VIA Electronic Mail: **pubcom@finra.org**

July 11, 2025

Ms. Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1700 K Street, NW
Washington, DC 20006-1506

Re: **Regulatory Notice 25-07 – Request for Comment: Supporting Modern Member Workplaces**

Dear Ms. Mitchell:

Please allow this to serve as comments from Cetera Financial Group, Inc. ("Cetera") with respect to FINRA Regulatory Notice 25-07. Notice 25-07 seeks comments regarding the effectiveness of certain FINRA rules and how they might be adapted to conform to recent changes in the securities industry and how it conducts business.

Cetera is the corporate parent of five FINRA member firms and two investment advisers. Through our nearly 14,000 financial professionals, we provide securities brokerage and investment advisory services to more than 1 million retail investors in all 50 states. Our customers are primarily individuals, families, and small businesses. Many of our branch locations are outside of urban areas, and typically house less than five associated persons and support staff.

We commend FINRA for taking this opportunity to seek comments from its membership and other interested parties with regard to member firm workplaces and operations. The past decade has produced unprecedented changes in technology, societal working habits, and communication methods, all of which have affected FINRA members and their customers in countless ways. These changes have caused many existing rules to become out of date, and a holistic look at the entire FINRA regulatory framework is appropriate at this time. Not all constituents will agree on whether or how rule changes should be made, but we believe that the broad approach taken by FINRA in Notices 25-07 and 25-04 is well calculated to achieve a result that will best serve the interests of the greatest number of people.

We will offer comments on specific issues, but at the outset, we believe it is helpful to consider how technology has changed the environment for both the securities industry and the customers we serve. Modern technology has revolutionized most knowledge-based industries by transforming the workplace from physical office spaces to centralized electronic systems. While members once operated in a largely paper-based environment, new technology has increased both the efficacy of virtual or digital platforms and investor preference for them. This trend was accelerated by the COVID-19 pandemic, which necessitated a quantum leap into adoption of fully-remote capabilities, work habits, procedures, and controls.

All of these phenomena are particularly relevant to the FINRA framework for definition of office locations that are deemed branches. When the current definitions for branch locations were adopted, virtually all work was conducted in physical offices with firm employees present. Employees generally needed to be in an office in order to accomplish their work functions, and supervision was largely conducted by managers who were physically present. Activities identified as presenting the greatest degree of risk or materiality were deemed to specifically require supervisory presence in an Office of Supervisory Jurisdiction, or OSJ.

Today's workplace is completely different. With the advance of technology, physical offices have been replaced by electronic networks. For the vast majority of FINRA members, employees can work and supervise others from any location that has internet access. Employees often have the ability to work at any hour from any location. Many work on a fully-remote basis and do not attend a firm-owned facility unless there is a specific need. Even when employees work in offices on a regular basis, business functions are being conducted from other locations. The gains in productivity resulting from the ability to accommodate employee lifestyles and location preferences have been enormous.

The securities industry is not unusual in that technology has changed the way it operates, but it is nearly unique in one respect: FINRA members are subject to a regulatory regime that often prevents them from fully utilizing technological advances that will benefit both themselves and their customers. Many current regulations were formulated in a working environment that simply no longer exists.

It is not unusual for regulation to lag behind the development of the industry that it oversees, but regulatory agencies should be vigilant and take regular opportunities to review their rules, recognize how conditions have changed, and adapt their regimes to more closely fit the actual conditions. The technological change that has brought revolutionary improvements in investment products and services, increased access and usability of advice, productivity gains, and concomitant reductions in costs borne by investors has not always been incorporated in rulemaking by FINRA and other regulatory agencies.

FINRA has recently adopted significant rule changes that made important strides in this direction. Amendments to FINRA Rule 3110.19 relating to designation of Residential Supervisory Locations and Rule 3110.18 relating to the timing and manner of inspection of branch offices represented important modernization efforts. (We commend FINRA for its foresight in proposing these changes and persistence in seeing them through approval by the SEC. It does not appear to have been easy.) In the spirit of those efforts, we suggest a few other matters that FINRA should consider as part of a broader effort to update its rules.

1. Definition of Branch Offices

Technology has completely altered the way in which investment advice and securities brokerage services are delivered to customers. As recently as 25 years ago, virtually all orders for transactions were conveyed in person or by telephone, with the active involvement of a firm employee. Customer funds and securities were delivered through the mail or in-person, and the products and services offered through FINRA member firms were far more limited than they are today.

Transactions are now routinely conducted via online platforms, often through personal communication devices such as cellphones. Electronic technology, algorithmic programs, and Artificial Intelligence have replaced much of the human role in supervision, from review and approval of transaction activity to oversight of funds movement. These advances have made firms more cost-efficient, and have also produced better and more comprehensive supervisory oversight capabilities with corresponding benefits for customers. It is hard to argue that a single branch manager reviewing individual transaction tickets provides a more effective level of oversight than the electronic supervision systems in place at most FINRA members today. The important point is that the development of technology has rendered traditional definitions of branch locations based on the functions performed in them obsolete.

The Securities Industry and Financial Markets Association ("SIFMA") has submitted extensive comments on categorization of branch offices, and we endorse their views. We submit that only physical premises which are ***held out to the public as places where customers may transact business or meet in person with a representative of the firm to transact business on a regular basis*** should be deemed branch offices for purposes of FINRA Rule 3110. No other locations from which firm business is conducted, temporarily or otherwise, should be defined as branches.

All branch locations should be subject to current rules relating to inspections, consistent with the provisions of FINRA Rule 3110.18. Member firms should be free to design and implement systems that best fit their business and clientele. The Pilot Program established by Rule 3110.18 also represents a huge leap forward for both firms and FINRA. It establishes the proposition that member firms should be allowed to assess their branch offices and the activities that take place in them and implement inspection processes that are calculated to yield the best results in relation to the resources devoted.

We also submit that the current OSJ designation no longer has any practical significance. Physical locations in which specific functions are conducted should be subject to a higher level of oversight, but that comprises a very short list. It would include locations in which primary versions (not copies) of required records are maintained or where customer funds or securities are routinely held for more than one day. The current definition of OSJ is overly broad and provides little practical use for member firms or customers.

