

VIA ELECTRONIC MAIL

September 21, 2010

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549- 1090

RE: File Number SR-FINRA-2009-042 – Amendment No 1 to Proposed FINRA Rule 3270
(Outside Business Activities of Registered Persons)

Dear Ms. Murphy:

On June 8, 2009, the Financial Industry Regulatory Authority, Inc. (FINRA) filed with the Securities and Exchange Commission (SEC) a proposed rule change relating to the outside business activities (OBA) of registered persons.¹ FINRA proposed to adopt NASD Rule 3030 (Outside Business Activities of an Associated Person) as FINRA Rule 3270 (Outside Business Activities of Registered Persons) in the consolidated FINRA rulebook (Proposed Rule). The Proposed Rule would delete Incorporated NYSE Rule 346 (Limitations—Employment and Association with Members and Member Organizations) and its interpretations. The Proposed Rule was published for comment in the Federal Register on July 8, 2009.² The SEC received six comments on the Proposed Rule, including FSI's comment letter dated July 29, 2009.³ On July 30, 2010, FINRA responded to the six comment letters⁴ and filed Amendment No. 1 to the Proposed Rule (Proposed Amendment).⁵

Proposed Rule 3270 would require prior written notice to a firm whenever a registered representative will be an employee, independent contractor, sole proprietor, officer, director or partner of another person, or will be compensated, or have the reasonable expectation of compensation, from any other person as a result of any OBA.⁶ Supplementary Material .01 set forth obligations of a firm when it received written notice of a proposed OBA.⁷ As originally proposed, Supplementary Material .01 would have required the firm to determine if the activity raised "investor protection concerns." If the activity did raise "investor protection concerns," the firm was obligated to implement procedures or restrictions on the activity.⁸

¹ FINRA Proposed Rule Change to Adopt FINRA Rule 3270 (Outside Business Activities of Registered Persons) in the Consolidated FINRA Rulebook, available at

<http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p118899.pdf>

² Securities Exchange Act Release No. 60199 (June 30, 2009), 74 FR 32668 (July 8, 2009), available at

<http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p119176.pdf>

³ FSI's Comment letter in Response to FINRA Proposed Rule 3270 date July 29, 2009, available at

http://www.financialservices.org/uploadedFiles/FSI/Advocacy_Action_Center/FINRA_Issues/FSI%20Comment%20Letter%20on%20FINRA%20Outside%20Business%20Activity%20Proposal%2007-29-09.pdf

⁴ FINRA's Response to Comments dated July 30, 2010, available at

<http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p121834.pdf>

⁵ Amendment No 1 to Proposed FINRA Rule 3270, available at

<http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p121833.pdf>

⁶ Proposed FINRA Rule 3270

⁷ Proposed FINRA Rule 3270, Supplementary Material .01.

⁸ Proposed FINRA Rule 3270, Supplementary Material .01.

In response to the comments received by the SEC, FINRA is now proposing amendments to the Proposed Rule. Specifically, FINRA is proposing changes to clarify proposed Supplementary Material .01.

The Financial Services Institute (FSI)⁹ welcomes this opportunity to comment on the Proposed Amendments. We are encouraged that FINRA has responded to our July 29, 2009 comment letter by proposing amendments to the Proposed Rule. However, we believe that the Proposed Amendment is overly broad, ill defined, and fails to give firms the clarity that they need to be able to achieve compliance with the Proposed Amendment.

Background on FSI Members

FSI represents independent broker-dealers (IBD) and the independent financial advisors that affiliate with them. The IBD community has been an important and active part of the lives of American investors for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD firms also share a number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; primarily engage in the sale of packaged products, such as mutual funds and variable insurance products; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered investment adviser firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial advisors are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their financial goals and objectives.

