July 20, 2011

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

Re: File Number SR-FINRA-2011-028

Dear Ms. Murphy:

This letter is submitted on behalf of the National Society of Compliance Professionals Inc. ("NSCP") in response to the SEC's publication of Release No. 34-64736 (the "Proposed Rule Change"). As explained below, NSCP has a very large membership and a great interest in ensuring that the outcome of the NASD's consolidation with the New York Stock Exchange ("NYSE") benefits all member firms.

Set forth below is a brief description of NSCP, its mission and goals, followed by a discussion of elements of the Proposed Rule Change that we believe should be revised because of the nature of the potential impact of those elements on NSCP members.

NSCP's Mission

As you may be aware, NSCP is a non-profit membership association with 1,900 members dedicated to supporting the compliance profession. Our members work in the compliance areas of broker-dealers and investment adviser firms and come from all sizes of firms. To our knowledge, NSCP is the largest organization of securities industry professionals in the United States devoted exclusively to compliance. NSCP serves its members' interests by sponsoring regional and national education meetings; publishing "white papers" on best practices within the securities industry; providing comments to federal and SRO regulators on new rules and proposed amendments to existing rules; and meeting with regulators to discuss "hot topics" in the industry and share the concerns of compliance professionals. In short, NSCP's mission is to ensure that the securities compliance industry meets high professional standards and effectively communicates its needs to regulators and others.

We would like to recognize several positive points in the Proposed Rule Change.

1. The formal endorsement of a risk-based review system for the supervision of transactions, correspondence and internal communications in Proposed Supplementary Materials .07 and .08. This appropriately provides greater latitude to each member firm to determine the most effective means of supervising its business to comply with regulatory requirements.

2. The recognition in Proposed FINRA Rule 3110(a) of the principle that the requirement for each member firm to establish and maintain a system to supervise the activities of its associated persons is limited to compliance with applicable securities laws and regulations.

Proposed Rule 3110(a) and Supplementary Material .01 (Business Lines).

FINRA proposes in Supplementary Material .01 that, for a member's supervisory system to be reasonably designed to achieve compliance with FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade), it must "include supervision for all of the member's business lines irrespective of whether they require broker-dealer registration."[1] Proposed FINRA Rule 3010(a), however, only requires members to "establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA and Municipal Securities Rulemaking Board (MSRB) rules."[2] Likewise, proposed FINRA Rule 3110(a)(2) limits a member's responsibility to designate an appropriately registered principal to carry out supervisory responsibilities to those activities which require broker-dealer registration. The contrast between the requirements of the Proposed Supplementary Material and Proposed FINRA Rule 3110(a), paragraphs (1) and (2), introduces an apparent contradiction that should be clarified. Although FINRA introduced the Proposed Supplementary Material to "avoid further confusion" over extending FINRA's oversight and rules into non-securities activities[3], that confusion has not been remedied in the current Proposal.

As noted in NSCP's previous comment letter[4] on this Rule Proposal, requiring members to supervise non-broker-dealer lines of business would impose an undue burden on existing broker-dealer compliance staff:

> "…member firms devote considerable resources to ensuring that compliance staff are well trained, properly licensed, and have the tools to do their jobs. This training must focus on a broker-dealer's "broker-dealer activities" – indeed, if member firms were required to bifurcate their compliance programs into separate programs to address rules and regulations not subject to FINRA's jurisdiction – and then devote resources to develop separate compliance programs that fit within the FINRA broker-dealer compliance model - fewer resources could be devoted to broker-dealer compliance activities."

[1] SR-2011-028, Supplementary Material .01 Business Lines. Exhibit 5, Pg 391.
[2] SR-2011-028, Proposed Rule 3110(a), Exhibit 5, pg 376.
[3] SR-2011-28, paragraph 5(c), pg 33.
[4] NSCP letter to Marcia E. Asquith dated June13, 2008.

While recognizing FINRA's jurisdiction over broker-dealers and their attendant securities activities, NSCP is concerned that the Proposed Supplementary Material as drafted may unintentionally but effectively result in an expansion of the scope of FINRA examinations of member firms to include non-broker-dealer and non-securities activities. The Proposed Supplementary Material should be revised, at a minimum, to state that member firms will be deemed to be in compliance with the Proposed Supplementary Material if they are engaged in a line of business that is subject to regulation by a federal or state regulator, or SRO, and are supervising that business in accordance with the requirements of that regulatory entity.

