

## AGENCY RULE REPORT

### TITLE 660. DEPARTMENT OF SECURITIES CHAPTER 11. OKLAHOMA UNIFORM SECURITIES ACT OF 2004

Date notice of intended rulemaking published in The Oklahoma Register: February 18, 2020

Name and address of agency:

Melanie Hall, Administrator  
Oklahoma Department of Securities  
City Place, Suite 400  
204 North Robinson  
Oklahoma City, Oklahoma 73102-7001

Titles and numbers of rules:

660:11-1-3. Definitions [AMENDED]  
660:11-5-2. Definitions [AMENDED]  
660:11-5-14. Agent termination [AMENDED]  
660:11-5-21. Supplemental disclosures [AMENDED]  
660:11-5-26. Merger and acquisition broker exemption [NEW]  
660:11-5-42. Standards of ethical practices for broker-dealers and their agents [AMENDED]  
660:11-7-2. Definitions [AMENDED]  
660:11-7-11. Initial registration [AMENDED]  
660:11-7-14. Investment adviser representative termination [NEW]  
660:11-7-20. Supplemental disclosures [AMENDED]  
660:11-7-21. Errors and omissions coverage [NEW]  
660:11-7-31. Post-registration reporting requirements [AMENDED]  
660:11-7-41. Record keeping requirements [AMENDED]  
660:11-7-42. Standards of ethical practices [AMENDED]  
660:11-7-46. Information security and privacy [NEW]  
660:11-9-31. Prospectus delivery requirement [AMENDED]  
660:11-9-33. Special requirements for promotional or ~~developmental~~-development stage companies [AMENDED]  
660:11-9-36. Promoters' and organizers' equity contributions [AMENDED]  
660:11-11-1. Definitions [AMENDED]  
660:11-11-40. Manual exemption [AMENDED]  
660:11-11-52. Oklahoma Accredited Investor Exemption [AMENDED]  
660:11-11-53. Exemption for offers but not sales [AMENDED]  
660:11-15-2. Protection from financial exploitation [New]

Authority: 71 O.S. Sections 1-605 and 1-608

Summary: The proposed rule amendments conform requirements for similar registrant categories, add protection from financial exploitation, conform investment adviser regulations relating to errors and omissions coverage and information security to model rules and/or to other states and

federal law, conform a registration exemption to a model rule and to federal law, correct statutory cites, and clarify changing regulatory procedure.

Need for rules: See Summary above. Also, the Administrator finds that 660:11-5-26, 660:11-7-14, 660:11-7-21, 660:11-7-46, 660:11-15-2 and the rule amendments are necessary or appropriate in the public interest or for the protection of investors and are consistent with the purposes intended by the Securities Act, 71 O.S.Supp.2019, §§ 1-101 through 1-701.

Details of adoption: The Administrator adopted 660:11-5-26, 660:11-7-14, 660:11-7-21, 660:11-7-46, 660:11-15-2 and the rule amendments on April 1, 2020, at the offices of the Oklahoma Department of Securities.

Summary of comments:

The Department received comments from three entities endorsing the promulgation of 660:11-5-26 concerning the exemption from registration for broker-dealers acting solely as mergers and acquisition brokers.

The Department received comments from seven entities requesting the reconsideration or clarification of the proposed language in Rule 660:11-7-42 regarding the provision clarifying the already established fiduciary duty of investment advisers and investment adviser representatives to their clients and the introductory language regarding the application of National Securities Markets Improvement Act of 1996 (Pub. L. No. 104-290). Several of the entities also expressed reservations over the provision prohibiting a firm from requiring arbitration in its investment advisory contracts.

The Department received a comment from one entity requesting that the proposed language in Rule 660:11-15-2 be amended to make it more uniform with recent legislation and rules in other states.

The Department staff recommended the correction of scrivener errors and citations that were not in the precise form mandated by the OAC rules on rulemaking and the addition and retraction of language and consequent renumbering and to clarify references to model rules and federal law. The Department staff made additional comments in response to the public comments.

The Administrator reviewed the comments made by all of the persons.

The Administrator chose to not proceed at this time with the language in Rule 660:11-7-42 describing the fiduciary duty owed by investment advisers and investment adviser representatives to their clients. The Administrator notes that such fiduciary duty is already imposed by caselaw and reserves the right to revisit this issue in the future.