2. Electronic Delivery of Customer Communications

Over the past 25 years, delivery of information to customers of almost all businesses has transformed from paper documents delivered by the U.S. Postal Service to electronic communications delivered via e-mail or other similar facilities. This is especially consequential to the securities industry. Broker-dealers are required to deliver written notices to customers in numerous instances, including confirmation of transactions, monthly account statements, and account records mandated by SEC Rule 17a-3(a)(17). SEC regulations also mandate regular delivery of voluminous amounts of disclosure material under the provisions of SEC Regulation Best Interest, Regulation S-P, and other similar rules.

Delivery of paper communications to customers is expensive and resource-consuming. It creates negative impacts on the environment through paper manufacturing and large volumes of paper waste that must be disposed of in landfills. It also creates opportunities for bad actors to obtain sensitive financial information about customers by intercepting physical mail, particularly in urban locations where residents share common mail facilities. A significant percentage of our customers have opted for electronic delivery as their exclusive method. We believe this trend will continue for a number of reasons, including how it facilitates customers' ability to access, review, and store their documents.

The rules applicable to delivery of required communications to customers are primarily governed by the SEC. Unfortunately, SEC guidance on this issue dates back nearly 25 years, and is woefully out of step with the modern world. We recognize that there are limits to what FINRA can do without action from the SEC, but we suggest that all regulatory regimes in the securities industry should permit electronic delivery as a default mechanism for all communications to customers unless the customer specifically requests otherwise.

There have been a number of recent efforts to promote electronic delivery of documents to investors. They include:

- The Improving Disclosures for Investors Act of 2023, introduced in the past session of Congress.[1] This legislation has not been passed, but recognizes the important and growing role of electronic communications for investors.

- SIFMA has published an extensive study on the topic of electronic delivery by securities firms.[2] It includes a discussion of the factors we have noted above, and proposes a constructive regime on which to build.

- The American Council of Life Insurers, Committee of Annuity Insurers and the Insured Retirement Institute have proposed a regime to foster electronic delivery as the default

[1] H.R. 1807 (12/01/2023).

[2] *See,* SIFMA, SIFMA AMG, FSI, and IAA Whitepaper, *E-Delivery: Modernizing the Regulatory Communications Framework to Meet Investor Needs for the 21st Century* (Sept. 2020), available at https://www.sifma.org/wp-content/uploads/2020/09/E-Delivery-Paper.pdf.

option for delivery of documents to customers. (Please see attached letter from these organizations to Chairman Jay Clayton of the SEC, dated October 23, 2020.)

- In October, 2019, the U.S. Department of Labor published proposed regulations dealing with electronic delivery as a default mechanism for delivery of required communications under ERISA.[3] The ERISA statute exists for purposes other than governing how documents are delivered to retirement investors. We suggest, however, that the underlying principle of promoting electronic delivery of all investment-related communications to investors is an important goal. The Department of Labor has attempted to move toward more modern standards for delivery of investment-related communications. FINRA and the SEC should do the same.

3. <u>Compensation Arrangements</u>

a. Payment of Compensation to Personal Service Entities

Notice 25-07 requests comments regarding payment of compensation to Personal Services Entities ("PSEs"). FINRA Rule 2040 generally prohibits payment of securities-related compensation to any individual or entity that is not registered as a broker. We believe that certain provisions of Rule 2040 are out of date and should be modernized.

SEC regulations require individuals or entities operating as brokers to register with the SEC and FINRA. A primary purpose of Rule 2040 is to assure that individuals or entities that receive commissions or other securities-related compensation, (often referred to as Transaction-Based Compensation, or "TBC") are subject to supervision by member firms and the jurisdiction of FINRA and the SEC. This is a logical approach. Individuals who are not properly identified and monitored should not be involved in the securities business of the member or have financial incentives connected to it. However, Rule 2040 is unduly restrictive in instances where associated persons of a member form and operate a PSE and are subject to oversight and supervision. Rule 2040 should be amended to provide that payments to the PSEs are permissible under specified circumstances.

Notice 25-07 points out that associated persons often work in teams. This is true at many FINRA member firms, but it is particularly common among firms that employ independent contractors ("ICs") as representatives. The majority of Cetera's representatives are ICs, and it is our understanding that many of them utilize PSEs. Most member firms are unwilling to pay compensation directly to PSEs, so the ICs receive compensation from the broker-dealer in their individual capacity and assign it to the PSE. The PSE then pays the operating expenses of the group and compensation to the individual owners based on a formula or other allocation.

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[3] See RIN1210-AB90, Federal Register : Default Electronic Disclosure by Employee Pension Benefit Plans Under ERISA.

The assignment of compensation to the PSE accomplishes the objective of aggregating TBC produced by the members of the group and facilitating payment of operating expenses, but since the individuals receive compensation directly from the broker-dealer, they receive an annual report of what they received as income on IRS Form 1099. This often leads to a mismatch between the income reported to the IRS as attributable to the individual and the actual amount received from the PSE after deduction of business expenses and allocation among the owners of the PSE. This creates a number of tax reporting issues and the potential for costly and time-consuming tax audits for both the PSE and the individual representatives. A recent Tax Court decision also casts doubt on the viability of assigning income to a PSE under the current FINRA and SEC framework.[4]

Recent data from FINRA indicates that approximately 25% of all large and medium-sized FINRA members identify themselves as IC firms[5], and we believe that the percentage of associated persons who are ICs is greater than 25%. Amending Rule 2040 to permit direct payments to PSEs would provide a significant benefit to a large number of FINRA member firms and representatives without a material negative impact on investor protection.

We also note that many representatives of FINRA member firms engage in Outside Business Activities ("OBAs") which are conducted away from the firm. These include sales of insurance products, tax preparation services, and investment advisory activities. Associated persons conducting OBAs are subject to the provisions of FINRA Rule 3240 and investment advisory business conducted through unaffiliated entities is subject to supervision by member firms under existing FINRA rules, but such activities are often conducted as OBAs.

