Lincoln Financial Network®
A member of Lincoln Financial Group

Carrie L. Chelko, Chief Counsel
Lincoln Financial Network
3400 One Commerce Square
Philadelphia, PA 19103
484-583-1413
carrie.chelko@lfg.com

April 17, 2014

Via Electronic Mail (rule-comments@sec.gov)
Elizabeth M. Murphy, Secretary
United States Securities and Exchange Commission
100 F. Street, NE
Washington, D.C. 20549-1090

Re: File Number SR-FINRA-2014-010

Dear Ms. Murphy:

Lincoln Financial Network ("LFN" or "Lincoln") appreciates the opportunity to submit this comment letter in response to the Financial Industry Regulatory Authority's ("FINRA") Rule 2243 rule filing. Lincoln Financial Network is the marketing name for Lincoln Financial Advisors Corp. (LFA) and Lincoln Financial Securities Corp. (LFS), two broker-dealers and registered investment advisors affiliated with Lincoln Financial Group (LFG).[1] Currently, LFN maintains an affiliation with over 8,500 advisors, which include registered representatives, investment advisor representatives, insurance brokers and agents.

LFN frequently recruits advisors from other FINRA broker-dealers and offers advisors an open architecture business model, allowing them the ability to offer a variety of investment products, including securities (e.g., stocks, bonds, mutual funds, variable annuities), advisory services, and non-securities products (e.g., fixed annuities and life insurance, including insurance sold by insurance companies others than LFG). As part of its recruitment efforts, LFN may offer forgivable loans to advisors to offset the expenses that advisors incur when transitioning. While LFN supports FINRA's overall efforts to protect investors and better regulate conflicts of interests in these types of recruitment and transition situations, LFN is concerned that Rule 2243 goes too far and is not appropriately tailored to address harm to investors and conflicts perceived by FINRA.

I. Economic Impact Assessment & Anti-Competitive Consequences

In September 2013, FINRA issued a public statement describing their framework for conducting an economic impact assessment when new rules are proposed. FINRA's framework, authored by the Office of the Chief Economist, is intended to ensure that FINRA rule proposals are better designed to protect the investing public and maintain market integrity, while

[1] The affiliated companies of Lincoln Financial Group act as issuers of insurance, annuities, retirement plans and individual account products and services. The affiliates include, but are not limited to the Lincoln National Life Insurance Company ("LNL") and Lincoln Life and Annuity Company of New York ("LLANY").

minimizing unnecessary burdens. FINRA has outlined three core principles to support its economic impact assessment: (1) consult with key stakeholders in the development of rules, (2) provide clarity about the objectives and potential impacts of rule proposals and alternatives considered and (3) obtain supporting evidence where practicable. With respect to the third core principle, FINRA has explained the following:

> Economic impact assessments seek to identify and anticipate how markets and market participants will alter their behavior in response to a new rule. To do this, it is important to assess who a proposal impacts (*e.g.*, investors, brokers, others), what participants will be required to do to implement a rule (*e.g.*, firms developing a new system to capture and deliver required disclosures), the costs and benefits of new compliance activities, and how behaviors will change (*e.g.*, investors will be better advised of a conflict and will take more care in making decisions).[2]

The Securities and Exchange Act of 1934 contains clear prohibitions for SROs, like FINRA, from promulgating any rules that unnecessarily impose any burdens on competition. See 15 U.S.C. § 78o-3(9). FINRA has stated that the proposed rule change will not result in any burden on competition that is not appropriate to further the purposes of the Securities Exchange Act of 1934 ("Exchange Act"). This very statement recognizes that competition will be impacted, though FINRA believes the burden to be appropriate.

Lincoln is concerned that FINRA has done little, if anything, to assess how proposed Rule 2243 will burden competition or whether it will have unintended anti-competitive consequences. Consistent with the economic assessment principles, FINRA should assess what impact Rule 2243 would have on market participants, including registered representatives, and how this Rule proposal could influence their decision to change employers.

A. Impact on registered representatives

Rule 2243 may constructively operate as a restrictive covenant that binds a registered representative to his or her current employer, especially if a registered representative feels restrained from transitioning to another member firm because of the onerous disclosure requirements that are not required of other registered personnel in the industry. From a public policy perspective, courts frown on restrictions that eliminate or negatively impact an individual's freedom of choice or movement to another employer.

