Cetera FINANCIAL GROUP

April 27, 2023

VIA ELECTRONIC MAIL (rule-comments@sec.gov)

Ms. Sherry R. Haywood
Assistant Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: File No. SR-FINRA-2023-006: Revisions to FINRA Rule 3110

Dear Ms. Haywood:

I write to offer comments on behalf of Cetera Financial Group ("Cetera") with respect to a rule proposal from the Financial Industry Regulatory Authority Inc. ("FINRA").[1] The proposed rule amendments would add Supplementary Material to FINRA Rule 3110.19 and revise the method for classifying certain branch locations of FINRA member firms. We will refer to the proposed amendments as the "Proposal".

Cetera is the corporate parent of four FINRA member firms with nearly 9,000 registered representatives doing business in all fifty states. We have large numbers of both branch offices and supervisory personnel who operate from locations that are physically separate from those of the individuals whose activities they supervise. The effects of the Proposal would be significant to Cetera and many other firms that are similarly situated.

FINRA Rule 3110 currently provides that if an associated person of a member firm performs supervisory activities from a branch location, that location is deemed an Office of Supervisory Jurisdiction ("OSJ"). Among other things, it is subject to inspection on a more frequent basis than other types of branch locations. The Proposal would add Supplementary Material .19 to Rule 3110, and create a new branch classification: The Residential Supervisory Location, ("RSL"). It would generally provide that a branch location would be classified as an OSJ only if specified activities are performed there. It would also limit eligibility by excluding certain locations from RSL classification based on the status of the firm or other events with which it or associated person have been involved.

FINRA put forth an earlier version of the Proposal in 2022. It was similar in most respects, but the current iteration adds significant new restrictions on the ability of firms to classify branches as RSLs. Cetera has been supportive of the Proposal, and we continue to believe that it represents a necessary and appropriate step in updating FINRA rules that no longer fully reflect how the securities industry operates, particularly with respect to physical presence of staff members. The provisions of the original Proposal generally struck a reasonable balance between re-envisioning an outdated system

[1] [1] Proposal to Adopt Supplementary Material .19 (Residential Supervisory Location), 88 FR 20568 (Mar. 31, 2023). https://www.govinfo.gov/content/pkg/FR-2023-04-06/pdf/2023-07145.pdf.

655 W Broadway, 12th Floor
San Diego, CA 92101

and preserving essential elements of investor protection. In particular, not allowing branches offices of firms that are subject to the provisions of FINRA Rules 3170 and 4110 is appropriate and directly related to enhancing investor protection. Similarly, not allowing individuals who are subject to heightened supervision to operate in RSLs makes sense. However, the new version of the Proposal would create additional restrictions on the ability of firms to classify branches as RSLs that are not reasonably related to the substance of the Proposal or investor protection. They should be eliminated or narrowed before further action.

1. **Any final rule should eliminate the provision making a location ineligible for RSL status simply due to the fact that a supervisor has not been employed in a supervisory position with the member firm for at least one year.**

Supplementary Material 3310.19(c)(1) provides that in order to eligible for classification as an RSL, all individuals performing supervisory functions at that location must have been doing so on behalf of the member firm for a minimum of one year. Cetera and a number of other commenters took issue with this provision in the original iteration. It is arbitrary and not reasonably related to the purposes of the Proposal. Branches would be ineligible for classification as an RSL simply because individual supervisors who may have been employed by the member firm for many years but who have previously either performed functions not directly related to supervision were not formally designated as supervisors. In addition, branches that house supervisors who have a lot of experience in supervisory roles with other member firms but have been employed by the current member firm for less than one year would be ineligible for RSL status.

In the text accompanying the Proposal, FINRA makes the following statement: "*While it is possible that an associated person may have prior supervisory experience from another firm, a new supervisor at the current member firm may need time to become knowledgeable about that firm's systems, people, products, and overall compliance culture.*"[2] This may or may not be accurate, but it is not accompanied by any objective evidence and is completely at odds with the comments received from most of the interested parties, particularly member firms who have direct experience in hiring and training supervisory personnel. We are not aware of any other provisions in the FINRA rules that apply a specified period of time for qualification to do anything. As soon as an individual passes the necessary qualification examinations, they can begin performing their functions immediately. The applicable time period in the Proposal could as easily be three months or three years. It is not supported by any objective evidence and can only be characterized as arbitrary.