Proposed FINRA Rule 3110(b) (Written Procedures) and Proposed Supplementary Material

FINRA is proposing in Rule 3110(b)(2) that "all" transactions of a member firm relating to the investment banking and securities business of the firm be reviewed by a registered principal, and that the principal's review be evidenced in writing. Proposed Supplementary Material .07, which FINRA has stated "is considered part of the rule and carries the same force of regulation"[5] as a rule, permits firms to use a risk-based review system to comply with the Rule. FINRA also acknowledges that "members may need to prioritize their review processes due to the volume of information that must be reviewed by using a review methodology based on a reasonable sampling of information…"[6] This competing guidance introduces ambiguity to the FINRA Rule book through an apparent inconsistency between the proposed requirement that "all" transactions be reviewed and the permissibility of using a risk-based approach that might include a review of fewer than "all" transactions. We suggest deleting the word "all" from the proposed rule, and revising the rule to more clearly adopt the risk-based standard. We identified this inconsistency in our response to Regulatory Notice 08-24[7] and do not believe it has been adequately addressed in the revised Proposal.

Proposed FINRA Rule 3110(c): Internal Inspections

Paragraph (c)(3) of Proposed Rule 3110 would require member firms to "prevent the inspection standards required pursuant to paragraph (c)(1) of this Rule, from being reduced in any manner due to any conflicts of interest that may be present." As stated in our response to Regulatory Notice 08-24[8] , we would expect compliance staff to have difficulty interpreting the precise meaning of "reduced in any manner." An additional challenge to compliance staff is presented by the reference to "inspection standards" in paragraph (c)(1) of the Proposed Rule. In fact, that paragraph is chiefly concerned with the periodicity of inspections. If the intent is that the periodicity of internal inspections should not be reduced due to any conflicts of interest, FINRA should modify this Proposed Rule accordingly.

[5] SR-2011-28, paragraph 5(a), pg 29.
[6] SR-2011-28, paragraph 5(h)(2), pg 42.
[7] NSCP letter to Marcia E. Asquith dated June13, 2008.
[8] NSCP letter to Marcia E. Asquith dated June13, 2008.

Proposed FINRA Rule 3110(d): Transaction Review and Investigation

FINRA is proposing in paragraph (d) of new Rule 3110 that each member "include in its supervisory procedures a process for the review of securities transactions that are effected for the account(s) of the member and/or the member's associated persons and any other covered account to identify trades that may violate the provisions of the Exchange Act, the rules thereunder, or FINRA rules prohibiting insider trading and manipulative and deceptive devices …"[9]

Paragraph (3) ("Definitions") of the Proposed Rule includes the following definition of the term "covered account" for the purpose of that Rule:

(i) any account held by the spouse, child, son-in-law, or daughter-in-law of a person associated with the member where such account is introduced or carried by the member;
(ii) any account in which a person associated with the member has a beneficial interest; and
(iii) any account over which a person associated with the member has the authority to make investment decisions.

The Rule Proposal expands the scope of the previous version of Proposed FINRA Rule 3110(d) to include a review for "manipulative and deceptive devices," as well as insider trading, for all accounts in which an associated person of a member may have a beneficial interest or the authority to make investment decisions. Concurrently, subparagraphs (ii) and (iii) of the Proposed Rule would require this review for accounts that associated persons of a firm may hold at other broker-dealers.

FINRA states that the Rule Proposal "is intended to help members comply with their existing obligations under Section 15(g) [*sic*] of the Act, which requires all registered brokers or dealers to "establish, maintain, and enforce written policies and procedures reasonably designed…to prevent the misuse in violation of [the Act] . . . or regulations thereunder, of material, nonpublic information by such broker or dealer or any person associated with such broker or dealer."[10]

The Rule Proposal would accomplish this with respect to insider trading, but goes beyond that objective by expanding the set of trades to be reviewed to those that may violate the various rules regarding "manipulative and deceptive devices." Rule 10b5-1(a) of the Act states that the "manipulative and deceptive devices" include, "among other things", insider trading. "Other things" could reasonably be expected to encompass the manipulation of security prices as describe in Section 9 of the Act. Detecting that type of activity for accounts held away from the member could be difficult and costly for members, in particular those offering on-line brokerage services. FINRA has established an expectation that online firms should strongly "consider conducting computerized surveillance of account activity to detect suspicious transactions and activity."[11] Online brokerage firms would be forced to establish electronic feeds of trading activity in covered accounts held at other member firms to enable the "computerized surveillance of account activity" in those accounts.

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[9] SR-2011-28, Proposed Rule 3010(d)(1), Exhibit 5, pg 387.
[10] SR-2011-28, paragraph 5(p)(1), pg 60.
[11] FINRA Letter of Acceptance, Waiver and Consent No. 2007009026302 in the case of Scottrade, Inc., pg 4.

