August 22, 2016

Via E-Mail to: FederalRegisterComments@cfpb.gov

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Re: Arbitration Agreements
Docket No. CFPB-2016-0020; RIN No. 3170-AA51

Dear Ms. Jackson:

The Investment Adviser Association[1] appreciates the opportunity to comment on the rules proposed by the Consumer Financial Protection Bureau that would (1) prohibit providers of certain consumer financial products and services from contractually mandating pre-dispute arbitrations relating to class action lawsuits, and (2) require covered providers to submit arbitration records to the CFPB.[2] We comment only with respect to the scope of the proposal.

Summary of Position

In creating the CFPB, the Dodd-Frank Wall Street Reform and Consumer Protection Act[3] (Dodd-Frank Act) excluded registered investment advisers acting in an SEC-regulated capacity from its jurisdiction. Nonetheless, the CFPB asks whether the proposed rules should include a specific provision excluding investment advisers if they are subject to an SEC rule that is functionally equivalent.

A specific exclusion is not necessary, both because registered investment advisers are already generally excluded from the CFPB's jurisdiction to the extent such persons are acting in an SEC-regulated capacity and because Congress explicitly granted the SEC and CFPB separate and parallel authority to regulate mandatory pre-dispute arbitration agreements. As a result, there can be no doubt that Congress intended for the SEC to exclusively regulate such agreements in contracts between registered investment advisers and their clients, and it would be inappropriate for the CFPB to attempt to exercise its limited authority in this context. In other

[1] The IAA is a not-for-profit association that represents the interests of investment adviser firms registered with the U.S. Securities and Exchange Commission (SEC). The IAA's membership consists of approximately 600 firms that collectively manage nearly $20 trillion for a wide variety of clients that are individual and institutional investors, including pension plans, trusts, investment companies, private funds, endowments, foundations, and corporations. For more information, please visit www.investmentadviser.org.

[2] Arbitration Agreements, 12 CFR Part 1040, RIN 3170-AA51, 81 Fed. Reg. 32830 (May 24, 2016), *available at* https://www.gpo.gov/fdsys/pkg/FR-2016-05-24/pdf/2016-10961.pdf.

[3] Public Law 111–203, 124 Stat. 1376 (2010).

words, there is no need for an express exclusion in the rule because the CFPB does not have the requisite jurisdiction to extend the rule to advisers in the first place.[4]

The CFPB generally does not have the authority to regulate SEC-registered investment advisers acting in their "regulated capacity."

In enacting the Dodd-Frank Act, Congress deliberately defined the SEC's and CFPB's respective authority to avoid duplication or overlapping rules.[5] As noted in the proposal, Congress did not give the CFPB statutory enforcement authority over SEC-regulated investment advisers.[6] Congress accordingly limited the CFPB's rulemaking authority to "covered persons" who provide "consumer financial products or services" defined to cover a wide range of consumer-related topics, such as consumer lending, brokering real property leases, deposit-taking activities, and consumer credit reports. Notably, the definition also includes providing "financial advisory services" but ***explicitly excludes***:

> "services ***relating to securities*** provided by a ***person regulated by the [SEC]*** or a person regulated by a State securities Commission, but only to the extent that such person acts in a ***regulated capacity***…" (emphasis added).

Management agreements between investment advisers and their clients as well as the advisory services provided pursuant to those agreements are squarely within the universe of activity regulated by the SEC. Indeed, regulating the adviser/client relationship is a significant SEC mandate. Specifically, the principles-based fiduciary standards and anti-fraud provisions of the Investment Advisers Act of 1940 (Advisers Act) provide a strong framework that governs all aspects of this relationship.[7] And contractual agreements between investment advisers and their clients regarding management services are a critical component of the adviser/client relationship that is explicitly regulated by the Advisers Act.

In addition to authorizing the SEC to restrict mandatory pre-dispute arbitration agreements, Section 205 of the Advisers Act requires certain provisions to be included in management contracts. For example, the contract must include a provision that prohibits assignment without client consent and for the appropriate refund of any unearned prepaid fees

[4] The CFPB also seeks comment on the extent to which an investment adviser who is acting in an SEC-regulated capacity may also be providing a consumer financial product or service that would be subject to the proposed rules. However, we believe that this question is not relevant for purposes of this rulemaking because Congress intended to preclude the CFPB from regulating matters that fall within the SEC's jurisdiction, as discussed in this letter.