Additionally, the current rule-making and regulatory comment process does not always reach those market participants most impacted by the rule proposal. Generally, trade associations, FINRA member firms, and attorneys are comfortable with the advocacy and rule-

---

[2] See FINRA *News Release* (Sept. 19, 2013) <http://www.finra.org/Newsroom/NewsReleases/2013/P346388>.

making process. However, very few financial advisors (of the approximately 253,000 active and producing registered representatives) participate in the comment process. LFN analyzed data from Discovery Data, an Ipreo Company, and found that approximately 26,000 registered retail advisors changed firms in 2013.[3] This is a significant number of market participants that could be impacted by implementation of Rule 2243.

FINRA should engage not only broker-dealers but also registered representatives, especially those who may have recently moved firms, to fully understand what impact Rule 2243 would have on their employment decisions. An industry-wide survey, sweep or inquiry, which is designed to elicit feedback on whether the specific disclosures in Rule 2243(a)(1) would influence a registered representative's decision to move to another broker-dealer. This type of an assessment is not only appropriate, but is practicable and advisable. Truly, the best indicator of whether competition would be unnecessarily or unfairly burdened would be the registered representatives who are required to provide the Rule 2243 disclosures to retail investors whom they service. These same registered representatives are also best situated to provide feedback on alternatives available to FINRA.

B. Impact on member firms

FINRA member firms, like registered representatives, will also be impacted by Rule 2243 in unbalanced ways. There are clusters of FINRA member firms that will derive clear benefits from this rule and clusters that will be disadvantaged by this rule. For example, the wirehouses, who have uniformly supported this rule, will be advantaged on three fronts. First, they will continue to gain market share through decreased attrition. Financial advisors are less likely to move firms in order to avoid the Rule 2443(a)(1) intrusive and sensational disclosures of their compensation levels. Second, the recruitment compensation packages, which have grown over the last decade at wirehouses, are likely to recede so that advisors can avoid disclosing compensation levels. Third, they and their registered representatives would not need to disclose additional incentives these registered representatives receive to retain client accounts and assets managed by departing registered representatives. The practice of providing additional incentives to retain client accounts and/or assets is a common practice in wirehouses.

Some smaller firms and independent broker-dealers have argued that this disclosure rule will "level the playing field," thus validating the competitive impact of this rule proposal. Historically, broker-dealers in these footprints offer higher payouts rather than significant recruitment or transition compensation. Accordingly, these member firms may attract advisors who will opt for greater payouts rather than the sensational disclosure of compensation.

Regional firms are likely to be a disadvantaged group of FINRA member firms. These firms offer transition compensation to advisors on a smaller scale than wirehouses and are,

[3] See Rep Movement Study from 2009-3Q2013, Discovery Data, an Ipreo Company (Feb. 2014) <www.discoveryco.com>.

oftentimes, more attractive to financial advisors and clients because of their full- and individualized-service models. Again, financial advisors will likely avoid movement to these institutions to avoid the specific disclosure obligations.

On the other hand, LFN, as an independent broker-dealer, may benefit from this FINRA rule, corroborating the concern that FINRA's proposed rule needs to be evaluated by the Commission for the industry-wide impact on competition. FINRA should evaluate alternatives that would not unnecessarily burden competition. For example, a general disclosure (rather than a specific dollar value range) revealing that transition compensation was received by the registered representative can also serve the purpose of engaging a client about potential conflicts of interest. The Commission should reject this rule and, instead, encourage FINRA to identify those alternatives and redraft the proposal in a competitively neutral manner.

C. Movement to RIAs

LFN is also concerned that the regulatory inconsistencies governing broker-dealers and registered investment advisers (RIAs) may also exacerbate the competitive concerns associated with this rule proposal. Registered representatives may feel less inclined to move to a FINRA regulated competitor because of the prescriptive disclosure requirements. This rule could further fragment the brokerage and investment advisory industries and serve to encourage the defection of registered representatives from FINRA member firms to RIAs, which would not require such burdensome, sensational and detailed disclosures on compensation.

II. Rule Inconsistent with Restrictive Covenant Laws

In the rule proposal, FINRA advocates that any action taken by a recruiting firm or representative that attempts to induce former customers to transfer assets should trigger the disclosures. More specifically, FINRA proposes that actions such as "a tombstone advertisement, a general announcement or a billboard, would be considered an attempt to induce former customers to move their assets", thus triggering the duty to disclose the recruitment compensation. FINRA's proposal appears to stop short of requiring a registered representative to disclose his or her compensation in a local newspaper or on a billboard. It does, however, overreach by reversing decades of industry-developed common law holdings that tombstone advertisements and generalized announcements are not deemed solicitations or inducements.

