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**Via Electronic Filing**

Florence E. Harmon  
Deputy Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington D.C. 20549-1090

**RE: File Number SR-FINRA-2009-047**  
**Proposed Rule Change to Adopt FINRA Rule 3160**

Dear Ms. Harmon,

The Cornell Securities Law Clinic (the "Clinic") welcomes the opportunity to comment on the proposed rule change (the "Rule Proposal") to incorporate National Association of Securities Dealers ("NASD") Rule 2350 ("Broker/Dealer Conduct on the Premises of Financial Institutions"), with certain amendments, as Financial Industry Regulatory Authority ("FINRA") Rule 3160 ("Network Arrangements Between Members and Financial Institutions"). The Clinic is a Cornell Law School curricular offering, in which law students provide representation to public investors and public education on investment fraud in the largely rural "Southern Tier" region of upstate New York. For more information, please see <http://securities.lawschool.cornell.edu>.

The Clinic generally supports the Rule Proposal, with one modification discussed below. The Rule Proposal generally improves investor protection by reducing potential confusion that may result from dealing with a financial institution and a broker-dealer simultaneously. However, as discussed below, removing the written acknowledgment requirement is detrimental to this goal.

The Rule Proposal seeks to incorporate the greater part of NASD Rule 2350, which aimed to reduce the potential confusion that may arise when retail banking customers encounter broker-dealer services on the premises of financial institutions. Additional amendments to Rule 2350 are also proposed: (1) amending Rule 2350, which applies only to on-site broker-dealers, to include all broker-dealers that enter into

networking agreements with financial institutions, regardless of whether they operate on or off the institution's premises; (2) changing the language regarding "setting" to reflect Securities and Exchange Commission ("SEC") Regulation R; (3) implementing the requirements of Rule 701 of Regulation R, which imposes certain obligations on broker-dealers that are parties to networking agreements, (4) removing Rule 2350's requirement that customers sign a written acknowledgment of the risks associated with securities, and (5) expanding the application of the disclosure requirements for advertising materials.

**1. The Clinic Opposes the Removal of the Written Acknowledgment Requirement**

The Clinic opposes the removal of NASD Rule 2350 (c)(3)(B), which requires that broker-dealers "make reasonable efforts to obtain from each customer during the account opening process a written acknowledgment of receipt of . . . disclosures" regarding differences between deposits and securities, and the risks associated with the latter. The Rule Proposal justifies removal of this provision with two reasons. First, because the proposed rule will apply to all broker-dealers regardless of whether they operate on or off the premises of a financial institution, written acknowledgments may be harder to obtain. Second, the Rule Proposal considers the written acknowledgment requirement unnecessary, because broker-dealers must make the disclosures orally and in writing.

Neither reason justifies the removal of the written acknowledgment requirement. First, when dealing with customers over the telephone or via the internet, broker-dealers should have no problem obtaining some form of adequate 'written' acknowledgement. For example, if dealing over the internet, broker-dealers could employ "clickwrap" technology that allows consumers to click an "I Accept" button after reading the terms and conditions of an agreement, or in this case after reading a disclosure.<sup>1</sup> If broker-dealers interact with customers over the phone, facsimile or email confirmations could easily be used. Any administrative burden imposed on broker-dealers by a written acknowledgment requirement is greatly outweighed by the benefit of reducing customer confusion.

Second, while oral and written disclosure requirements help to ensure that there is no customer confusion arising from a networking agreement, written acknowledgment of the acceptance of such disclosures also reduces confusion. While it is true that some customers may sign an acknowledgment without reading it, others will consider the oral and written disclosures more carefully if they are required to sign a document stating that they received them. In conclusion, the Clinic opposes the removal of the written acknowledgment requirement because it poses no significant burden on broker-dealers and would, in some if not all cases, reduce potential customer confusion.

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<sup>1</sup> See generally Robert A. Hillman & Jeffrey J. Rachlinski, *Standard-Form Contracting in the Electronic Age*, 77 N.Y.U. L. REV. 429, 464 (2002) (discussing the use of clickwrap technology for online consumer transactions).

**2. The Clinic Supports Expanding the Scope of Rule 2350 to Include Broker-Dealers that Operate Off the Premises of Financial Institutions**

The Clinic supports amending the scope of Rule 2350, which only applies to on-site broker-dealers, to include all broker-dealers that enter into networking arrangements with financial institutions. The distinction between on-site and off-site broker-dealers does not further the goal of reducing potential customer confusion when dealing simultaneously with financial institutions and broker-dealers. Uniform application of proposed FINRA Rule 3160 to all broker-dealers that have entered into networking agreements with financial institutions will decrease the likelihood of customer confusion. The Clinic therefore supports this amendment.