In the U.S., approximately 201,000 financial advisors – or 64% percent of all practicing registered representatives – operate as self-employed independent contractors, rather than employees, of their affiliated broker-dealer firm.¹⁰ These financial advisors are self-employed independent contractors, rather than employees of the IBD firms. These financial advisors provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisors are typically “main street America” – it is, in fact, almost part of the “charter” of the independent channel. The core market of advisors affiliated with IBDs is clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisors are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other centers of influence.¹¹ Independent financial advisors get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisors have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisors. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is

⁹ The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has 123 Broker-Dealer member firms that have more than 188,000 affiliated registered representatives serving more than 15 million American households. FSI also has more than 14,500 Financial Advisor members.

¹⁰ Cerulli Associates at <http://www.cerulli.com/>.

¹¹ These “centers of influence” may include lawyers, accountants, human resources managers, or other trusted advisors.

committed to preserving the valuable role that IBDs and independent advisors play in helping Americans plan for and achieve their financial goals. FSI's mission is to ensure our members operate in a regulatory environment that is fair and balanced. FSI's advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

Comments on the Proposed Rule

As stated above, we believe that the Proposed Amendment is overly broad ill defined, and fails to give firms the clarity that they need to be able to achieve compliance with the Proposed Amendment. These concerns are outlined in more specially below.

The Proposed Amendment would require that, upon receipt of a written notice, a member shall consider whether the proposed activity will: (1) interfere with or otherwise compromise the registered person's responsibilities to the member and/or the member's customers or (2) be viewed by customers or the public as part of the member's business based upon, among other factors, the nature of the proposed activity and the manner in which it will be offered.¹² Additionally, based on the member's review of such factors, the member would be required to evaluate the advisability of imposing specific conditions or limitations on a registered person's OBA, including where circumstances warrant, prohibiting the activity.¹³

The language of the Proposed Amendment provides as follows:

Supplementary Material .01 Obligations of Member Receiving Notice. Upon receipt of a written notice under Rule 3270, a member [must make a determination whether the proposed activity raises investor protection concerns, and if so, the firm must implement procedures or restrictions on the activity to protect investors, or prohibit the activity] shall consider whether the proposed activity will: (1) interfere with or otherwise compromise the registered person's responsibilities to the member and/or the member's customers or (2) be viewed by customers or the public as part of the member's business based upon, among other factors, the nature of the proposed activity and the manner in which it will be offered. Based on the member's review of such factors, the member must evaluate the advisability of imposing specific conditions or limitations on a registered person's outside business activity, including where circumstances warrant, prohibiting the activity. A member also must evaluate the proposed activity to determine whether the activity properly is characterized as an outside business activity or whether it should be treated as an outside securities activity subject to the requirements of NASD Rule 3040[110(b)(3)]. A member must keep a record of its compliance with these obligations with respect to each written notice received and must preserve this record for the period of time and accessibility specified in SEA Rule 17a-4(e)(1).

¹² FINRA Proposed Amendment, See Page 3 of 8, at <http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p121833.pdf>

¹³ *Id.*

- **Overly Broad Application - *Proposed Amendment Should be Narrowed in Scope*** – We believe that under the current language of the Proposed Amendment, it would cause virtually every broker-dealer to question any outside business activity that is financial in nature (e.g., insurance sales, investment advice, mortgage brokering, real estate agent, CPA, attorney, etc.). As a result, these firms would have to create policies and procedures that would impose specific conditions and limitations related to engaging in these other financial related OBAs.

As mentioned above, financial advisors affiliated with an IBD generally focus on comprehensive financial planning services and unbiased investment advice. These financial advisors provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisors are typically “main street Americans” who have tens and hundreds of thousands as opposed to millions of dollars to invest. Often, these financial advisors are the only provider of financial services and planning in their community. If restrictions are placed on these financial advisors and specific conditions and limitations are imposed by a broker-dealer on these activities, customer access to investment advice, investment services, and investment choice will be reduced.

