The Surety & Fidelity Association of America

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December 17, 2010

Via Electronic Mail

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

Re: Notice of Filing of Proposed Rule Change
To Adopt FINRA Rule 4360 ("Notice")
File No. SR-FINRA-2010-059

Dear Ms. Murphy:

The Surety & Fidelity Association of America ("SFAA") is a trade association of companies that are licensed to provide surety and fidelity bonds. The vast majority of fidelity bonds that are obtained by financial institutions such as securities dealers are provided by SFAA members. SFAA also develops various standard fidelity forms and riders that are available for use by our members. The Financial Institution Bond, Standard Form No. 14 ("Form 14"), developed by SFAA, is intended to insure against fidelity, forgery and theft risks for broker dealer and securities firms. The captioned proposed rule sets forth the fidelity bond requirements for members of the Financial Industry Regulatory Authority ("FINRA"). Thus, SFAA and our member companies have a significant interest in Rule 4360.

On September 9, 2009, we submitted comments to FINRA when it initially proposed the rule under Regulatory Notice 09-44. As set forth in the captioned Notice, Rule 4360 has been revised to address many of the concerns that were raised in our 2009 letter. However, some clarifications are needed to ensure that the type of coverage prescribed by Rule 4360 is, in fact, available in the market.

As stated in the Notice, proposed Rule 4360 would not maintain the exemption for sole proprietorships and sole stockholder firms. The Notice indicates that such firms may need fidelity bond coverage, because such firms may have employees and may be exposed to burglary and theft risks covered by a fidelity bond. 75 Fed. Reg 72850, 72853 (November 26, 2010). We agree with this premise. However, subsection (b)(2) of Rule 4360 raises a concern whether the rule is requiring the owners of firms themselves to be covered for fidelity (Insuring Agreement A - employee dishonesty). It states: "[A] member must maintain fidelity bond coverage for any person associated with the member, except directors or trustees who are not performing acts within the scope of the usual duties of an officer or employee." Because an owner or sole stockholder may be associated with the firm, the rule suggests that the fidelity bond must cover, under Insuring Agreement A, the dishonesty of sole stockholders or owners. Such coverage is not available in the market. As the sole owner or sole stockholder, the person is essentially the alter-ego of the insured. It is a well established principal of insurance that one cannot insure against loss caused by one's own intentional acts. Further, the insurer underwrites the insured and determines whether to provide fidelity coverage based on the soundness of the insured's internal controls. There is no one to oversee a sole owner or stockholder, and such a person can easily evade those controls, however sound they may be. Thus the dishonesty of the sole stockholder or owner is a risk that cannot be underwritten prudently. For the reasons provided, we recommend that subsection (b)(2) be revised to state:

> Insuring Agreement A (Fidelity) must cover the acts of ~~[A] member must maintain fidelity bond coverage for~~ any person associated with the member, except a sole proprietor or sole stockholder, or directors or trustees who are not performing acts within the scope of the usual duties of an officer or employee.

On a related note, the discussion in the Notice imprecisely describes the scope of coverage under Insuring Agreement A. The Notice states, "The purpose of a fidelity bond is to protect a member against certain types of losses, including, but not limited to, those caused by the malfeasance of its officers and employees." 75 Fed. Reg at 72851 (emphasis added). "Malfeasance" is a broad term and is not necessary restricted to intentional conduct. The term means only wrongful conduct. Black's Law Dictionary (9th ed. 2009). The fidelity coverage forms that are available in the market cover losses caused by the employee's dishonesty if the employee intended to cause the loss. Thus, one of the purposes of the fidelity bond is to protect a member against the employee's intentional dishonest acts, not negligence or laziness, even if such conduct were malfeasance. We ask that any approval of Rule 4360 by the Commission make this clarification.

Thank you for your consideration.

Sincerely,

Robert J. Duke