In addition, inappropriate activity in a retail brokerage account cannot reasonably be detected in a vacuum. For example, a limited purpose broker-dealer that is not authorized to engage in retail activity would be hard-pressed to analyze whether an employee trading in his or her account at another firm is engaging in inappropriate activity. Such supervision realistically can be performed only in the context of broader firm activity. For instance, a firm engaging exclusively in institutional sales and trading activity should have a supervisory system that encompasses a review of its employees' outside accounts against that activity. However, if an employee is engaging in inappropriate account activity beyond that, it would likely be impossible for the firm to detect it.

Requiring member firms to adopt these measures for the review of "manipulative and deceptive devices" beyond insider trading activity seems unnecessary in that each member involved in retail brokerage has the obligation, under existing rules, to review all accounts introduced or carried by the member for that type of activity.

The Proposed Rule should be revised to clearly limit the scope of the rule to the identification of trades that may constitute insider trading.

Alternatively, paragraph (3) of the Proposed Rule ("Definitions") could be revised to limit the scope of subparagraphs (ii) and (iii) to accounts introduced or carried by the member.

Proposed Supplementary Material .13 Use of Electronic Media to Communicate Written Supervisory Procedures.

Proposed Supplementary Material .13 would permit a member to distribute and amend its written supervisory procedures using electronic media, subject to certain conditions, including "notifying associated persons of such amendments" and "verifying, at least once each calendar year, that associated persons have reviewed the written supervisory procedures." Each of these elements should be revised to narrow the scope of the item to those associated persons to whom the written supervisory procedures pertain.

Written supervisory procedures (WSPs) are intended for the use of supervisors in their supervision of the business, not for the use of all associated persons. Further, while some WSPs may pertain to every supervisor, others are only applicable to a particular business area. Giving members the ability to restrict the distribution of amendments to the WSPs, and the requirement for the annual review, to applicable supervisors would both simplify the administration of this process by member firms and direct the attention of supervisors to those WSPs for which they are responsible.

Proposed Supplementary Material .15 General Presumption of Three-Year Limit for Periodic Inspection Schedules.

Proposed Supplementary Material .15 establishes a "general presumption that a non-branch location will be inspected at least every three years." This is problematic in view of the broad definitions of "non-branch locations" in current NASD Rule 3010(g) and Proposed Rule 3110(e)(2). For example, based on the current and proposed Rules, an office of convenience would be deemed to exist if an associated person were to use it on one day in one calendar year. Members are currently required to inspect such locations on a regular schedule, with the frequency and scope of inspections to be determined based on factors such as the nature and volume of business conducted at the office and

the nature and extent of contact with customers.[12] Creating a presumption that such a location must be inspected "at least every three years" establishes an arbitrary standard that appears unwarranted in view of existing guidance with respect to non-branch locations.

Proposed Rule 3120(b)((2).

Proposed Rule 3120(b)(2) requires that the annual report to senior management pursuant to subparagraph (a) of the Rule include "a discussion of the preceding year's compliance efforts… in each of the following areas" and goes on to list risk management as one of the seven required topics.

Of the seven topics identified for a discussion of the preceding year's compliance efforts, six are the subject of specific FINRA or NASD rules (e.g., trading and market activities, AML). Risk management, however, although integral to the management by many firms of their supervisory system, is not an area mandated by specific rule, i.e., risk management per se is not a separately required element of the broker-dealer compliance program requiring supervisory controls.

Furthermore, Risk Management is already established in many large firms as a separate control area, analogous to Compliance and Internal Audit. Requiring a member firm's Chief Compliance Officer (CCO) to address risk management as a formal element in a required report to senior management places the CCO in the position of having to report, as part of his or her compliance program, the functional activity of another control area that in many firms is likely to be under the purview of the firm's Chief Risk Officer and is qualitatively distinct from the work of the compliance department. In addition, CCOs may not have the requisite skills to provide an analysis of the technical aspects of risk management.

In view of the foregoing, we suggest that FINRA confirm, within this Proposed Rule, that it is permissible for the CCO to rely on certifications, representations or undertakings from managers of areas not under the purview of, or routinely overseen by, Compliance, such as Finance and Risk Management, in submitting information related to those areas in the annual compliance report.

We look forward to being of continued assistance in the rule consolidation process. On behalf of NSCP, I thank you for your consideration.

Very truly yours,

Joan Hinchman
Executive Director, President and CEO

[12] NASD Notice to Members 98-38.