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March 1, 2019

Ms. Diana Foley  
Nevada Secretary of State's Office  
Securities Division  
2250 Las Vegas Boulevard North  
Suite 400  
North Las Vegas, Nevada 89030

RE: Request for Comment on Draft Regulations pertaining to Nevada  
Revised Statutes 90.575, 628.010 and 628.020

Dear Ms. Foley:

The Alternative and Direct Investment Securities Association ("ADISA"), on behalf of its members, appreciates the opportunity to comment on the draft fiduciary regulations referenced above ("Proposed Regulations"). ADISA is the nation's largest trade association for the non-traded alternative investment space, and in Nevada represents about 50 financial professionals in companies who primarily work for and operate locally-owned, state-wide businesses--not to mention their hundreds of Nevada investor clients plus our thousands of members nation-wide who do business reaching into Nevada. Several from the Division's office have attended and observed our educational events in the past, including at our annual convention held in Las Vegas every fall since our inception in 2014. Suffice it to say, our interests in Nevada and in the Division's actions are vital and sincere (please note, we have also submitted under separate cover a petition from several dozen ADISA members from Nevada as well as doing business in Nevada).

The Proposed Regulations are intended to implement the Nevada legislature's 2017 decision to revise the definition of "financial planner" to remove the then-current exclusions for broker-dealers, sales representatives and investment advisers. Since, under Nevada law, financial planners are subject to a fiduciary standard, the effect of Senate Bill 383 is to similarly place the actions of broker-dealers, sales representatives and investment advisers to that same standard. We understand Nevada's desire to ensure that its residents are adequately protected from inappropriate, self-serving conduct carried out by financial professionals operating in the State, and we believe that the Proposed Regulations provide a basis for ensuring that financial professionals, including those such persons who are subject to broker-dealer regulation at the State and Federal level, can serve clients in Nevada without having to make wholesale changes to their business model (or withdraw from doing business in the State as broker-dealers), and at the same time not compromise the interests of such residents.

1. Availability of Episodic Fiduciary Duty Exemption:

We want to focus your attention on the so-called “Episodic Fiduciary Duty Exemption” contained in Section 2 of the Proposed Regulations. We are encouraged by your recognition, inherent in this concept, that investment products may be offered to and purchased by investors without any expectation that the broker-dealer or sales representative is providing on-going advice of the kind that clients associate with an “investment adviser” or other financial professional that has an on-going duty to its clients (i.e., one that extends beyond the product or strategy in question). The Proposed Regulations appropriately, in our view, allow a broker-dealer (even one that is subject to a fiduciary duty imposed by Section 1), to receive transaction-based commissions so long as it is “in the client's best interest to be charged by transaction as opposed to other types of fees,” and the commission is “reasonable.”

We wish to note, however, that several proposed limitations on the availability of the Episodic Fiduciary Duty Exemption (the “Exemption”), all but remove the ability for clients to benefit from products or services where there is no on-going advice nor the expectation of on-going advice or an on-going duty by requiring most if not all broker-dealers (and their representatives) - even when they have otherwise acted in a manner that would seem to comport with the “episodic” duty approach set forth in Section 2 - to comply with the full panoply of requirements applicable to firms and persons who have a full (and on-going) fiduciary duty under the Proposed Regulations. As we see it, the leeway permitted a broker-dealer under Section 2 to charge a client on a commission basis for a single or infrequent securities transaction, which is the case for many alternative investment product offerings, will conflict with the general duties proposed to be imposed on those who owe their clients an on-going fiduciary duty. In particular, we see the potential for conflict arising between the parameters of the Exemption as applied to a single commission-based transaction, on the one hand, where the emphasis in the Proposed Regulations is on the appropriateness of charging a client a commission “as opposed to other types of fees,” and the duty, imposed on all fiduciaries under the Proposed Regulations, to recommend only those securities or investment strategies that are “in the client's best interest,” and the duty to avoid placing the firm’s, the representative’s or another client’s interest ahead of the client’s interests.

