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Via email: rule-comments@sec.gov

July 29, 2013

RE: SR-FINRA-2013-025:
Proposed Rules Changes Regarding Supervision

Integrated Management Solutions USA LLC ("IMS") is pleased to comment on SR-FINRA-2013-025, Proposed Rules Changes Regarding Supervision (the "Proposed Rules"). These have been proposed by FINRA as part of its process of developing a new consolidated rulebook and to detail proposed supervisory requirements.[1]

IMS is one of the largest providers of financial accounting and compliance consulting services to the financial services industry, providing such services to about 100 FINRA members, among others types of financial services firms.[2] We believe that our regular, daily experience with FINRA rules and how they are used by FINRA itself provides a perspective that enables us to assess the impact of the Proposed Rules on FINRA members from both a regulatory and business perspective. In our role as business experts, moreover, we are also conscious of the damage that elements of the Proposed Rules will likely cause to a significant number of member firms.

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1 Securities and Exchange Commission, Release No. 34-69902, File No. SR-FINRA-2013-025, pp. 2-3, passim.

2 The statements in this comment letter incorporate the views of IMS, not those of our clients.

Overall Concerns

Despite some limited distinctions in the Proposed Rules based on a firm's gross revenues, FINRA continues to impose compliance costs on firms that significantly, disproportionately and adversely impact small to medium-sized firms. Moreover, these rules have been proposed without any significant cost-benefit analysis of their impact, in disregard of Congressional mandates in the Dodd-Frank Act[3] and elsewhere. Although the Release in support of the Proposed Rules states that firms should exercise independent judgment and be allowed some flexibility in implementation, the Proposed Rules are a "treatise" in micromanagement by FINRA. In the guise of rule consolidation, the Proposed Rules go far beyond existing rules and practices, impose substantial costs on firms, and provide little, if any, significant improvement in compliance practices and procedures. We do not see how mandating the hiring of additional compliance personnel and the preparing of additional reports will necessarily lead to more effective and vigorous compliance or the elimination of conflicts of interest. FINRA's lip service to risk-based compliance rules buries effective risk management with additional requirements that have not been validated or proven cost-effective.

Our original draft letter in response to the Proposed Rules discussed many of the issues raised by others in their submitted comment letters. To avoid duplicative comments, we wish to state that we support the concerns and recommendations raised in the letters submitted by (1) Ira D. Hammerman, Esq., Senior Managing Director and General Counsel, SIFMA (dated July 29, 2013); (2) Mr. J.S. Brandenburger of FSC Securities Corporation (dated July 25, 2013); and (3)

[3] We recognize that the current proposed rules originated in 2008 as part of the FINRA consolidation process and that the Dodd-Frank Act was enacted afterwards. Still, the underlying concepts of that Act should not be ignored.

Mr. Steve Putnam of Raymond James Financial Services (dated July 25, 2013), yet we see other items that should be addressed.

Supplementary Materials

Without explanation, FINRA engages in rule-making through the guise of Supplementary Materials, ostensibly to clarify the proposed rules. Resort to surreptitious rule-making in the Supplementary Materials is needlessly confusing and these substantive provisions should be in the rules themselves. FINRA has further totally ignored the costs of implementing these new rules. The Proposed Rules have been modified since 2008, when initially proposed, and again in 2011, when further revisions were made. FINRA is now proposing that a firm with only a single registered person (a "One-Person OSJ") have its on-site principal "...under the effective supervision and control of another appropriately registered principal ('senior principal')." The senior principal is expected to "...conduct on-site supervision of such OSJ on a regular periodic schedule determined by the member."[4] Among the stated factors, which are not exclusive, to be used by the member to establish the examination schedule for the senior principal are:

(1) the nature and complexity of the securities activities conducted at the location;

(2) the nature and extent of contact with customers; and

(3) the disciplinary history of the on-site principal.[5]

But there are no guarantees that a senior principal can effectively understand the operations of the firm, which, in the ordinary course, evolve in response to business conditions, nor that such person will properly evaluate what he or she reviews, no matter how regularly his or her visits are scheduled. We doubt that a senior principal would have been able to stop Bernie Madoff, who apparently maintained at least 2 sets of books. FINRA is setting up an unworkable

4 SEC Release No. 34-69902, p. 6.
5 Id.

set of requirements that keeps spinning along regardless of how people actually function in their respective firms.

In another situation, the Supplementary Materials detail what is likely the most pervasive situation for smaller firms operating out of multiple locations, generally with no more than a handful of Associated Persons at each such location. Where, formerly, a single principal may have supervised multiple OSJs, FINRA now mandates that an on-site principal be designated to supervise each such OSJ, "...on a regular and routine basis."[6] FINRA has created a "general presumption that a principal will not be assigned to supervise more than one OSJ."[7] Moreover, if a member decides to assign one principal to supervise more than two OSJs, that decision is not only presumptively unreasonable, but will also subject the member to greater regulatory scrutiny. The Supplementary Materials list five non-exclusive factors to guide a member in implementing this "non-rule rule." FINRA further requires (in the Supplementary Materials) a member to document the factors it used to determine why its supervisory structure is reasonable.

These two scenarios impose greater expense on smaller firms regardless of the nature and complexity of the member's business, regardless of the extent of customer contact and regardless of the member's disciplinary history. FINRA is disregarding its own stated criteria for making such assessments and imposing, on a one-size, generic basis, needless costs on members and their Associated Persons. Large firms can hire more compliance people to deal with these "non-rule rules." Small firms cannot afford it.

