

STATE OF MINNESOTA  
DEPARTMENT OF COMMERCE

In the Matter of the Proposed  
Rule Amendments for the Purpose  
of Requiring that Certain  
Disclosures be Made by Persons  
Who Engage in the Business of  
Financial Planning.

STATEMENT OF NEED  
AND REASONABLENESS

Statement of Authority

Minn. Stat. § 80A.25, subd. 1, gives the Commissioner of Commerce ("Commissioner") authority to "from time to time make, amend, and rescind such rules, forms and orders as are necessary to carry out the provisions of §§ 80A.01 to 80A.31...." Minn. Stat. § 82.28 gives the Commissioner the authority to "promulgate such rules and regulations as are reasonably necessary to carry out and make effective the provisions and purposes" of Chapter 82. Minn. Stat. § 60A.17, subd. 15, provides that the Commissioner "may adopt rules pursuant to Chapter 14 to further implement and administer the provisions of this section."

Additional rulemaking authority provided in Minn. Stat. § 45.023 authorizes the Commissioner to "adopt, amend, suspend, or repeal rules....whenever necessary or proper in discharging the Commissioner's official responsibilities."

The Commissioner finds the proposed amendments necessary and appropriate in the public interest and consistent with the purposes fairly intended by the policies and provisions of Chapters 45, 60A, 80A and 82.

### History

On October 15, 1984, the Commissioner published notice of his intent to solicit outside information at 9 S.R. 766 for the consideration in the promulgation of rules and amendments under Minnesota Statutes Chapters 60A, 80A and 82. After a review of comments solicited, the Commissioner published the proposed rules in the State Register on January 21, 1985.

### Facts Establishing Reasonableness

The proposed rules and amendments pertaining to financial planners relate to the Department of Commerce's regulation of securities broker-dealers and agents, investment advisers and investment adviser representatives, real estate brokers and salespersons and insurance companies and agents. As the areas of

securities, real estate and insurance are primarily financially-oriented industries, many persons working in these areas have marketed themselves as being "financial planners."

The proposed rules and amendments are intended to provide consumers with information concerning the background of persons representing themselves to be "financial planners," insofar as these persons are regulated by the Department in the insurance, real estate or securities areas. Because potential bias exists when a person who sells a specific product also offers counsel to others as to the advisability of purchasing that product and because a client's knowledge of that potential bias may affect his or her financial decisions, the Commissioner finds it necessary to require that a disclosure document containing specified information be provided.

Because three separate areas are being addressed by the proposals, i.e. securities, insurance and real estate, three separate but related sets of rule amendments are being recommended. Proposed Minnesota Rules, Part 2875.1051 addresses securities broker-dealers, agents, and investment advisers and investment adviser representatives who are engaged in the business of "financial planning;" proposed Part 2790.0550 addresses insurance companies and agents who represent themselves to be "financial planners;" and proposed amendments to Parts 2800.0100 and 2800.4600 affect real estate brokers and salespersons who engage in the business of "financial planning."

The first part of each set of rules (Part 2800.0100, Subpart 14; Part 2790.0550, Subpart 1; Part 2875.1051, Subpart 1) defines "business of financial planning" to mean "providing or offering to provide, financial planning services or financial counselling or

advice, on a group or individual basis." The definition further provides that persons who use specified designations shall be deemed to be representing themselves as being engaged in the business of financial planning. In addition to persons using the designations specified, persons using similar designations or titles shall be deemed to be representing themselves as being engaged in the business of financial planning. The latter broadly-defined inclusion is recommended because the term "financial planning" is used as a marketing term and marketing titles can vary depending upon what regulations are adopted.

The second part of each set of amendments (Part 2800.4600, Subpart 1; Part 2790.0550, Subpart 2; Part 2875.1051, Subpart 2) prohibits a person regulated by the Department from representing that he or she is engaged in the business of financial planning unless he or she provides a disclosure document to the client. As previously indicated, the disclosure document is intended to provide the prospective client with information pertaining to any potential conflict of interest or bias held by the person offering the financial planning services.