**3. The Clinic Supports the Rewording of the “Setting” Requirements**

The Clinic supports the Rule Proposal’s minor changes to NASD Rule 2350(c)(1) (Setting). The Clinic recognizes that the proposed minor changes in no way affect the substance of 2350(c)(1), but have been proposed to conform the FINRA Rule text with the text of existing statutes and regulations. The Clinic strongly supports the substance of 2350(c)(1), because requiring broker-dealers to clearly distinguish themselves from the financial institution they have entered into a networking agreement with will reduce the likelihood of customer confusion in this setting.

**4. The Clinic Supports Imposing Rule 701 Obligations to All Broker-Dealers that are parties to Networking Agreements**

The Clinic supports imposing the obligations outlined in Rule 701 of SEC Regulation R<sup>2</sup> on all broker-dealers which enter into networking agreements with financial institutions because these obligations will reduce the likelihood of customer confusion. Additionally, imposing Rule 701 obligations on broker-dealers directly, instead of requiring that networking agreements include certain broker-dealer obligations as NASD Rule 2350 does, is a more effective way of policing broker-dealer conduct in the context of third-party brokerage arrangements.

The Clinic supports allowing referral fees to take the form of incentive compensation or contingent compensation when dealing with high net worth customers pursuant to Rule 701 solely because the net worth requirement is set appropriately high and because Rule 701 imposes additional obligations on broker-dealers when dealing with such customers. One danger of allowing referral fees at all is that financial institution employees will effectively become “finders or salespeople for a broker-dealer.”<sup>3</sup> If the employees act like salespeople for broker-dealers, the rationale for allowing financial institutions to enter into networking agreements with broker-dealers

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<sup>2</sup> 17 C.F.R. § 247.701 (2008).

<sup>3</sup> See 72 Fed. Reg. 56522, 56523.

without registering as securities dealers is undermined. Limiting normal referral fees to a “one-time nominal cash fee” that is not contingent on whether the referral results in a transaction effectively removes the incentive for financial institution employees to act like salespeople for the broker-dealer.<sup>4</sup>

However, by adopting Rule 701, FINRA proposes to adopt an exception to these requirements for high net worth customers. The assumption on which this exception is justified is that “such . . . individuals are more likely to be able to understand and evaluate the relationship between a financial institution and its employees and the institution’s broker-dealer partner and the impact of that relationship on any resulting securities transaction with the broker-dealer.”<sup>5</sup> While this assumption may be true in some cases, it is certainly false in others. For example, newly wealthy or elderly customers that satisfy the net worth requirement may not have the corresponding level of sophistication that Rule 701 assumes.<sup>6</sup>

The Clinic nevertheless supports the adoption of Rule 701 for two reasons. First, the high net worth threshold – “5 million dollars in net worth excluding the primary residence and associated liabilities”<sup>7</sup> – is sufficiently high to exclude the vast majority of investors from this exception. Second, the additional requirements Rule 701 imposes on broker-dealers when dealing with a high net worth customer (notably the suitability/sophistication determination and requiring that the broker-dealer has a reasonable basis to believe the customer is a high net worth customer) are sufficient to guard against customer confusion.

## **5. The Clinic Supports the Expansion of the Advertising Disclosure Requirements**

The Clinic supports expanding the scope of the disclosure requirements related to advertising. NASD Rule 2350 advertising disclosure requirements apply to material that announces the location of a financial institution where broker-dealer services are provided or that are distributed by the broker-dealer on the premises of the financial institution. The Proposed Rule extends the disclosure requirements to a broker-dealer’s advertisements that promote the name or services of the financial institution or that the broker-dealer distributes at any location where the financial institution is present or represented. Increasing the scope of advertising material that is subject to disclosure requirements will help reduce customer confusion. The Clinic therefore supports this amendment.

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<sup>4</sup> See 15 U.S.C. 78c (4)(B)(i)(IV)

<sup>5</sup> See 72 Fed. Reg. at 56523.

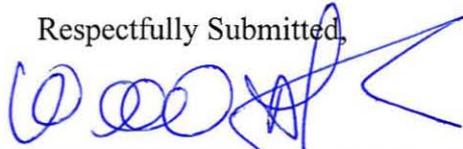
<sup>6</sup> The Clinic also notes that the Gramm-Leach-Bliley Act did not support such an exception. See 15 U.S.C. 78c.

<sup>7</sup> 17 C.F.R. § 247.701(d)(1)(i)(A).

**Conclusion**

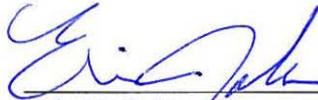
The Clinic greatly appreciates the opportunity to comment on this Rule Proposal. The Clinic generally supports the Rule Proposal because it protects investors by reducing the potential for customer confusion when dealing with financial institutions and broker-dealers that have entered into networking agreements. However, the Clinic believes that the removal of the written acknowledgment requirement represents a step in the wrong direction and does not further the goal of protecting investors from confusion when dealing with financial institutions and broker-dealers simultaneously.

Respectfully Submitted,



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