The large majority of retail-focused FINRA member firms offer both securities brokerage and investment advisory services to customers, either as dually-registered entities or by offering investment advisory services through an affiliate. These services are provided to customers through associated persons acting as both registered representatives and Investment Advisor Representatives. SEC policy permits investment advisers to pay investment advisory fees to PSEs. We thus have a system under which the same agency (the SEC) regulates the same entities and individuals (broker-dealers, investment advisers, and their associated persons) providing very similar services to the same customers, but does not permit the same payment mechanisms. This is anomalous at best. We also note that the laws of most states permit insurance companies to pay insurance commissions and related revenue to PSEs that are not registered as insurance agencies.

The SEC has issued guidance on many occasions with respect to payment of TBC to unregistered entities, often in the form of No-Action letters. Notice 25-07 refers to one such letter, in which the SEC notes that receipt of TBC is not, in and of itself,

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[4] See Fleischer v. Commissioner of Internal Revenue, Tax Court Memo 2016-238.
[5] 2024-Industry-Snapshot.pdf

determinative of broker status. However, SEC guidance on this topic has generally been limited to narrow sets of facts and circumstances, and has never specifically addressed the broad prohibition on payments to PSEs in Rule 2040.

The SEC has noted concerns about payments of TBC to individuals who are not subject to oversight and control, and Rule 2040 should include limitations on the ability to pay TBC to PSEs. These could include requirements that all owners of the PSE be associated persons of the broker-dealer, acknowledgment by the PSE that it is subject to oversight by both the firm and applicable authorities, or other appropriate proscriptions.

FINRA has a legitimate interest in knowing who is receiving TBC and whether or not they are involved in the securities business of a member firm. That is necessary for customer protection. However, if FINRA has sufficient visibility and control over instances in which TBC is being made to PSEs owned or controlled by associated persons of members, amending Rule 2040 to allow for direct payment of TBC to PSEs will create significant benefits for IC representatives without any reduction in customer protection.

b. Continuing Commission Arrangements

Notice 25-07 also requests comments on continuing commission arrangements. It is our understanding that ICs often utilize PSEs to promote succession planning and continuity in ownership of their business and relationships with their customers. The PSE structure encourages shared responsibility for customer relationships, specialization among team members, and opportunities to realize the value of a business that many representatives have spent their lives building.

The median age of FINRA representatives has been estimated to be approximately 50, but this is likely misleading. We believe that the large majority of the customer assets at FINRA members is administered by representatives aged 60 or older. This is perhaps to be expected, given that older representatives have been in the business longer and presumably have more customers. They also tend to have customers who are older and own or control a disproportionate amount of all investment assets. In any event, numerous studies, including one by McKinsey & Co. have predicted an avalanche of retirements by experienced financial advisers in the coming decade.[6] FINRA, member firms, and representatives all have an interest in promoting the orderly transition of customer relationships and investment assets from retiring representatives to teams that are familiar with customers and are likely to remain in the business for a long time.

FINRA Rule 2040(b) permits payment of compensation to retired or disabled representatives, their survivors, or other beneficiaries under certain circumstances. One of the requirements is that there must be an agreement between the member firm and the individual prior to the time when the payments start. This is a reasonable condition in these circumstances, and Cetera has encouraged its financial professionals to enter into agreements with us providing for ongoing compensation as provided in Rule 2040(b).

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[6] McKinsey Study - The-looming-advisor-shortage-in-US-wealth-management.pdf 03.2025.pdf

Unfortunately, we are aware of instances in which representatives died or became disabled prior to establishment of a formal agreement with the firm.

In order to make payments to any beneficiary within the provisions of Rule 2040(b), the agreement must be in place prior to the death or disability of the representative. If it is not, member firms will likely be unwilling to make payments to survivors or other beneficiaries, which could create significant economic hardship for them. Amending Rule 2040 to allow for payments to PSEs would allow the value of the ownership interest of a deceased or disabled representative/owner to be transferred to survivors through a purchase of that interest by the PSE or the other owners. Rule 2040 should prevent transfer of an ownership interest in a PSE to individuals who would not otherwise be eligible to own it, but should provide for a reasonable period of time in which to allow for sale or disposition of a deceased or disabled owner's interest to individuals who are authorized to acquire it.

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Thank you for providing us this opportunity to comment on these important issues. We look forward to further engagement with FINRA and it's staff on all of them. If you have questions or we may offer any further information on any of these matters, please let me know.

Sincerely,

Mark Quinn
Director of Regulatory Affairs
Cetera Financial Group

October 23, 2020

SUBMITTED ELECTRONICALLY

The Honorable Jay Clayton
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Electronic Delivery of Required Documents under the Federal Securities Laws

The American Council of Life Insurers,[1] the Committee of Annuity Insurers[2] and the Insured Retirement Institute[3] (together, the "***Associations***") urge the Securities and Exchange Commission ("***Commission***" or "***SEC***") to update its interpretive guidance and regulations governing the electronic delivery of documents by issuers of investment company and other SEC-registered securities (including issuers of variable insurance and annuity contracts), broker-dealers, investment advisers and transfer agents (together, "***Financial Services Firms***"). It has been a quarter of a century since the Commission first established general requirements for electronically delivering documents required to be delivered under the federal securities laws ("***Required Documents***").[4] Transformative advances in technology and communication, broad adoption of these technologies by the investing public, changes in investor preference for receiving investor communications, as well as the recent demands of the COVID-19 pandemic which required emergency relief in this area, demonstrate the unquestionable need for the

[1] The American Council of Life Insurers ("***ACLI***") is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 280 member companies represent 94 percent of industry assets in the United States.

[2] The Committee of Annuity Insurers ("***CAI***") is a coalition of life insurance companies formed in 1981 to participate in the development of federal policy with respect to tax, securities, ERISA, and banking law issues affecting annuities. The Committee's current 32 member companies represent over 80% of the annuity business in the United States and are among the largest issuers of annuity contracts to IRAs and employer-sponsored retirement plans. A list of the Committee's member companies is attached as Exhibit A.

[3] The Insured Retirement Institute ("***IRI***") is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, and distributors such as broker-dealers, banks and marketing organizations. IRI members account for more than 95 percent of annuity assets in the U.S., the top 10 distributors of annuities ranked by assets under management 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.

