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## Texas State Securities Board

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November 26, 2018

*Via electronic mail & inter-agency mail*

Jennifer Jones, Acting Director  
Sunset Advisory Commission  
P.O. Box 13066  
Austin, Texas 78711-3066

Dear Director Jones:

Thank you for the opportunity to comment on the Sunset Staff Report on the State Securities Board ("agency"). Your time and consideration during the review process, and in particular, the report's "draft" phase are very much appreciated. Lead Analyst Alan Leonard and Policy Analyst Taj Sheik's professionalism, diligence, and service to Texas are similarly respected and appreciated.

Brief comments for the Commission's consideration on the issues and recommendations in the Sunset Staff Report follow:

**Summary @ Pg. 1, 3<sup>rd</sup> Paragraph – "the loss of the staff's cultivated expertise to higher paying national regulators."**

By way of minor comment – the Sunset description is a factually accurate, historical characterization since our last Sunset review, however attrition in recent years has been more pronounced by agency employee migration to securities firms and industry compliance consulting firms.

**Recommendation 1-1 – Clarify statute to authorize the agency to provide prosecutorial assistance and require the agency to develop a process to determine staff resources available to support prosecutions.**

Sunset staff found "the agency continues to use its appropriated resources in a responsible manner that supports the prosecution of securities crimes while being mindful of its other statutory responsibilities."

The agency respectfully submits for the Commission's consideration whether the analysis of resource requirements to assist in securities-related criminal prosecutions need be accomplished through formal rulemaking concerning its internal processes and procedures. The agency automatically makes these assessments on all potential law enforcement matters that require a dedication of agency resources.

The agency believes it can formalize its internal policies and procedures in an outward-facing manner to better inform the public and stakeholders how the agency enforces the Securities Act without the need for formal rulemaking and provide the transparency that this recommendation contemplates.

The agency is unclear if the reporting requirement component of the recommendation would be through an addition to its existing key performance measure reporting requirements or through the agency's statutory reporting requirement, set forth in Section 2.J of the Securities Act. The agency supports the addition of the reporting requirement through either or both.

The agency appreciates Sunset staff's recognition of the agency's "nearly spotless conviction rate." The agency notes it routinely reports information related to its assistance to prosecuting offices in enforcing the Securities Act, as well as additional agency functions, to Governor Abbott's office. Information regarding prosecutorial assistance is also routinely reported to the Legislature, Comptroller, State Auditor's Office, the Speaker of the House, and Lieutenant Governor's Office in reports such as the agency's strategic plan and annual financial report.

The recommendation could be implemented well in advance of March 1, 2020, provided the Commission's final recommendation provides for the agency to implement the recommendation through publicly-available, internally-developed policies and procedures as opposed to formal rulemaking.

**Recommendation 1-2 – Authorize the agency to order refunds for violations of agency statute or rules.**

The agency supports the recommendation and respectfully requests clarification of the recommendation. The recommendation suggests refund (restitution) authority would apply with respect to negotiated orders resulting in enforcement actions. Report *Findings* addressing Issue 1-2 (Staff Report @ Pg. 10 – *No refund authority*) suggest restitution authority would extend to matters unable to reach a negotiated settlement that then result in a contested case proceeding. Clear restitution authority in both the negotiated and contested case contexts would enhance investor protections. In practice, the agency is already utilizing restitution made to investors as a mitigating circumstance in its negotiated settlements.

**Recommendation 1-3 – Remove the requirement that branch offices be registered.**

The agency is neutral with respect to the recommendation. The agency notes it will still receive branch office location information and information related to the designated supervisor for branch office activities under the recommendation.

**Recommendation 1-4 – Direct the agency to develop a penalty matrix.**

The agency supports transparency in administrative penalties and sanctions levied against registrants. However, the agency maintains certain reservations with implementing such a matrix in administering investor protections and ensuring competitive access to capital for legitimate business.

A penalty matrix could yield disparate penalties and sanctions for similar violations, such as an unnecessarily harsh sanction for a smaller registrant as compared to a larger registrant. A matrix could lead a firm to make business decisions on a cost-benefit analysis basis to determine the level of compliance the firm would otherwise undertake to comply with rules and regulations designed to protect investors. A matrix may also disincentivize a registrant from negotiated resolutions most beneficial to Texas investors.

Unlike some regulatory agencies, the Securities Board assesses penalties and sanctions against registrants in a highly-centralized manner and has not had instances of disparate treatment for substantially-similar registrant misconduct.

The agency requires proposed, negotiated resolutions of registrant violations be vetted with staff financial examiners and attorneys, division assistant directors, division directors, the deputy commissioner, and securities commissioner, with a documented assessment of previous agency orders of penalties and sanctions, aggravating factors, and mitigating circumstances made before the entry of a negotiated order. The agency notes previous sanctions and penalties are also well-known to securities law practitioners and play a central role in negotiated resolutions.

**Recommendation 1-5 – Direct the board to develop and adopt rules describing all phases of its complaint process.**

The agency respectfully submits for the Commission's consideration whether the development of information on its complaint processes need be accomplished through formal rulemaking rather than internal processes and procedures that would be provided publicly in a more robust and accessible way than current practice.

Based on discussions with Sunset staff during the review process, the agency also requests clarification to the proposed recommendation. The agency understands the recommendation to apply to complaints received against registrants pursuant to Section 2-6 of the Securities Act. The agency otherwise supports the recommendation.

**Recommendation 1-6 – Direct the agency to improve its tracking of complaint and case resolution timeframes.**

Based on discussions with Sunset staff during the review process, the agency requests clarification to the proposed recommendation. The agency understands the recommendation to apply to complaints received against registrants pursuant to Section 2-6 of the Securities Act. The agency otherwise supports the recommendation.

**Recommendation 1-7 – Direct the agency to review its risk-based inspection tool at least every four years.**

The agency supports the recommendation to review risk factors and other changes in the securities industry, but notes risk factors and industry changes are assessed under current practice.

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For example, with the implementation in September 2017 of Section 45 of the Securities Act requiring firm reporting of suspected vulnerable victim exploitation, the compliance examination program began ensuring that samples of firm client files for inspection included elderly client accounts, when applicable. Similarly, in early 2018, the examination program began assessing whether firms were entering the emerging cryptocurrency markets on behalf of their clients.

The agency will begin to formally document its ongoing risk assessments as a component of its mandated inspection cycle for the compliance examination program in advance of September 1, 2020, and will assess emerging risks and industry changes on at least a semi-annual basis.

**Recommendation 1-8 – Direct the agency to accept online submissions of applications and fees.**

The agency supports the spirit of the recommendation and will explore its implementation in as full of a manner as possible. The agency maintains implementation concerns with respect to cybersecurity threats, security in the processing of fees, and the security of registrants' personal identifying information through a new online means. Availability of resources required for implementation of adequate safeguards for new online submission and fee mechanisms present an additional concern for the agency.

**Recommendation 1-9 – Direct the agency to remove the notarization requirements on its forms.**

The agency supports the recommendation.

In closing, the agency appreciates Sunset staff's and the Commission's difficult work on behalf of the Securities Board's review process. The Securities Board's team has benefited considerably from the review process. Thank you for your efforts, time, and consideration.

With regards,



Travis J. Iles  
Securities Commissioner