

MEMO# 35414

August 22, 2023

Complaint Challenges Two New Missouri Securities Division Rules

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TO: ESG Advisory Group RE: Complaint Challenges Two New Missouri Securities Division Rules

On August 10, 2023, the Securities Industry and Financial Markets Association filed a complaint in the US District Court Western District for the State of Missouri challenging two new Missouri Securities Division rules that would require specified financial professionals to obtain a client's written consent on state-scripted documents before providing advice that "incorporates a social objective or other nonfinancial objective."[\[1\]](#)

The rules make it a dishonest or unethical business practice in Missouri for broker-dealers, agents, investment advisers, and investment adviser representatives to fail to disclose to any client or prospective client if such financial professional "incorporates a social objective or other nonfinancial objective" into: (i) a discretionary investment decision to buy or sell a security or commodity for a client; (ii) advice or a recommendation and/or solicitation to client for the purchase or sale of a security or commodity; or (iii) the selection, or advice or a recommendation to a client regarding the selection, of a third-party manager or subadviser to manage the investments in the client's account.

The complaint asserts that the rules are preempted by the National Securities Markets Improvement Act of 1996 (NSMIA). Specifically, the complaint states that:

- Under NSMIA, the US Securities and Exchange Commission (SEC) was given exclusive authority to regulate the conduct of any investment adviser managing \$100 million or more in client assets, and states may not make any rules regulating the activities of these firms. Therefore, to the extent that the rules apply to federal covered investment advisers and investment adviser representatives, they are preempted by NSMIA;
- NSMIA preempts the rule as applicable to broker-dealers because it requires broker-dealers to make and keep records that differ from, or are in addition to, the records required by SEC rules; and
- NSMIA prevents states from imposing conditions on federally "covered securities" (which include most of the securities ordinary investors buy and sell, such as mutual funds) and, therefore, to the extent that the rules apply to covered securities under

NSMIA, they are preempted by NSMIA.

The complaint further asserts that the rules are preempted by the Employee Retirement Income Security Act of 1974 (ERISA), which broadly preempts states from regulating private and employer-sponsored pension and welfare plans. Therefore, the complaint states that, to the extent that the rules apply to pension accounts, they are preempted by ERISA.

The complaint additionally asserts that the rules violate the protection against compelled speech provided by the First Amendment of the United States Constitution. Specifically, the complaint alleges that the rules violate the First Amendment protection against compelled speech by requiring financial professionals to adopt and express the government's position, through the use of the state-scripted written consent, on a controversial matter subject to public debate that is not purely factual.

Finally, the complaint asserts that the rules are unconstitutionally vague. The complaint states that the rules fall far short of providing regulated persons with the ability to ascertain with certainty what strategies or securities include "social" or "nonfinancial objectives," and are therefore unconstitutionally vague.

The complaint seeks to have the rules: (i) declared invalid as preempted by NSMIA and ERISA; (ii) declared to constitute unconstitutional state compulsion of speech under the First Amendment; and (iii) declared to be void as impermissibly vague. It also seeks to permanently enjoin the Secretary of State of Missouri and the Missouri Securities Commissioner, who regulate the securities industry in Missouri, from implementing, applying, or taking any action whatsoever to enforce the rules.

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Notes

[1] The complaint in the matter of Securities Industry and Financial Markets Association vs. John R. Ashcroft and Douglas M. Jacoby, Civil Action NO. 2:23-cv-4154 (Aug. 10, 2023) can be viewed at

<https://www.sifma.org/wp-content/uploads/2023/08/SIFMA-Complaint-Filed-in-the-U.S.-District-Court-for-the-State-of-Missouri.pdf>.