III. Individual Privacy & Safety Implications

Proposed Rule 2443 requires the disclosure of any payments in excess of one hundred thousand dollars. Unlike the precise dollar value disclosure (e.g., $624,654) proposed in Regulatory Notice 13-02, FINRA's new rule proposal requires the disclosure of payments falling in certain ranges. The proposed ranges are (a) $100,000 to $500,000, (b) $500,000+ to $1 million, (c) $1+ million to $2 million, (d) $2+ million to $5 million, and (e) over $5 million. FINRA modified the specificity requirement purportedly to reduce the privacy and safety concerns, noting that the investor protection benefits outweigh the privacy and safety of registered representatives. This modification is a distinction without a difference and it does little to remediate the privacy and safety concerns of registered representatives.

FINRA has indicated that the disclosure requirements are "intended to prompt a dialogue between the former customer and the registered representative . . . [on] the impact of a decision to transfer assets to a new firm."[4] However, the disclosures cannot be restricted to only those former customers who are evaluating whether to transfer assets. The disclosures can be disseminated and seen by countless other individuals, even non-investors, triggering privacy and safety concerns of registered representatives. FINRA has failed to substantively address commenters' concerns about privacy and has dismissed these concerns, providing only unsubstantiated conclusions.

The privacy and safety concerns are real. The rule proposal does little to protect this information from reaching individuals beyond those who were intended to receive the disclosures. Broker-dealers are obligated under SEC Regulation S-P to protect the dissemination of non-public information, including an investor's net worth, even when the net worth is not specifically disclosed, but is disclosed in a range, similar to that proposed by Rule 2443(a)(1). However, there are no mechanisms identified by FINRA for ensuring that investors have the same undertakings. Taken to an extreme, there is nothing stopping an aggrieved firm, a competitor representative or a disgruntled investor from posting highly sensitive compensation information on a social media forum like FaceBook, LinkedIn or Twitter. FINRA should not dismiss these concerns outright without conducting an impact assessment on potential for widespread dissemination of sensitive compensation, loan or payment information

IV. Alternatives to Mitigate Conflicts of Interests

In Regulatory Notice 13-02 and as part of the Rule 2243(a)(1) commentary, FINRA advocates that the payment disclosure requirements are necessary to identify and mitigate conflicts of interests. Further, FINRA suggests that specific compensation ranges need to be disclosed to customers so that they have a sense of the "nature and magnitude" of a representative's recruitment compensation.[5] This implies that the "magnitude" of the payment equates with the magnitude of the potential conflict of interest. A conflict is a conflict, regardless of magnitude. Further, there are methods to remediate or mitigate conflicts without sensationalizing compensation through specific disclosures.

In October 2013, nine months after Regulatory Notice 13-02 was issued, FINRA published its *Report on Conflicts of Interest* ("*Report*").[6] Surprisingly, Regulatory Notice 13-02 and the tenets of proposed Rule 2443 were not discussed in this *Report*. However, reference was

---

[4] See Notice of Filing of Proposed Rule Change to Adopt FINRA Rule 2243, Fed. Reg. Vol. 79, No. 60. 17592, 17595 (Mar. 28, 2014).
[5] Id.
[6] See FINRA *Report on Conflicts of Interest* (Oct. 14, 2013) <http://www.finra.org/web/groups/industry/@ip/@reg/@guide/documents/industry/p359971.pdf>.

made to other compensation practices that may create conflicts (e.g., excessive trading to reach recognition club levels or qualify for bonuses). FINRA's *Report* recognizes that many firms have adequate conflicts management frameworks and effective practices to identify and remediate conflicts. Firms utilize a range of enhanced monitoring, surveillance and heightened supervision to identify and mitigate conflicts, including those relating to compensation. Firms also have the ability to structure payments and compensation so that compensation is not based on revenues generated from customer accounts.

FINRA concluded that there is no "one-size-fits-all" framework to managing conflicts.[7] Yet, in this circumstance, FINRA is prescribing specific disclosure requirements for perceived conflicts that can certainly be identified and mitigated through the different and "effective" frameworks described in the *Report*.[8] FINRA Rule 2243(a)(1) is unnecessary because there are adequate alternatives to disclose and mitigate conflicts. LFN supports FINRA's efforts to reduce conflicts and provide meaningful, plain English disclosures to address those conflicts. However, the rule proposal, as drafted, is not appropriately tailored to address the perceived conflicts and harm to investors.