The Administrator also chose not to proceed at this time with the language in Rule 660:11-7-42 limiting an investment adviser from requiring an arbitration forum in its investment advisory contracts for resolution of any conflicts. This issue may also be revisited in the future.

The Administrator revised the proposed language in Rule 660:11-15-2 to make it more uniform with rules or legislation recently passed by other states in that a securities firm must only report suspected financial abuse to the Department upon determination of such abuse.

The Administrator adopted the staff comments concerning matters raised by the public comments and to correct scrivener errors and renumbering as needed.

Hearing attendees by teleconference: Melanie Hall, Administrator; Department staff - Z. Faye Martin Morton, Gerri Kavanaugh, Terra Bonnell, and Carol Gruis; Marin Gibson, representing SIFMA; John Johnson, representing Campaign for Clarity; and Robin Traxler, representing the Financial Services Institute, and Jenny Kalsu, a court reporter for Word for Word Reporting, LLC.

Attached is the pertinent rule impact statement.

Proposed effective date: November 1, 2020.

**RULE IMPACT STATEMENT**  
**OAC 660:11**

Pursuant to the Administrative Procedures Act, Section 303.D of Title 75 of the Oklahoma Statutes, the Oklahoma Department of Securities ("Department") hereby submits the following Rule Impact Statement for PERMANENT rule proposals for OAC Title 660, Department of Securities, Chapter 11, Oklahoma Uniform Securities Act of 2004.

**Brief Description of the Purpose of the Proposed Rules and Rule Amendments:**

The proposed rule amendments conform requirements for similar registrant categories, add protection from financial exploitation for vulnerable adults, reinforce the requirement that investment advisers cannot impose forum selection clauses (specifically those for mandatory arbitration) conform investment adviser regulations relating to errors and omissions coverage and information security to model rules and to federal law, conform a registration exemption to a model rule and to federal law, correct statutory cites, and clarify changing regulatory procedure.

**Description of the classes of persons who most likely will be affected by the rule proposals, including classes that will bear the cost of the rule proposals, and any information on cost impacts received by the agency from any private or public entities:**

One proposed new rule provides an exemption from registration for certain broker-dealers and their agents who conduct mergers and acquisitions. One proposed new rule describes the procedures by which an investment adviser representative notifies Department of their termination. One new rule and three amended rules require registered investment advisers to maintain errors and omissions insurance policies. Department staff conducted a survey of Oklahoma-based investment advisers that indicated almost half already maintained such insurance. The cost of the insurance ranged between \$707.00 to \$12,359.00 dependent on the number of investment adviser representatives, the amount of assets under management and a risk assessment of the firm and individuals. One new rule requires investment advisers to implement and maintain information and security policies. One new rule requires broker-dealers, agents, investment advisers, and investment adviser representatives to notify the Department should they have reason to believe that a vulnerable adult is being financially exploited and to allow the firms to place a temporary hold on the customer's account. One amended rule clarifies that mandatory arbitration cannot be included in investment advisory contracts due to the existing prohibition of forum selection clauses. This clarification will require investment advisers to review their contracts with clients and, in some instances, enter into new or amended contracts. It may also require an investment adviser to seek legal or compliance advice to ensure its contracts are compliant. The Department has not conducted an analysis of any corresponding costs which will be dependent on the investment adviser's number of clients and any legal or compliance advice the investment adviser chooses to obtain. Two amended rules make it an unethical practice for broker-dealers and investment advisers to share offices with non-related persons without disclosing their relationship and safeguarding customer data. One amended rule specifies the duty of care owed by an investment adviser and investment adviser representative to their clients. Persons subject to Department regulation and Department staff members might experience less stress in compliance with securities laws. The staff has not received any information on cost

impacts from any private or public entities and does not anticipate any other significant impact as a result of the rule proposals.

**Description of the classes of persons who will benefit from the rule proposals:**

Certain broker-dealers and their agents who conduct mergers and acquisitions will no longer have to register with the Department. Vulnerable adults may lose less of their hard-earned life savings if firms and individuals report potential exploitation. Investment advisers and their clients may benefit from errors and omissions policies because clients could often recoup arbitration or court awards without jeopardizing the solvency and viability of firms. Investors will be allowed to choose a convenient and non-restrictive forum to resolve disputes. Investors will benefit from understanding the relationship between persons sharing offices. Persons subject to Department regulation and Department staff members may benefit from the rules and the amendments due to more precise information and greater clarification to aid in compliance.