Seemingly, the Proposed Rules were drafted in a laboratory where seniority is relied on as the sole criterion to provide checks and balances in member oversight. These rules do not

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6 Id.

7 SEC Release No. 34-69902, p. 7. (Emphasis added.)

reflect the reality of broker-dealer operations. For example, take the situation where the most senior person in the firm occasionally produces revenue; are compliance professionals in the firm precluded from reviewing the senior person's activities? Proposed Rule 3110(b)(6) might force a firm, under these circumstances, to hire a "senior principal" if the senior person in the firm may determine the compliance person's compensation and/or continued employment with the firm. How many times can this so-called hot potato issue be passed around the circle, and at what cost? We laud the concept of checks and balances, but note that the US Government has 3 co-equal branches. FINRA has instead created an endless circle of ever-tightening loops.

A more constructive approach would be to differentiate among the categories of clients a particular firm serves, as well as the scope of its business. FINRA says that these are relevant factors, but ignores those very factors in the Proposed Rules themselves. Transactions with retail customers are more likely to require greater supervision than those with institutional and high net worth individual clients. Firms that conduct general sales activities are more likely to generate customer complaints than a firm that provides investment banking services to institutions, or wholesales investment products or trading algorithms to other broker-dealers. Instead, FINRA focuses on the number of supervisors a firm has, as though quantity could ever be used as a proxy for complexity or exposure. One is hard-pressed to defend FINRA's total disregard of these critical business differences in the Proposed Rules. What FINRA has proposed is a needlessly cumbersome and complicated supervisory structure without any commensurate cost-benefit or improvement in compliance. In fact, we believe that merely adding compliance officers, even if very experienced and knowledgeable, likely creates more problems than it solves. Who watches the watchers?[8]

Bricks and Mortar

FINRA is operating in a vacuum of its own making. It is seeking to consolidate outdated rules, drafted many years ago in a bricks and mortar world. The way the broker-dealer world operates has changed significantly since NASDR evolved into FINRA. Moreover, once FINRA was formed, in 2007, NYSE rules largely froze as of that year. FINRA is laboriously trying to reconcile a bricks and mortar approach to regulation where firms are now operating electronically and virtually. Even FINRA operates in an electronic environment, where filings are made through its Gateway and then accessed remotely. Determining adherence to rules and regulations is not necessarily going to be learned by visiting an office. For example, many salespersons and investment bankers travel extensively to meet with client companies and are rarely found in their nominal offices; many operate from their homes and rarely visit a branch or main office of their firms. Review of their e-mail is a far more effective way to identify potential red flags than visiting such a person's home. We suggest that a home office visit in such situations is comparable to visiting a firm's server to see where its e-mails are stored. What could possibly be learned from such purported inspections? FINRA simply doesn't get it!

"Covered Accounts"

We strongly urge FINRA to follow SIFMA's analysis and recommendations with respect to the expanded definition of "covered accounts" and the unnecessary compliance burdens this definition creates. We only add the observation that by focusing on the minutiae of who may be

[8] The Release does not consider whether a firm may, for costs reasons alone, decide to outsource some or all of these newly-mandated supervisory reviews. See, Notice to Members 05-48.

deemed to own a covered account, FINRA, once again, is disregarding the risk-based principles it nominally espouses. The criteria should be the tests FINRA says it is using, namely, the ability to influence/make investment decisions or financial dependence, not who owns the account. Even a spouse could establish that he or she makes independent investment decisions. Ownership muddies the waters because it is not a risk assessment factor.

Disparity Between Risk-Based Principles and Implementation

Our experience with the firms to which we provide compliance services indicates a huge disparity between FINRA's stated principles and the actual practice of FINRA examiners during a routine firm examination. All too often an examiner's opinion diverges from that of the principals of the firm, with the examiner insisting on his or her interpretation rigidly and capriciously. A beneficial rule for firms and examiners alike should state that if a firm's procedures are reasonable in light of the scope of its business, the extent of its customer contact and its disciplinary history, and are properly documented, they should be presumed to be acceptable to FINRA examiners.

Our Recommendations

Incorporate the Supplementary Materials into the Proposed Rules

FINRA is to be commended for proposing risk-based, also called (by FINRA) principles-based, rules that purportedly differentiate among firms based on a firm's size, resources and business model. Essentially, we agree with FINRA's theoretical approach, but believe FINRA has not followed its own guidelines in the Proposed Rules.[9] We remain concerned about the implementation of these principles, particularly with respect to smaller firms. FINRA has been

9 FINRA has cleverly avoided a rule-making problem by using Supplementary Materials to impose requirements not stated in the rule itself.

somewhat disingenuous in its use of Supplementary Materials. We recommend that FINRA use a more honest and forthright approach to rule-making to benefit its members.

Standardized WSPs

In addition, FINRA could affirmatively help firms meet their compliance responsibilities by drafting standard, pro forma, base line WSPs that can be adapted, if necessary, by each firm. Currently, something approaching regulatory guidance for drafting WSPs has been provided by the NFA for CPOs (commodity pool operators) and CTAs (commodity trading advisors), among other entities it regulates. http://www.nfa.futures.org/nfa-compliance/publication-library/regulatory-requirements-guide.pdf

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Thank you for the opportunity to comment on the Proposed Rules. Should you have any further questions, please feel free to call Howard Spindel at 212-897-1688 or Cassondra Joseph at 212-897-1687, or contact us by e-mail at **hspindel@intman.com** or **cjoseph@intman.com,** respectively.

Very truly yours,

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