An example of the problem addressed by the disclosure document is the case where a senior citizen was solicited by a "financial planner." The "financial planner" charged a fee of \$1500 for the services. The senior paid it. After a review of the senior's finances, the "financial planner" recommended that the senior invest in life/annuity policies issued by an insurance company. The senior was never advised that the "financial planner" was licensed as an insurance agent, that the "financial planner" would receive substan-

tial commission on the sale, or that the "financial planner" had never advised people to buy stocks, bonds, real estate or other investments.

The first item required to be disclosed is how the person providing the financial planning services will be compensated. The Commissioner believes that it is important for the prospective client to be informed as to whether the person is compensated by a set fee or by commissions resulting from the sale of products he or she sells to the client. Accomodation has been made for cases in which a person is compensated by a variation or combination of fees and commissions. This disclosure is needed to inform the client of the potential influence that the manner of compensation may have on the financial advice given. The example above would be affected by this requirement, in that the senior would see the relationship between the planner's compensation and the sale of products.

Also required to be disclosed are the names of the firms which issue, trade, or distribute the services or products offered or sold by the financial planner. The Commissioner finds this disclosure necessary to inform the client of any affiliations the financial planner has which could affect the advice given to the client. The example of the senior citizen would be addressed by this disclosure, in that the senior would see the obvious interest of the planner in promoting products of the insurance companies he represented.

The third item to be disclosed are the licenses held by the person under Minnesota Statutes, Chapters 60A, 80A, or 82. These chapters govern the areas of insurance, securities, and real estate, respectively. This disclosure is intended to inform the client of

activities, other than financial planning, in which the person is engaged that may have an effect upon the financial advice given. Again, the example previously given would be affected by this requirement as the senior would be informed of the insurance agent license held by the "financial planner."

The final disclosure is that of the identity of products or services which the licenses previously specified authorize the person to offer or sell. The Commissioner finds this disclosure necessary to tell the client of the potential relationship between the advice being given and the sale of financial products. The example of the case involving the senior citizen would be affected by this disclosure, in that the senior would see the clear interest of the planner in selling insurance products.

The purpose of the rules in their entirety is to give the client sufficient information to enable him or her to make an informed decision. The rules merely require a truthful disclosure of facts relevant to the formation of a thoughtful financial decision.

#### SMALL BUSINESS CONSIDERATIONS

Minnesota Statutes § 14.115 requires that the impact of proposed rules on small business be considered in the development of those rules. Specifically, the statute, at subdivision 2, requires that less stringent compliance standards and reporting requirements for small businesses be considered. The statute also requires that

methods designed to reduce the impact of the rules on small businesses be incorporated into the rules if they are feasible and consistent with the statutory objectives associated with the rules.

The proposed rule amendments were unanimously endorsed by the members of a task force organized by the Department to discuss the area of "financial planning." The task force was composed of representatives from the securities, insurance, real estate and financial planning areas, many of whom are owners of small businesses. Members affiliated with small businesses included Don Bartho, Total Financial Planning, Inc.; David Pagel, First National Preferred Investment Corp.; Roger A. Hubley, Chartered Financial Services of Minnesota, Inc.; Robert Labat, R. D. LaBat & Associates, Inc.; and several attorneys whose clients include small businesses. Other task force members included Ann Drea Benson, Piper, Jaffray and Hopwood; Kevin Howe, IDS/American Express; and Richard Heise, Engler & Budd, Co.

Comments regarding the proposed rule amendments were solicited from small businesses not only through the State Register, but also through the Minnesota Association of Life Underwriters, Inc.'s newsletter and the Commerce Contact, a quarterly newsletter published by the department and sent to all brokerage firms, real estate agents, and insurance agents licensed in Minnesota. Additionally, articles about the task force and its purpose published in the metropolitan newspapers drew further comments and greater attendance at task force meetings from representatives of small businesses.

Many states, including Hawaii, Michigan and California, are introducing proposals which include a prohibition on the use of the term "financial planner" and/or an outright statement that conflicts of interest are held by the person offering the services.

In light of small business concerns, the rule amendments proposed by the Department are not as restrictive as those proposed in other states. In the event that these rules do not curtail existing problems, however, further rule amendments will be proposed.

Each of the methods described at Minnesota Statutes § 14.115, subdivision 2 (a) - (e) was considered in proposing the rule amendments. Provisions contained in the amendments are believed to be necessary to achieve legislative purposes.