[4] *See Use of Electronic Media for Delivery Purposes,* Release No. 36345 (Oct. 1995) (**"*1995 Release*"**); *Use of Electronic Media by Broker- Dealers, Transfer Agents, and Investment Advisers for Delivery of Information*; *Additional Examples Under the Securities Act of 1933*, Securities Exchange Act of 1934, and Investment Company Act of 1940, Release No. 37182 (May 1996) ("***1996 Release***"); *Use of Electronic Media,* Exchange Act, Release No. 42728 (Apr. 2000) ("***2000 Release***"), together, the "***SEC Releases***."

Commission to update the applicable regulatory framework. Indeed, the Associations respectfully submit that the focus of any future discourse with regard to e-delivery should not be whether change is needed and warranted, but instead what the breadth and scope of those changes should be.

Since setting forth its general requirements, the Commission has developed a patch-work of specific rules for the electronic delivery of certain Required Documents, such as proxy materials for fund shareholders, insurance dedicated fund statutory prospectuses underlying variable contracts, variable contract statutory prospectuses, semi-annual fund reports, and final prospectuses for certain types of issuers. The resulting e-delivery framework now in place contains different delivery standards for particular documents in addition to the general standards that apply to all other documents. This fragmented approach is both confusing to investors and burdensome for Financial Services Firms to administer on a document by document basis. Moreover, an ad hoc approach is inconsistent with, and ill-fitted to, the pervasive on-line world that we now live in. Our transition to a touchless society has accelerated consumers' and business' use and acceptance of electronic delivery of all forms of documents. The paradigms established by the Commission were created when paper was the preferred method of delivery and the digital world was far into the future. We suggest that it is time for the regulatory community to create paradigms that embrace a digital consumer and business model. To achieve that purpose, the Associations believe that the time has come for promulgating a comprehensive framework where e-delivery, not paper, is the default for *all* Required Documents and *all* end-users, i.e., both new investors and current ones.

To this end, we are encouraged by the recent statement made by Dalia Blass, Director of the Division of Investment Management, that it is "time to reconsider our approach to shareholder and client communications ... [and] consider guidance that treats physical and electronic delivery as equals rather than measuring delivery against a paper standard."[5] In addition, we applaud other industry participants who have recently made extensive submissions to the Commission calling for a holistic e-delivery regulatory framework that places a default to e-delivery as its cornerstone.[6] We strongly support these Industry Letters, in spirit and largely in substance. Specifically, we are in full agreement with the investor benefits of e-delivery so aptly described, and we generally agree with new e-delivery framework laid out in these submissions. In addition, we believe the numerous e-delivery data points relating to investor preferences, on-line usage and enhanced investor experience that were included in the Industry Letters amply justify the Commission's need to modernize its now outdated general approach to e-delivery.[7]

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[5] *See* D. Blass, Director, Division of Investment Management, *Speech: PLI Investment Management Institute* (Jul. 2020) ("D. Blass Speech"), at https://www.sec.gov/news/speech/blass-speech-pli-investment-management-institute.
[6] *See, e.g.,* "E-Delivery: Modernizing the Regulatory Communications Framework to Meet Investor Needs for the 21st Century" from SIFMA dated September 2020 ("***SIFMA Paper***"); the letter from Fidelity, Charles Schwab and Blackrock dated September 8, 2020 to Chairman Clayton ("***Fidelity Letter'***); and the letter from the Investment Company Institute dated September 10, 2020 to Dalia Blass ("***ICI Letter"***) (together, "Industry Letters").
[7] We also note the important environmental benefits associated with any enhanced e-delivery framework and the concomitant reduction of paper reports and documents, including fewer trees needed to make paper, a reduction in landfill waste and a reduction in resources associated with processing, printing, and transporting paper documents (which ultimately reduce greenhouse gas emissions, water consumption and pollution, air pollution, wood and energy use, and solid waste). *See, e.g., Optional Internet Availability of Investment Company Shareholder Reports,* Release No. 33-10506 (Jun. 2018), at p.25 (discussing environmental benefits).

Like other industry participants, the Associations believe that the Commission should build upon the principles underlying successful previous Commission rulemakings and interpretive guidance that are premised on a "notice and access" and/or "access equals delivery" framework to update the current regulatory structure. The Associations feel obliged to supplement these recent submissions *only* to identify and address certain heightened challenges that often apply to Financial Services Firms, including many in the insurance industry due to the maturity of the insurance market. In this regard, above and beyond the elements of an updated framework that supports a digital consumer and business model proposed by these other industry participants, for the reasons set forth below, the Associations strongly urge the Commission to include the following additional e-delivery elements:

(i) Subject to certain conditions, Generic Documents (defined below) should be permitted to be delivered on a modified "access equals delivery" basis;
(ii) Only Personal Documents (defined below) should be required to delivered on a "notice and access" basis; and
(iii) Following a notice period, *all* investors should be transitioned to e-delivery, i.e., not having an e-mail address, smartphone number or other electronic address (collectively, "electronic contact") for existing investors should *not* be an impediment to transitioning such clients to e-delivery of Required Documents.

The Associations are confident that these additional standards would benefit *all* financial industry participants and investors.

I. The General SEC Regulatory Framework Governing the Electronic Delivery of Required Documents is Out-Dated, Confusing and does not meaningfully facilitate E-Delivery

The Associations commend the Commission's prescience in advancing electronic delivery of Required Documents when, starting in 1995, it established the basic framework governing the electronic delivery of Required Documents.[8] At that time, investor use of the Internet was still in its infancy and the heart of the Commission's requirements - notice, access and evidence of delivery - were appropriate given the technology and rate of Internet adoption at that time. As discussed below, however, the Associations submit that this framework is no longer workable and, due to a number of legal and technological developments, has ceased to facilitate e-delivery.

