FINANCIAL SERVICES INSTITUTE
VOICE OF INDEPENDENT BROKER-DEALERS AND INDEPENDENT FINANCIAL ADVISORS
www.financialservices.org

VIA ELECTRONIC MAIL

December 6, 2010

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

RE: File Number SR-FINRA-2010-034 – Notice of Filing of Amendments No. 1 and 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Amended, to Adopt FINRA Rule 4530 (Reporting Requirements) in the Consolidated FINRA Rulebook

Dear Ms. Murphy:

On October 18, 2010, FINRA filed Amendment Number 1 to FINRA's proposal to adopt FINRA Rule 4530 in the Consolidated FINRA Rulebook (Proposed Rule),[1] and on October 22, 2010, FINRA filed Partial Amendment Number 2[2] to the Proposed Rule. On November 12, 2010, the Securities and Exchange Commission (SEC) filed for comment a Notice of Filings of Amendments No. 1 and 2 and an Order Granting Accelerated Approval of a Proposed Rule, as Amended, to Adopt FINRA Rule 4530.[3] In the November 12, 2010 filing, the Securities and Exchange Commission (SEC) solicits comments on the recently filed amendments to the Proposed Rule and its Order of approval.

The Financial Services Institute (FSI)[4] welcomes this opportunity to comment on the Proposed Rule, as amended. We note that the Proposed Rule is substantially similar in nature to the rule proposals set forth in Regulatory

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[1] Notice of Filing of Amendment No. 1 to Proposed Rule Change to Adopt FINRA Rule 4530 (Reporting Requirements) in the Consolidated FINRA Rulebook at http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p122280.pdf

[2] Notice of Filing of Amendment No. 2 to Proposed Rule Change to Adopt FINRA Rule 4530 (Reporting Requirements) in the Consolidated FINRA Rulebook at http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p122331.pdf

[3] Notice of Filing of Amendments No. 1 and 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Amended, to Adopt FINRA Rule 4530 (Reporting Requirements) in the Consolidated FINRA Rulebook at http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p122432.pdf

[4] 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.

Notice 08-71[5] and the July 30, 2010 filing, which FSI commented on through a January 16, 2009 comment letter[6] and a September 15, 2010 comment letter,[7] respectively. While we are encouraged to see that FINRA adequately responded to several items raised in our prior comment letters,[8] we have serious concerns about certain aspects of the Proposed Rule. Although we have raised these concerns in prior comment letters, we believe that FINRA has not sufficiently responded to critical issues that require attention in drafting the Proposed Rule. Specifically, we are concerned with the monetary reporting thresholds set forth in section 4530(a)(1)(G) and 4530(a)(1)(H), the scope of the Proposed Rule, and the duplicative reporting requirements. These concerns are outlined below in more detail.

Background on FSI Members

FSI represents independent broker-dealers (IBDs) 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.[9] 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

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[5] Regulatory Notice 08-71, FINRA Requests Comment on Proposed Consolidated FINRA Rule Governing Reporting Requirements, available at http://www.finra.org/Industry/Regulation/Notices/2008/P117455

[6] FSI Comment Letter in response to Regulatory Notice 08-71, available at http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/noticecomments/p117738.pdf

[7] Letter from Dale E. Brown, President and CEO, Financial Services Institute, to Elizabeth M. Murphy, Secretary, Commission, dated September 15, 2010, available at http://sec.gov/comments/sr-finra-2010-034/finra2010034-7.pdf

[8] FSI is encouraged to see that FINRA sufficiently responded to issued related to ministerial violations, issues related to former associated persons, and provided additional and consistent definitions throughout the Proposed Rule.

[9] Cerulli Associates at http://www.cerulli.com/.

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.[10] 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 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, FSI has serious concerns about certain aspects of the Proposed Rule. Specifically, we are concerned with the monetary reporting thresholds set forth in section 4530(a)(1)(G) and 4530(a)(1)(H), the scope of the Proposed Rule, and the duplicative reporting requirements. These concerns are outlined below in more detail.

- **Reporting Thresholds are Too Low** – As provided for in our prior comment letters, Proposed Rule 4530(a)(1)(G) and 4530(a)(1)(H)(2) provide that each member firm should promptly report to FINRA if the member:

> "is a defendant or respondent in any securities- or commodities-related civil litigation or arbitration, is a defendant or respondent in any financial-related insurance civil litigation or arbitration, or is the subject of any claim for damages by a customer,

[10] These "centers of influence" may include lawyers, accountants, human resources managers, or other trusted advisors.