V. Business Conduct Abuses & Sales Practice Violations

FINRA also advocates that the proposed rule is consistent with the provisions of Section 15(A)(b)(6) of the Securities Exchange Act ("Exchange Act"), which requires, among other things, that FINRA rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. However, FINRA's rule proposal appears to be more of a solution in search of a problem, as there is little evidence that the Rule remediates recognizable fraudulent or manipulative acts or practices.

FINRA also wants to gather specific compensation information so that it can utilize the information in its risk-based examination program and to evaluate member firms' conflict management processes.[9] The compensation data has been available to FINRA for years, yet there has been little regulatory activity in this area. There are no widespread enforcement actions, sweep examinations or inquiries which point to significant sales practice or business conduct abuses in this area.

The most notable recent regulatory guidance was issued in August 2009 when SEC Chairman Mary Schapiro sent a letter to firms reminding them of their supervisory obligations during the recruitment process.[10] Many firms strengthened their oversight following Chairman Schapiro's letter. Since then, an assessment of the regulatory activity and guidance in this area

---

[7] Id. at 36.
[8] Id. at 30-31.
[9] See Notice of Filing of Proposed Rule Change to Adopt FINRA Rule 2243, Fed. Reg. Vol. 79, No. 60. at 17596 (Mar. 28, 2014).
[10] See Chairman Schapiro Letter (Aug. 31, 2009) <http://www.sec.gov/news/press/2009/2009-189-letter.pdf>.

would suggest that the control environments of broker-dealers are adequate. There is little FINRA examination activity around the recruitment practices that Firm's employ. FIRNA frequently issues investor alerts to educate investors on matters of importance or conflicts of interest. Interestingly, there have been no investor alerts issued by FINRA to prompt investors to have a dialogue about their recruitment compensation. Further, there are few, if any, enforcement actions that relate to the very conduct that FINRA believes needs to be regulated. As such, the Commission, when determining whether to approve FINRA's rule proposal, should consider whether this rule is not only fair and balanced, but whether the rule is necessary to remediate a genuine harm that is plaguing the industry and harming investors.

VI. Conclusion

LFN is supportive of FINRA's efforts to provide investors with a more complete picture of the factors involved in a decision to transfer assets to a new firm. LFN is also supportive of customer engagement and a dialogue of the factors that motivated a registered representative to change employers. Additionally, LFN generally supports FINRA's efforts to reduce conflicts of interest where they exist and provide meaningful, plain English disclosures to address those potential conflicts.

However, FINRA's rule proposal goes well beyond what is necessary and reasonable to accomplish the stated purposes. In fact, FINRA has not articulated a strong, much less compelling, basis for the necessity of this rule. In that regard, there has been no demonstration of customer harm or an industry-wide misconduct that would substantiate the need for rulemaking. The dearth of enforcement actions and regulatory settlements support a conclusion that the current mechanisms and controls are effective and that this rule proposal is more akin to a solution looking for a problem, rather than a solution to a problem.

If there truly are conflicts or if additional disclosures would assist a customer in his or her decision-making, alternatives to the current rule proposal are available. A specific disclosure of ranges of compensation is unnecessary and general disclosures, in a fair and balanced manner, would be sufficient. Further, FINRA should ensure that additional disclosures impacting a customer's choice of firms are also addressed in this rule proposal so that the rule is balanced and inclusive. For example, this rule does not address retention bonuses that a registered representative might receive in order to stay with a firm. In addition, this rule does not address compensation that might be received by a registered representative who takes over servicing a customer's account in order to retain customers of a departed registered representative. Again, conflicts attendant to these situations could also impact a customer's choice of firms and can be mitigated through general disclosures.

LFN recommends that FINRA conduct a pilot program with the wirehouses, who have uniformly supported proposed Rule 2243, and those smaller firms and independent broker-dealers who have argued that Rule 2243 will "level the playing field". This pilot program should test whether this proposed rule would have any meaningful benefit to retail consumers and/or would effectively stifle competition between member firms for financial advisors. This pilot program should also form a component of the economic impact assessment discussed in Section I above.

Finally, and perhaps most importantly, LFN encourages the SEC and FINRA to conduct an appropriate economic impact assessment, obtain evidence and identify reasonable alternatives, after fully engaging all impacted market participants. LFN looks forward to a continuing dialogue with FINRA in the hopes that FINRA can identify alternate, more reasonable solutions than those that are currently proposed in Rule 2243. If you have any questions, please do not hesitate to contact me at 484.583.1413 or carrie.chelko@lfg.com.

Respectfully Submitted,

Carrie L. Chelko, Esquire
Chief Counsel
Lincoln Financial Network