Since the SEC Releases, the Commission has responded to electronic delivery advancements via several ad hoc rulemakings, as highlighted below. While the Associations applaud these advancements and believe these rulemakings do, indeed, aptly facilitate e-delivery, most Required Documents are out of scope of these rulemakings and continue to be subject to the unworkable SEC Releases. These rulemakings, which the Associations believe should serve as the basis for an updated *comprehensive* e-delivery framework, include the following:

- In 2005, the Commission adopted amendments to permit final prospectuses filed on EDGAR to satisfy prospectus delivery requirements. In particular, under Rule 172 under

[8] *See the 1995 Release*.

the Securities Act of 1933, as amended ("***Securities Act***"), certain issuers and brokers and dealers are permitted to satisfy final prospectus delivery obligations if a final prospectus is filed with the SEC within the time required and other conditions are satisfied. The rule provides that a final prospectus will be deemed to precede or accompany a security for sale for purposes of Section 5(b)(2) of the Securities Act as long as the final prospectus is filed with the Commission or it will be filed as part of the registration statement.

  - This pure access equals delivery model means prospectus delivery is deemed effective without the "traditional" notice and evidence of delivery (e.g., consent).

- In 2007, the Commission adopted amendments to the proxy rules to permit issuers and market intermediaries to post proxy materials online instead of mailing them as long as they provided notice to shareholders of their ability to access these materials and provided them with a means to elect to continue to receive them via paper delivery.[9]

  - This notice and access model means that proxy material delivery is deemed effective without the traditional evidence of delivery (e.g., consent).

In doing so, the Commission wrote at the time:

> [W]e believe that current levels of access to the Internet merit adoption of the notice and access model as an alternative to the existing proxy distribution system. In this regard, we note that more than 10.7 million beneficial shareholders already have given their affirmative consent to electronic delivery of proxy materials and approximately 87.8% of shares voted were voted electronically or telephonically during the 2006 proxy season. Moreover, research submitted to us during the comment period indicates that approximately 80% of investors in the United States have access to the Internet in their homes, a greater percentage than we estimated at the proposing stage.[10]

- In 2018, the Commission adopted Rule 30e-3 under the Company Act, which permits mutual fund annual and semiannual shareholder reports to be delivered digitally, by default, subject to a transition period and specified investor protections.[11] Rule 30e-3 implements a "notice and access" regime for these reports and requires, among other things, a paper notice containing certain designated information be sent to fund shareholders within 70 days after the close of the period for which the report is made. The Commission noted that it would consider applying a similar framework to other types of Required Documents in the future.

  - This notice and access model means that shareholder report delivery is deemed effective without the traditional evidence of delivery (e.g., consent).

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[9] *See* Rule 20a-1 under the Investment Company Act of 1940, as amended ("***Company Act***") and Rule 14a-16 under the Exchange Act of 1934, as amended.
[10] Internet Availability of Proxy Materials, Rel. No. 34-55146 (Jan. 22, 2007).
[11] *See Optional Internet Availability of Investment Company Shareholder Reports,* Rel. No. 33-10506 (Jun. 5, 2018).

- In 2020, the Commission adopted Rule 498A which included the option, subject to certain conditions including notice, for insurers to deliver prospectuses for insurance dedicated funds underlying registered variable contracts by posting them on-line.[12]

  - This notice and access model means that variable contracts' underlying fund prospectus delivery is deemed effective without the traditional evidence of delivery (e.g., consent).

- In August 2020, the Commission proposed to modernize mutual fund shareholder reporting and prospectus delivery obligations. Following the initial sale of the security, subject to certain conditions, the delivery of current (annual) versions of the fund's summary and statutory prospectus would be effected by making such materials available online. In addition, the funds would send shareholders new streamlined shareholder reports that include information about the on-line availability of fund prospectuses, as well as notices of any material changes.

  - This "modified" notice and access model means that retail mutual fund prospectus delivery for existing shareholders (i.e., annual updates) is deemed effective without a traditional notice and/or evidence of delivery (e.g., consent). The notice is not traditional because is not temporal – it occurs at a different time than the on-line posting of the fund prospectuses.

Notably, with respect to each of these rulemakings, electronic delivery is the default yet *no* electronic contact information is required. Unfortunately, every other Required Document continues to be subject to the more burdensome conditions set forth in the SEC Releases.

As briefly mentioned above, the SEC Releases include three critical components for utilizing e-delivery: notice (whether it be the document itself or a separate notice that the document is available); access (via a mode that is comparable in accessibility to the postal system); and evidence of delivery (*i.e*., there is reason to believe the investor has received the information). This last requirement, both on its own and combined with the challenges and distinct requirements of E-SIGN, has resulted in many Financial Services Firms primarily "evidencing" delivery by sending the investor an electronic message and asking the investor to respond via the same electronic means (thereby "evidencing" the ability of the Financial Services Firm effectively to deliver Required Documents electronically). This only potentially works, of course, when (i) the firm has an electronic contact, and (ii) the investor responds in-kind.

However, many Financial Services Firms (including insurance companies) cannot even commence this "consent" process, as they do not, in fact, have electronic contact information for investors; indeed, our insurance company members do not have electronic contact information for the overwhelming majority -- millions -- of their investors. Many of these investors bought their securities, which are predominantly designed to be long-term investment contracts, in time periods when e-mail addresses were either not commonplace and/or were not or could not be routinely obtained through the initial application process; without question, smartphones did not

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[12] *See* Updated *Disclosure Requirements and Summary Prospectus for Variable Annuity and Variable Life Insurance Contracts*," Rel. No. 33-10765 (Mar. 11, 2020).

exist when many of these securities were purchased. Moreover, obtaining electronic contacts for legacy investors has proven to be extremely difficult. Accordingly, a future framework that would make electronic contact information fundamental to effecting e-delivery for a majority of Required Documents wholly overlooks this pervasive challenge faced by many Financial Services Firms and would leave these firms and their investors standing in the same place they are standing today: effectively, firms would have to have to continue to paper deliver most Required Documents -- even certain Generic Documents (as defined below) that are publicly available, and such investors would continue to Required Documents in paper- despite the unquestionable benefits of e-delivery and widespread investor preferences for the same. The Associations respectfully submit that any new framework should, at a minimum, address the *current* obstacles and challenges facing industry participants in facilitating e-delivery, including this one.

II. <u>Proposed Electronic Delivery Framework</u>

The Associations believe that the benefits of electronic delivery combined with the Commission's own recognition that "notice and access" and "access equals delivery" disclosure regimes for certain Required Documents are appropriate, strongly support an overhaul of the Commission's current regulatory framework governing the electronic delivery of *all* Required Documents. At the same time, we believe that updated electronic delivery standards, like the various SEC ad hoc e-delivery rulemakings to-date, can successfully incorporate appropriate investor protections. To that end, our proposal includes certain investor protection principles that we believe assure investors will receive appropriate information and protection. Indeed, we have derived these principles from current Commission regulations that incorporate "notice and access" and "access equals delivery" concepts.