**Description of the probable economic impact of the rule proposals upon affected classes of persons or political subdivisions, including a listing for all fee changes and, whenever possible, separate justification for each fee change:**

Certain broker-dealers and agents exempted from registration would no longer have the expenses of registration. Certain investment advisers may experience expenses in the initial preparation of information and privacy policies, but the expenses should not be significant or ongoing. Investment advisers will experience increased expenses due to the purchase of errors and omissions insurance, however the benefit to themselves and to their clients will outweigh that expense. A Department survey concluded that almost 50% of Oklahoma -based investment advisers already carry errors and omissions insurance. Of the Oklahoma-based investment advisers surveyed, the average annual premium for a \$1,000,000.00 policy ranged from \$707.00 to \$12,359.00. The disparity in premiums are due to exclusions in the policies, the number of investment adviser representatives, the amount of assets under management, and, most importantly, an assessment of risk. Investment advisers who require mandatory arbitration will need to obtain new or amended contracts with their clients. The economic impact of this rule will be dependent on the number of clients an investment adviser has whose contracts include mandatory arbitration and any costs the investment adviser chooses to spend on legal or compliance advice. No significant economic impact is expected on any other affected classes of persons or political subdivisions as a result of the proposed new rules and amendments. The proposed rules and rule amendments do not change or create any fees.

**The probable costs and benefits to the agency and to any other agency of the implementation and enforcement of the rule proposals, the source of revenue to be used for implementation and enforcement of the rule proposals, and any anticipated effects on state revenues, including a projected net loss or gain in such revenues if it can be projected by the agency:**

No additional revenue will be needed for the implementation or enforcement of the proposed rules and rule amendments. The changes likely will increase efficiency of agency personnel due to greater clarity in compliance requirements for regulated persons.

**A determination of whether implementation of the rule proposals will have an economic impact on any political subdivisions or require their cooperation in implementing or enforcing the rules:**

Implementation of the proposed rules and rule amendments is not anticipated to have an economic impact on any political subdivisions or require the cooperation of political subdivisions in implementing or enforcing the proposed rules or rule amendments.

**A determination of whether implementation of the rule proposals may have an adverse economic effect on small business as provided by the Oklahoma Small Business Regulatory Flexibility Act:**

The errors and omissions insurance requirement will cause smaller investment advisers additional expense, but will also afford greater protection to the investment advisers and to their clients. The mandatory arbitration clause will require investment advisers who require mandatory arbitration to enter into new contracts or amend the contracts with their clients. The economic impact will vary based on how many affected clients the investment adviser has and the fee of any counsel the investment adviser seeks regarding compliance. No other known adverse economic impact on any small business is expected as a result of the proposed rules and rule amendments.

**An explanation of the measures the agency has taken to minimize compliance costs and a determination of whether there are less costly or nonregulatory methods or less intrusive methods for achieving the purpose of the rule proposals:**

The Department limited the errors and omissions policies to a minimum coverage of \$1,000,000. Conforming any affected advisory contracts with the mandatory arbitration provision may involve only minimal costs to include any conferences with clients to explain changes. The Department's staff does not anticipate any other increased costs as a result of the rule proposals. Department staff is unaware of any less costly or nonregulatory methods or less intrusive methods for achieving the purpose of the proposed rules and rule amendments.

**A determination of the effect of the rule proposals on the public health, safety and environment and, if the rule proposals are designed to reduce significant risks to the public health, safety and environment, an explanation of the nature of the risk and to what extent the rule proposals will reduce the risk:**

The rules relating to financial exploitation of vulnerable adult and the errors and omissions insurance should significantly affect the health and safety of persons who need those protections most - namely, older persons whose life savings are at risk and all persons who are clients of investment advisers that cannot afford to pay arbitration or court awards. The staff of the Department is unaware of any negative effect the proposed rules and amendments would have on the public health, safety and environment.

**A determination of any detrimental effect on the public health, safety and environment if the rule proposals are not implemented:**

The staff of the Department believes there will be a significant detrimental effect on the public health and safety of certain populations if the vulnerable adult rule and the errors and omission rules and amendments are not implemented.

**This rule impact statement was prepared on March 4, 2020.**