> broker or dealer that is financial or transactional in nature, [which] and such civil litigation, arbitration or claim for damages has been disposed of by judgment, award or settlement for an amount exceeding **$15,000. However, when the member is the defendant or respondent or is the subject of any claim for damages by a customer, broker or dealer, then the reporting to [the Association] FINRA shall be required only when such judgment, award[,]or settlement is for an amount exceeding $25,000; or [(8) is the subject of any claim for damages by a customer, broker, or dealer which is settled for an amount exceeding $15,000. However, when the claim for damages is against a member, then the reporting to the Association shall be required only when such claim is settled for an amount exceeding $25,000;] (Emphasis added)**
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> Or,
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> is" an associated person of the member is the subject of any disciplinary action taken by the member [against any person associated with the member] involving suspension, termination, the withholding of [commissions] compensation or of any other **remuneration in excess of $2,500, [or] the imposition of fines in excess of $2,500[,]** or is otherwise disciplined in any manner [which] that would have a significant limitation on the individual's activities on a temporary or permanent basis. **(Emphasis added)**

While "FINRA believes that the current dollar thresholds continue to be consistent with the purposes of the rule,"[11] we believe that the reporting thresholds should be increased and adjusted to reflect a reasonable rate of inflation over the 14-year period since NASD Rule 3070 was originally adopted. While FINRA states in the proposing release that "the $15,000 reporting threshold for an associated person is consistent with the Forms U4 and U5 current reporting thresholds,"[12] we still believe that it should be increased to match inflation. Moreover, we believe that FINRA has not provided a sufficient rational as to why it believes "that the current dollar thresholds continue to be consistent with the purposes of the rule." Accordingly, we request additional support from FINRA as to why it believes that the current reporting dollar thresholds continue to be consistent with the purposes of the rule.

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[11] See page 15, http://sec.gov/rules/sro/finra/2010/34-62621.pdf
[12] *Id.*

Moreover, we recommend that the Proposed Rule be amended to reflect the following reporting thresholds:

- Proposed Rule 4530(a)(1)(G)
  - Thirty thousand dollars ($30,000) for financial advisors;
  - Fifty thousand dollars ($50,000) for broker-dealers.

- Proposed Rule 4530(a)(1)(H)(2)
  - Five thousand dollars ($5,000) for financial advisors.

- **Scope of the Proposed Rule is Overly Broad** - As outlined in our prior comment letters, we believe that the Proposed Rule represents a significant expansion of the scope of the existing reporting requirements. For example, Section 4530(a)(1)(A) of the Proposed Rule expands broker-dealer reporting obligations well beyond the securities business of broker-dealer firms by including violations of any "insurance, commodities, financial or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body, self-regulatory organization or business or professional organization."[13] Events involving foreign regulatory bodies are also added to the reporting obligations of Sections 4530(a)(1)(C), (D) and (F). In addition, Section 4530(a)(1)(G) would require the reporting of insurance related civil litigation or arbitration matters that meet the reporting thresholds outlined in the Proposed Rule. In effect, these sections expand FINRA's reach to include matters over which it does not currently have jurisdiction. We oppose any attempt on FINRA's part to extend its jurisdiction beyond the broker dealer activities it is authorized by the Securities and Exchange Commission (SEC) to regulate.

  Ultimately, we believe that the scope of the Proposed Rule will place an undue and unenforceable burden on IBD firms. Accordingly, we urge the SEC to scale back the scope of the Proposed Rule by eliminating reporting requirements for activities outside the scope of FINRA's current jurisdiction.

- **Duplicative Reporting Requirements** – As provided for in our prior comment letters, Section 4530(e) of the Proposed Rule provides as follows:

  "[(d)] (e) Nothing contained in this Rule shall eliminate, reduce[,] or otherwise abrogate the responsibilities of a member or person associated with a member to promptly [file with full disclosure,] disclose required [amendments to] information on the Forms BD, [Forms] U[-]4 [and] or U[-]5, as applicable, [or] to make any other required filings[, and] or to

[13] 4530(a)(1)(A)

> respond to [NASD] FINRA with respect to any customer complaint, examination[,] or inquiry. In addition, members are required to comply with the reporting obligations under paragraphs (a), (b) and (d) of this Rule, regardless of whether the information is reported or disclosed pursuant to any other rule or requirement, including the requirements of the Forms BD or U4. However, a member need not report an event otherwise required to be reported under paragraphs (a) or (b) of this Rule if the member discloses the event on the Form U5, consistent with the requirements of that form."
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> In the Proposed Rule filing with the SEC, FINRA notes that "[w]hile information disclosed on the Forms BD and U4 are not subject to this exception [granted to information reported on a U5] at this time, FINRA will work toward the goal of eliminating duplicative reporting of information disclosed on those forms." Regulatory Notice 08-71 also represented that FINRA was working to eliminate duplicative reporting of information. Moreover, in 1995, the NASD made this same commitment without resulting progress on the initiative or reducing duplicative reporting requirements.[14]
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> Accordingly, we believe that FINRA should take advantage of this current opportunity to act, and should draft the rules to reduce duplicative reporting rather than postponing this effort to another day. Firms should not be required to report the same information to different areas within FINRA. FINRA should assess its current systems and aid its members in reducing reporting requirements. As a result, we urge FINRA to eliminate the requirement for member firms to report information that has already been reported via Forms BD and U4.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with you to achieve further efficiency in the reporting process while maintaining investor protection.

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

Respectfully submitted,

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[14] See Exchange Act Release No. 34-35956, 60 FR 36841 (July 18, 1995): "Further, upon implementation of the redesigned CRD which will provide more ready access to registration information, the NASD will undertake to review the proposed reporting rule to determine whether certain of the duplicative requirements may be eliminated. To the degree that such modifications are feasible, the NASD would intend to delete such provisions from the proposed rule."

Dale E. Brown, CAE
President & CEO