[5] See Congressional Record – House, Report on Resolution Providing for Consideration of Conference Report on H.R. 4173, Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), H5212, H5216 – 5217 (June 30, 2010), *available at* https://www.congress.gov/crec/2010/06/30/CREC-2010-06-30-pt1-PgH5212-3.pdf.

[6] See Dodd-Frank Act § 1027(i)(1) (providing that Dodd-Frank Act Title X provisions may not be construed as altering, amending, or affecting the authority of the SEC and that the Bureau has no authority to enforce Title X with respect to a person regulated by the SEC).

[7] In fact, registered investment advisers are subject to SEC examinations and enforcement actions where oversight of the adviser/client relationship is the primary focus.

upon termination. The Advisers Act also voids any condition, stipulation, or provision intended to bind a client to waive compliance with the law.

While the subject of mandatory arbitration provisions in advisory contracts was not specifically addressed in the Advisers Act prior to the Dodd-Frank Act, the SEC had clearly considered these types of clauses to be well within its jurisdiction.[8] Thus, we believe that agreements between investment advisers and their clients that are subject to the requirements of the Advisers Act are outside the CFPB's jurisdiction because they clearly are in connection with "services related to securities" by an SEC-regulated person "acting in a regulated capacity."

The SEC's explicit statutory authority to regulate mandatory pre-dispute arbitration agreements precludes the CFPB from extending the proposed rule to SEC-registered investment advisers.

Consistent with the overarching principle to avoid duplication or overlapping rules, Congress explicitly granted the CFPB and SEC separate authority to regulate mandatory pre-dispute arbitration agreements by enacting parallel provisions in the Dodd-Frank Act — Section 1028 for the CFPB and Section 921(b) for the SEC. Section 1028 directed the CFPB to study pre-dispute arbitration agreements in connection with consumer financial products or services and report back to Congress, both of which were done last year.[9] Section 1028 also authorized the issuance of rules restricting or prohibiting the use of arbitration agreements, consistent with the findings of the CFPB's study. We note that neither the proposal nor the study address the use of arbitration agreements by SEC-regulated persons, including registered investment advisers.[10]

Section 921(b) largely parallels Section 1028, although it does not require the SEC to conduct a study. It authorizes the SEC to "prohibit, or impose conditions or limitations on the use of, agreements that require customers or clients of any investment adviser to arbitrate any future dispute between them arising under the Federal securities laws, the rules and regulations thereunder, or the rules of a self-regulatory organization if it finds that such prohibition, imposition of conditions, or limitations are in the public interest and for the protection of investors." We note that while the SEC has not yet proposed rules regarding the use of mandatory arbitration agreements, it continues to gather comments in connection with this

[8] The SEC staff has previously stated that arbitration provisions in advisory contracts were incompatible with the Advisers Act. See McEldowney Financial Services, SEC Staff No-Action Letter (Oct. 17, 1986) (noting that the Advisers Act provides certain non-waivable rights of action, including "the right to choose the forum, whether arbitration or adjudication, in which to seek resolution of disputes." This position has been subject to litigation. See e.g. Bakas v. Ameriprise Financial Services, Inc., 651 F. Supp. 997 (D. MN 2009) (noting that the SEC position was based on a Supreme Court decision (Wilko v. Swan, 346 U.S. 427 (1953)), which had been overturned).

[9] See Bureau of Consumer Fin. Prot., Arbitration Study: Report to Congress, Pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act §1028(a) (2015), *available at* http://files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf.

[10] It is also not clear whether the CFPB's post-study outreach discussed in the proposal included SEC-regulated persons.

authority.[11] Moreover, as noted above, it is also an area in which the SEC has previously expressed its views.[12]

It is clear that the authority to regulate pre-dispute arbitration agreements between registered investment advisers and their clients falls squarely within the jurisdiction of the SEC, and that the CFPB must defer regulation in this area to the SEC. Accordingly, the CFPB should confirm in any adopting release that SEC-registered investment advisers are not subject to the proposed rules in the first instance, without the need of an explicit exclusion.

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We appreciate your consideration of our comments. Please do not hesitate to contact us me or Sanjay Lamba, IAA Assistant General Counsel, at (202) 293-4222 with any questions about our position.

Respectfully,

/s/

Robert C. Grohowski
General Counsel

[11] See https://www.sec.gov/spotlight/regreformcomments.shtml. Comments received are *available at* https://www.sec.gov/comments/df-title-ix/pre-dispute-arbitration/pre-dispute-arbitration.shtml.

[12] See *supra* note 8.