A. Change in Default

Consistent with the requests made by the Industry Letters,[13] the Associations believe the Commission should change the default for delivering all Required Documents from paper to electronic delivery.[14] In the digital world in which we now live, the disadvantages of paper delivery are too great[15] and the advantages of electronic delivery are too multi-faceted for paper to continue to serve as the default delivery mechanism. The Associations also believe that this change in delivery default should apply both to new and current investors.

B. Mechanics

To effectuate a change in the default method of delivering Required Documents electronically, the Associations recommend that the Commission adopt the processes set out below.

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[13] *See, e.g.*, the SIFMA Paper.

[14] "Electronic" delivery includes either delivery via a notice sent to the investor's electronic contact with a password protected link or on-line posting to a publicly available website. The ultimate delivery mechanism would depend on the document type, as discussed below.

[15] *See e.g.*, Staff Statement Regarding Temporary International Mail Service Suspensions to Certain Jurisdictions Related to the COVID-19 Pandemic, at https://www.sec.gov/tm/temporary-international-mail-service-suspension for a discussion of the shortcomings of mail delivery in the current health crises.

1. Initial Notice/Transition Notices – New & Existing Investors

New investors. Following the effective date of the new e-delivery regulatory regime, new investors would be informed in writing during the initial application process as to how they will receive Required Documents **(*"Initial Notice"*)**. They would have the opportunity to opt out of electronic delivery of Personal Documents (defined below) starting from the point of sale (or at any time in the future). The Initial Notice would set forth certain specified information, including how to request a paper copy of any Required Document free of charge; how to opt out in the future; and the effect of not providing electronic contact information.

Existing investors. In order to pivot from default paper to default electronic delivery of Required Documents for exiting investors, Financial Services Firms would send notices (via paper to those existing investors who today receive documents in paper and electronically to those investors who today receive documents electronically) ("***Transition Notices***") informing them that delivery mechanism for sending Required Documents will shift from paper to electronic delivery.[16] Among other things, the Transition Notices would clearly disclose to investors that at the end of a transition period of one year ("***Transition Period***"), the documents specified in the Transition Notices will be delivered electronically in accordance with the procedures we enumerate below. The Transition Notices would alert investors to their significance,[17] be written in plain English, and explain how Required Documents will be delivered following the Transition Period. They would also inform existing investors that they can elect to opt-out of electronic delivery of Personal Documents, as defined below, at any time before or after the Transition Period and explain how they can do so. Like the Initial Notice for new investors, the Transition Notices would include information such as information about how to request a paper copy of any Required Document free of charge; how to opt out in the future; and the effect of not providing electronic contact information. After the Transition Period, investors who are not already enrolled in electronic delivery would receive an annual notice reminding them of the URL address of the website where Generic Documents, as defined below, will be electronically posted and maintained, as well as a posting schedule, as applicable. They will also be reminded that they will be sent a notice each time any Personal Document, as defined below, is available. The notice will also remind them that they can opt out of electronic delivery of Personal Documents at any time. In addition, investors who wish to receive a personal electronic notice for *all* Required Documents can always elect to do so.

Consistent with the Commission's delivery framework under certain of its current rules (*e.g.,* Rule 172) investors would not have the option permanently to opt out of electronic delivery of any Generic Documents, as defined below.

2. Delivery of Generic Documents – New & Existing Investors

Investors who have already opted in to e-delivery will not be affected and will continue to receive electronic notices at their electronic address without change under the new framework.

[16] If the Transition Notice communication to any investor who has supplied electronic contact information results in an undeliverable message, the investor will instead be notified by mail.
[17] For example, the Notice can contain prominent language alerting the recipient that this is an important document to be read immediately.

Consistent with the frameworks established by the Commission in Rule 172 (with respect to certain prospectuses), rules related to the internet availability of proxy materials, Rule 498A (with respect to the underlying insurance dedicated funds) and Rule 30e-3 (with respect to shareholder reports), and the framework the Commission has proposed under Rule 498B (specifically with respect to mutual fund prospectuses), each as discussed above,[18] the Associations believe that all Required Documents that are publicly available, do not relate to any particular investor and do not contain any personally identifiable information, such as prospectuses (including any amendments and supplements thereto) and fund annual reports (collectively "***Generic Documents***"), should be treated as delivered under a modified "access equals delivery" framework – that is, if such documents are filed with the SEC and the other conditions described immediately below are met.

Specifically, in order for electronic delivery of Generic Documents to be effective, certain notice and website posting requirements would apply, as follows:

- An annual notice would be required to be sent to each investor
- The annual notice would be sent to the investor via the electronic contact information, or, alternatively, the mailing address on file. If any electronic communication to any investor's electronic contact results in an undeliverable message, the investor instead will be notified by mail.
- The notice would contain the URL address of the website where Generic Documents will be electronically posted and maintained (the "***Website***") as well as a posting schedule, as applicable.
- Such notice would be required to contain information about how the investor can request a paper copy of the Generic Document at any time free of charge.
- While investors could request a paper copy of a Generic Document at any time, they would not be able permanently to opt out of electronic delivery of Generic Documents. The Generic Documents would be posted on the noted Website.

Like documents delivered under Rule 172, the rules related to the internet availability of proxy materials, Rule 498A and Rule 30e-3, investors will be able to instantly access, download, print, search and store such documents from any electronic device with access to the Internet. In addition, no investor electronic contact information should be required with regard to the electronic delivery of Generic Documents.

