due to manners in which technology can be "modified or counterweighted to eliminate the harmful effects of a conflict," that it can be tested to substantiate such modification or counterweighting was successful.[41]

Although the Proposed Conflicts Rules purport that the Proposal's new conflict of interest definition and requirements to eliminate or neutralize the effect of any identified conflict do not supplant the existing standards of conduct for Firms, in the Proposal, the SEC explicitly sets forth that failure to comply with this new standard may run afoul of existing rules until such time a conflict is eliminated or neutralized.[42] "If a firm has determined that it needs additional time to eliminate, or neutralize the effect of, a conflict of interest in accordance with the Proposed Conflicts Rules, it would also need to consider whether

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[40] Proposal, at 53986. *See also,* Proposal, at 54002 (describing the applicable standards of conduct).

[41] Proposal at 53986.

[42] Proposal at 53977, *See Also* Fn. 142: "The elimination or neutralization requirement of the proposed rules applies only to a narrower, defined subset of the broader universe of conflicts – those conflicts that a firm determines actually place the interests of the firm or certain associated persons ahead of the interests of investors. This is in contrast to, for example, an investment adviser's fiduciary duty, which encompasses any interest that might incline the adviser, consciously or subconsciously, to provide advice that is not disinterested., or similarly in contrast to the broader universe of conflicts covered by Reg BI. Other conflicts of interest that only might affect the firm's investor interactions would continue to be subject to these other obligations, as applicable."

continuing to use such covered technology before the conflict is eliminated or neutralized would violate any applicable standard of conduct (*e.g.*, fiduciary duty for investment advisers or Reg BI for broker-dealers). In certain cases, it may be impossible to comply with the applicable standard of conduct without stopping the use of the covered technology before the conflict of interest can be adequately addressed."[43] For example, technology is an essential element of Firms' Reg BI compliance programs, particularly in the context of the reasonable alternatives analysis required under Reg BI. Without access to technology, compliance with that requirement would become nearly impossible in light of the breadth and complexity of investment options available in the marketplace.[44]

Conclusion

IRI firmly believes that the Proposal must be withdrawn. It is rife with countless flaws, as explained throughout this letter and as we expect will be explained in letters from numerous other commenters. These flaws cannot be remedied in order to produce a workable and effective final rule. Instead, a fresh start is needed.

Following withdrawal of the Proposal, we encourage the SEC to undertake a more tailored, constructive, inclusive, engaging, and ongoing effort to better understand new technology and to determine how best to balance the value of innovation with the need for appropriate consumer protection. For our part, IRI would welcome the opportunity to participate in such an effort.

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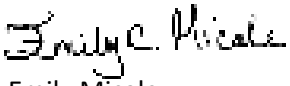
Thank you again for the opportunity to provide these comments. If you have questions about any of our comments on the Proposal or if we can further assist with matters, please contact the undersigned at jberkowitz@irionline.org or emicale@irionline.org.

Sincerely,

Jason Berkowitz
Chief Legal & Regulatory Affairs Officer
Insured Retirement Institute



Emily Micale
Director, Federal Regulatory Affairs
Insured Retirement Institute

[43] Proposal, at 53987.

[44] We note that the definition of investor interaction expressly excludes "interactions solely for purposes of meeting legal or regulatory obligations[, which] are subject to existing regulatory oversight and/or do not involve the type of conflicts the proposed rules seek to address." However, the Proposal does not make clear whether the use of covered technology to support the reasonable alternatives analysis required under Reg BI would fall within the scope of this exclusion.