Without conceding that this potential conflict exists in every instance where a commission is charged, our experience is that the more traditional (i.e., “on-going”), fiduciary standard presumes that asset-based fees that do not vary by transaction as viewed as more in line with fiduciary concepts, as there is little to no opportunity for a variation in compensation to accompany a particular recommendation or selection in the asset-based fee approach. Leaving open the ability for a broker-dealer to conclude that a commission-based approach is the best one for a client in the context of a particular security, product or strategy “as opposed to other types of fees” is an important and, we submit, necessary aspect of any model for the regulation of financial services. Certain products are designed to have durations over several years, and therefore are less liquid investments (in the short term); in other words, some investment ideas are by their nature entered into only episodically and with a long term investment horizon. Indeed, characteristics of alternative securities specifically include:

- A diversity of non-traded and non-marketable investment products;



- The non-regular basis of most transaction or product recommendations; and
- The somewhat atypical relationship between buyers of these products and their financial professionals, which is understood to be infrequent in nature and not on-going.

Allowing the broker-dealer's duties to effectively reflect these facts (in part by allowing the firm to receive a one-time or periodic commission), aligns the interest and, importantly, the expectations and understanding, of the broker-dealer and its representative with that of its client. Such alignment is the essence of a financial professional being a fiduciary with regard to its clients.

Accordingly, we believe that the Exemption should be tailored to ensure that broker-dealers and their representatives that recommend transactions on an infrequent basis are fully eligible for the Exemption and can align their conduct – and their fees – fully with all aspects of the Proposed Regulations.<sup>1</sup> An Episodic Fiduciary is not freed from all aspects of the concepts that are associated with fiduciary status – rather the approach would recognize the more limited nature of the duties owed to clients (and expected from clients), in the episodic context. For that reason, we agree that the availability of the Exemption should be expressly conditioned on the broker-dealer (or its representative) not using one of the titles that the Regulation identifies as inconsistent with the notion of a non-ongoing advisory or planning relationship.

## 2. The SEC's Regulation Best Interest Proposal:

Published reports suggest that the SEC is close to finalizing its own Regulation Best Interest standard ("Reg BI"). Reg BI would, as proposed, establish a uniform "best interest" standard for broker-dealers. We believe a national standard, if adopted, would provide enhanced investor protection and be easier to administer than a series of individual state laws and regulations, and for that reason we have submitted a comment letter to the SEC that is generally supportive of the agency's proposed approach. While the SEC's standard has been attacked in some quarters for ostensibly seeking to permit broker-dealers to engage in so-called "conflicted" behavior with regard to their clients, we do not believe that Reg BI as proposed leaves room for the type of broker-dealer conduct that, others have asserted, will operate solely in the broker-dealers' interest and contrary to the best interests of their clients.

Furthermore, we wish to point out one important aspect of proposed Reg BI as proposed that we believe is relevant to the State of Nevada's consideration of its own regulations applicable to broker-dealers and their representatives.<sup>2</sup> Specifically, one essential element of the SEC's Reg BI standard are the twin requirements that broker-dealers act with appropriate care and diligence, and in a manner that does not place their interests before that of their clients. Here, by contrast, the Proposed Regulations include a prohibition against a broker-dealer not placing its interest (or that of another client), ahead of the client's own, but also would treat as a

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<sup>1</sup> Both FINRA's suitability rule and the Securities and Exchange Commission's Regulation Best Interest standard (discussed below), limit the duration of the suitability or best interest obligation to that point in time when the recommendation is made.

<sup>2</sup> We note in passing that many commenters assert that the Proposed Regulations raise pre-emption concerns. As seen by these groups, both the law and the Proposed Regulations go beyond the State's legal authority.

breach any recommendation, etc., that was not in the client's best interest. There is a significant possibility that these two duties would in effect set two different standards for broker-dealers and would therefore cause significant problems for firms looking to do business with residents of the State.

As a result, we believe that Nevada should excise the provision from its Proposed Regulations that makes it's a breach of a broker-dealer's fiduciary duty to act other than solely in the client's best interest. Alternatively, with the understanding that the SEC may make changes to Reg BI as adopted, we suggest that Nevada make it clear in its final regulations that any broker-dealer operating in the State and subject to a fiduciary duty would be deemed to be compliant with that duty if and to the extent that the broker-dealer and its representative complied with the terms of Reg BI, as adopted.

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Thank you again for the opportunity to provide our thoughts on the Proposed Regulations. We look forward to working with the Division to create workable rules that protect and serve the interests of Nevada investors while encouraging the provision of high quality advice and investment recommendations to residents of the State.

Sincerely,



Greg Mausz  
President

cc: Drafting Committee—John Grady, Tom Rosenfield, Larry Sullivan, Catherine Bowman