As noted above, the Commission has already established "access equals delivery" and "notice and access" delivery frameworks for certain types of Generic Documents. The Associations believe it is appropriate to extend these frameworks to all Generic Documents. These delivery frameworks effectively replace the need for evidence of delivery (i.e., consent) with the ability for investors to opt-out and/or receive paper upon request. Additionally, neither Rule 172, Rule 30e-3, Rule 498A nor proposed Rule 498B require that an investor's electronic contact information be obtained in order to effect compliant electronic delivery. Each of these rules does require some form of notice, but both paper and electronic notices are permitted. The logic of the Commission's statements when it adopted Rules 172, Rule 30e-3, 498A and 30e-3

[18] *See* discussion on pages 4-5, supra.

applies to all Generic Documents, not just those that are subject to those rules; accordingly, any updated framework should extend this treatment universally to all Generic Documents.

3. Delivery of Personal Documents

The Associations recommend the Commission take a somewhat different approach with respect to Required Documents that relate to a particular investor and contain personally identifiable information, such as account statements and confirmations (collectively "***Personal Documents***"). Importantly, the Associations believe that somewhat differing approaches are appropriate for delivering Personal Documents to new investors *or* existing investors for whom electronic contact information is on file but who have not elected e-delivery *versus* delivering Personal Documents to existing investors for whom no electronic contact information is on file – however, with the result being the same: all investors would be defaulted into e-delivery absent an opt-out.[19] Most significantly, as with Generic Documents, e-delivery of Personal Documents should be permitted even if a Financial Services Firm lacks an investor's electronic contact information as set out below.

a. New Investors & Existing Investors for Whom Electronic Contact Information is on File But Who Have not Elected E-delivery

New Investors. Going forward from the effective date of a new e-delivery regulatory regime, new investors would be notified in writing during the application process that all Personal Documents will be delivered via an electronic notice with a password protected link. An investor would be permitted to "opt out" of electronic delivery of Personal Documents at the point-of-sale, but such an investor can opt in at any time in the future by contacting the insurer.

Existing Investors. Existing investors who have already opted in to e-delivery will not be affected and will continue to receive electronic notices at their electronic address without change under the new framework. Existing investors who have not elected e-delivery but who have provided electronic contact information would be transitioned to e-delivery of Personal Documents following delivery of the Transition Notice as described above, and they would be permitted to opt out during the Transition Period. Going forward, like new investors, if such existing investors do not opt out, all Personal Documents would be delivered to them via an electronic notice with a password protected link.[20]

For existing investors in this category, as well as new investors who have not opted out of electronic delivery, Financial Services Firms would send an electronic notice each and every time a Personal Document is available to the electronic contact address that has been

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[19] Investors who previously consented to e-delivery for some or all of their Required Documents will continue to receive Personal Documents per their prior e-delivery election.

[20] If any communication to an investor who has supplied electronic contact information results in an undeliverable message, that investor would receive mailed annual notices going forward.

provided by the investor. These electronic notices would contain the URL address of the Website where the Personal Document will be electronically posted and maintained. Because the information provided in the document will contain personally identifiable information, the Website will require the investor to provide a unique username and password to gain access to the Personal Document. Financial Services Firms often include additional security protections, such as dual authentication, that provide a higher level of security.

Where an investor has never before accessed the Website, the investor can be directed to a unique and secure log-in screen, prompted to provide information verifying the investor's identity,[21] and asked to provide a unique username and password to access the Personal Documents. Once an investor's username and password are created, an investor will be able to access the Personal Documents.

Each notice would also contain information regarding how to obtain a paper copy of the Personal Document, as well as how to permanently opt out of e-delivery of Personal Documents.

b. Existing Investors for Whom No Electronic Contract Information is On File

While the Associations agree with the approach outlined in the Industry Letters as it would apply to delivery of Personal Documents to new investors and existing investors for whom electronic contact information has been obtained, as outlined immediately above, the Associations' members have substantial experience with existing investors for whom there is no electronic contact information on file. As previously noted, because insurance contracts are long-term investment vehicles, Association members continue to administer millions of contracts that were issued many years ago and for which they do not have electronic contact information of the contract owners.

The Associations therefore request that the Commission adopt the following permissive approach for Financial Services Firms that do not have an electronic address for existing investors. Following delivery of the Transition Notice described above, if an investor with no electronic contact information on file does not provide an electronic address, he or she would begin receiving Personal Documents, as follows:

- The Financial Services Firm would post the Personal Documents to an online personal account at a designated Website address.
- A paper notice would be mailed to the investor each time a Personal Document is posted.
- The paper notice would contain the URL address of the Website where the Personal Document would be maintained.

[21] Other means of verifying the investor's identity and enabling the investor to provide a unique username and password to access the Personal Documents can also be made available, including, for example, a toll-free customer service number.

- The Website would require the investor to provide a unique user ID and password to gain access to the Personal Documents (as described above in the prior sub-section).
- The notice would contain information regarding how to obtain a paper copy of the Personal Document free of charge, as well as how to permanently opt out of e-delivery of Personal Documents. The notice would also contain information regarding how to receive personal electronic notices for all Required Documents, if preferable.

While this proposed framework is an expansion of the current regulatory framework, in terms of defaulting existing contract owners into e-delivery of Personal Documents, we note that it is similar to the regulatory scheme established by the Commission under Rule 172, rules related to internet availability of proxy materials, Rule 498A and Rule 30e-3, and proposed Rule 498B. These rules provide for a "notice and access" or modified "access equals delivery" or "access equals delivery" delivery process and none of them are dependent on a registrant having an electronic address of an investor. Like other frameworks already adopted or proposed by the Commission, this approach effectively replaces the need for consent with the ability for investors to opt-out and/or receive paper upon request.[22]

[22] To the extent the Commission believes that evidence of delivery (i.e., consent) should be required to deliver Personal Documents in the manner requested herein, the Associations submit that the following guidance from the Commission concerning implied consent is very instructive, even though the context of this guidance was not e-delivery of documents:

> "While most commenters agreed that informed consent is a component of the fiduciary duty, a few commenters objected to what they saw as subjectivity in the use of the term "informed" to describe a client's consent to a disclosed conflict. The fact that disclosure must be full and fair such that a client can provide informed consent does not require advisers to make an affirmative determination that a particular client understood the disclosure and that the client's consent to the conflict of interest was informed. Rather, disclosure should be designed to put a client in a position to be able to understand and provide informed consent to the conflict of interest. **A client's informed consent can be either explicit or, depending on the facts and circumstances, implicit**." *Commission Interpretation Regarding Standard of Conduct for Investment Advisers*, Advisers Act Release 5248 (the "***Fiduciary Interpretation***") at https://www.sec.gov/rules/interp/2019/ia-5248.pdf. (Emphasis added. Internal footnotes omitted).