In an effort to narrow the application of the Proposed Amendment, and prevent the limitation of customer access to investment advice, investment services, and investment choice, we urge FINRA to remove the second prong of the Proposed Amendment and adopt the following language:

Supplementary Material .01 Obligations of Member Receiving Notice. Upon receipt of a written notice under Rule 3270, a member [must make a determination whether the proposed activity raises investor protection concerns, and if so, the firm must implement procedures or restrictions on the activity to protect investors, or prohibit the activity] shall consider whether the proposed activity will: (1) interfere with or otherwise compromise the registered person’s responsibilities to the member and/or the member’s customers or (2) be viewed by customers or the public as part of the member’s business based upon, among other factors, the nature of the proposed activity and the manner in which it will be offered. Based on the member’s review of such factors, the member must evaluate the advisability of imposing specific conditions or limitations on a registered person’s outside business activity, including where circumstances warrant, prohibiting the activity.

While we see the importance of the public’s perception of certain OBAs, we believe that a member firm should focus on the legal responsibilities that run to its customers and the legal responsibilities that run to its registered person in determining if an OBA should be limited or prohibited. We fear that including perceptions in the evaluation of an OBA will cause broker-dealers to narrow the activities that they approve, thus limiting customer access to investment advice, investment services, and investment choice

- **Definition of “Responsibilities”** – The first prong of the Proposed Amendment requires the broker-dealer to “consider whether the proposed activity will interfere with or otherwise compromise the registered person’s **responsibilities** to the member and/or the member’s customers” (emphasis added). It is not clear from the documentation provided by FINRA, or the materials related to the Proposed Amendment what “responsibilities” are being referenced or referred to by FINRA. We suggest that FINRA expressly define what responsibilities it is alluding to in the Proposed Amendment.

Alternatively, we suggest that that FINRA remove the term “responsibilities” and adopt the following language in the Proposed Amendment: “consider whether the proposed activity will interfere with or otherwise compromise the registered person’s **[responsibilities] obligations under FINRA Rules, federal or state laws** to the member and/or the member’s customers”

Items that were not addressed in the Proposed Amendment by FINRA, but were raised in the Proposed Rule release:

- **Proposed Rule Should Impose an Ongoing Duty to Inform Broker-Dealers of Material Changes to Outside Business Activities** – We believe the Proposed Rule should impose an ongoing obligation on financial advisors to inform their broker-dealer of material changes to the nature of their outside business activity. This will insure that the broker-dealer has the necessary information to make informed decisions about the financial advisor’s continued involvement in the activity or the need to impose new conditions or restrictions with respect to the activity.

In FINRA’s July 30, 2010 response to comments on the Proposed Rule, FINRA provided that:

“the requirement for a registered person to amend or supplement the nature of the prior written notice is implicit in the proposed change. A registered person’s prior written notice is valid only to the extent that it continues to accurately describe the outside business activity. This, it is incumbent on the registered person to provide prior written notice before altering the nature of any outside business activity previously disclosed in writing to the firm.”¹⁴

We believe that this requirement is not implicit, as FINRA suggests, and should be expressly written within the context of the Proposed Rule. Absent such a requirement, broker-dealers will be unfairly exposed to regulatory scrutiny and legal exposure beyond their ability to control.

- **FINRA Should Provide Guidance on Implementation of the Final Rule** – Independent financial advisors have complied with their existing obligations under NASD Rule 3030 by providing their broker-dealers with prompt written notice of their OBA. Some of these businesses have been in operation for many years, provide much needed products and services to investors, and employ thousands of individuals. However, the Proposed Rule is silent as to its application to these pre-existing business relationships. It will be an enormous undertaking for IBD firms to analyze each of these established OBAs and

¹⁴ FINRA’s Response to Comments dated July 30, 2010, 4

adopt policies and procedures for each of them. We also believe it is unreasonable for FINRA to expect these businesses to accept broker-dealer efforts to control their longstanding business practices based upon vague potential investor protection concerns. Therefore, we believe it would be unfair to apply the Proposed Rule's requirements retroactively to such activities. We urge FINRA to adopt this policy, and state so clearly, when it implements the final rule.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with you to enhance investor protection.

Thank you for your consideration of our comments. Should you have any questions, please contact me at (202) 379-0943

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Dale Brown", written in a cursive style.

Dale E. Brown, CAE
President & CEO