In discussing informed consent, Footnote 24 of the Fiduciary Interpretation remarks that it is generally considered on an objective basis "**and may be inferred**." (Emphasis added). Similarly, footnote 68 of the Fiduciary Interpretation states that "**the client could implicitly consent by entering into or continuing the investment advisory relationship with the adviser**." (Emphasis added).

The Associations believe these statements by the Commission in the Fiduciary Interpretation issued last year are relevant and significant with respect to what standards should apply to the electronic delivery of Personal Documents. The above statements in the Fiduciary Interpretation relate to an investment adviser's obligation to provide full and fair disclosure of its conflicts of interest to its clients so that the clients can provide informed consent to such conflicts. While the statements do not relate to the electronic delivery of disclosure documents, if consent can be implied from clients continuing their relationship with investment advisers in the context of a fiduciary relationship requiring full and fair disclosure **and** informed consent, then, *a fortiori,* consent reasonably can be implied by investors deciding not to opt out of electronic delivery when they receive the information in the notices described above. The Associations submit that the Fiduciary Interpretation establishes the standard under which Financial Services Firms can infer consent from investors. If the standards in that interpretation are satisfied, then investor consent can be inferred. Put succinctly, the Associations believe the standards for the electronic delivery of Personal Documents logically should be no higher than the standards applicable to fiduciaries under the Advisers Act.

III. E-SIGN

Under the Electronic Signatures in Global and National Commerce Act ("E-SIGN"), "if a statute, regulation, or other rule of law requires that information relating to a transaction or transactions in or affecting interstate or foreign commerce be provided or made available to a consumer *in writing*," (emphasis added) then it requires that: (1) a consumer affirmatively consents to the use of electronic records and has not withdrawn such consent; and (2) the consumer consents electronically, or confirmed his or her consent electronically, in a manner that reasonably demonstrates that the consumer can access information in the electronic form that will be used to provide the information that is the subject of the consent.

Our members continue to struggle with whether the consent requirements under E-SIGN apply to the delivery of Required Documents and so they continue to adhere to requirements derived from both E-SIGN and the SEC Releases. This is largely due to the fact that certain Commission rules continue to have an "in writing" requirement, and Financial Services Firms typically follow E-SIGN's process for obtaining consent (which, as noted, requires that consent be obtained electronically or confirmed electronically in the manner that will used to delivery documents). Not surprisingly, some of the Industry Letters have noted that many investors continue to receive paper copies of Required Documents due to the cumbersome process of consenting to electronic delivery. In addition, the additive requirements of E-SIGN continue to confuse and confound investors who incorrectly believe that they already have adequately consented to electronic delivery when they provide consent in person, orally over the telephone or on a paper application.

As a result, the Associations believe it is essential for the Commission to (i) amend its rules to eliminate any "in writing" requirements or (ii) explicitly and clearly exempt its rules governing the delivery of Required Documents from E-SIGN. This would enable Financial Services Firms to comply with the standards set by the Commission without having to worry about whether such compliance will result in violations of E-SIGN. As other industry participants have noted in the recent Industry Letters, such action would not be unprecedented and would also align with the actions of other federal regulators and federal programs that now facilitate greater use of electronic delivery, including, for example, when the Department of Labor recently used its exemption authority under E-SIGN to allow employers to post retirement plan disclosures online or deliver them to workers by email as a default.[23]

IV. Conclusion

Financial Services Firms have increasingly been permitted to use new technologies to communicate with investors and deliver Required Documents. These technologies create a positive experience for investors and lead investors to make better informed decisions. However, the Commission's current regulatory framework for electronic delivery of documents is fragmented and does not reflect how investors wish to receive information. Indeed, because the current framework was adopted well before the near ubiquitous access to electronic information that investors now enjoy, it does not go far enough to facilitate e-delivery, and it has

[23] *See, e.g., Default Electronic Disclosure by Employee Pension Benefit Plans Under ERISA*, 85 FR 31884 (July 2020), p.9, at https://www.dol.gov/agencies/ebsa/laws-and-regulations/laws/erisa/new-electronic-disclosure-rule.

hindered the adoption of new delivery methods that are beneficial to investors. The Associations believe it is appropriate to revise the model for delivering documents electronically under the federal securities laws, and the cornerstone of such a new model should be default electronic delivery for all Required Documents and all investors. It is unquestionably the fastest, safest, and most effective form of document delivery.

Given the unrelenting pace of technology, the Associations appreciate that any action taken by the Commission will require updates with the passage of time; however, we are hopeful that, at a minimum, any present action at least addresses the *current* obstacles and challenges facing industry participants in facilitating e-delivery. To that end, the Associations' proposal is a significant modernization of the Commission's existing interpretive guidance that comprehensively addresses the realities of the current marketplace. At the same time, however, the proposed framework builds upon and is consistent with existing Commission rules and interpretations that have recently been adopted, and includes and serves both existing and new investors. Accordingly, the Associations believe that its proposed use of "notice and access" and "access equals delivery" principles are appropriate, consistent with relevant precedent and with the interests of investors.

The Associations would be happy to discuss how the proposed framework can be implemented and to answer any questions.

Respectfully submitted,

AMERICAN COUNCIL OF LIFE INSURERS

Peter C. Reeder

Patrick Reeder
Vice President & Deputy General Counsel

COMMITTEE OF ANUITY INSURERS
For the Committee of Annuity Insurers, By:

Eversheds Sutherland (US) LLP

Eversheds Sutherland (US) LLP
steveroth@eversheds-sutherland.com
dodiekent@eversheds-sutherland.com
michaelkoffler@eversheds-sutherland.com

INSURED RETIREMENT INSTITUTE

Jason Berkowitz
Chief Legal & Regulatory Affairs Officer

cc: The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner
The Honorable Allison Herren Lee, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
Ms. Dalia Blass, Director, Division of Investment Management
Mr. William Hinman, Director, Division of Corporation Finance
Mr. Brett Redfearn, Director, Division of Trading and Markets