This provision also creates practical problems for member firms in hiring and retaining supervisors. The COVID-19 pandemic was a terrible event, but it forced all FINRA member firms to adapt to a fully-remote working environment. It also allowed member firms to recruit, train, and manage staff who were not located in the geographic locations where the firm maintained physical branch offices. This was and is a material benefit to member firms, employees, and ultimately to customers who received the benefits of more effective supervision.

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[2] 88 FR 20578.

It allowed member firms to hire the best and most experienced staff members without regard to geographic location, and allowed employees the flexibility to live where they chose.

If a member firm wishes to hire a supervisor in a remote location, the arbitrary one-year requirement will prevent them from classifying their residence as an RSL for at least one year, which may prevent the firm from hiring the individual. Similarly, if a member firm has an employee working in a non-OSJ location and performing non-supervisory functions, in order to shift their responsibilities to include supervision it would be forced to designate the branch location as an OSJ for a period of one year. The benefits of this are minimal and do not outweigh the burdens.

2. **The provision making a branch location ineligible for designation as an RSL if an associated person is the subject of certain proceedings is neither reasonable nor practicable and should be deleted from the Proposal.**

Rule 3110.19(c)(6) provides that a branch location would be ineligible for designation as an RSL if one or more associated persons at that location "…are currently ***subject to***, or have been notified in writing that they will be subject to, any ***investigation, proceeding, complaint*** or other action by the member, the SEC, an SRO, including FINRA, or state securities commission (or agency or office performing like functions) ***alleging*** they have failed reasonably to supervise another person subject to their supervision, with a view to preventing the violation of any provision of the Securities Act, the Exchange Act, the Investment Advisers Act, the Investment Company Act, the Commodity Exchange Act, any state law pertaining to the regulation of securities or any rule or regulation under any of such Acts or laws, or any of the rules of the Municipal Securities Rulemaking Board or FINRA**."**[3] **(Emphasis added.)**

The breadth of this provision is somewhat remarkable, and, we believe, would be unique among FINRA rules. It would prevent a member firm from designating a branch as an RSL if any individual working in it is subject to an "investigation" or "complaint", neither of which is adequately defined. The securities industry is unusual in that it requires associated persons to report allegations of securities-related matters without regard to their accuracy or veracity, without formal adjudication, and with public notice that may last years past dismissal or resolution. This has always struck many people as unfair, but it has been in place for a long time and most associated persons have accepted it. However, the provisions of Rule 3110.19(c)(6) take this concept to another level by providing that if an associated person is the subject of a complaint or investigation that alleges a failure to supervise another person subject to their supervision, the branch location in which they work could not be designated as an RSL.

This raises a number of issues. The term **"the subject of"** is too broad and too vague to allow member firms and associated persons to apply it with any degree of confidence. It is common for

[3] 88 FR 20577.

customers of FINRA members or others to make allegations against associated persons that are inaccurate or lacking in detail sufficient to determine who might have been culpable or even involved. We can easily envision a circumstance in which an individual supervisor is referred to in a customer complaint only by status, but which results in an investigation by a regulatory agency. It unfairly shifts the presumption from innocence to guilt without any form of substantive finding, much less adjudication. On a more practical level, investigations by regulatory agencies often go on for multiple years without resolution. Placing individuals and member firms in this sort of perpetual limbo is neither fair nor practicable.

If a provision of this type is to is to be included in any final rule, it must be much more limited and specific. It should provide that RSL eligibility would only be precluded if the associated person has been notified by a regulatory agency, in writing, that the agency intends to take or recommend enforcement action against the individual for failure to perform supervisory responsibilities. A model for this already exists, in the form of "Wells" notices that are provided to the subjects of possible enforcement action by the SEC and FINRA. Most states do not have analogous provisions, and the processes that they follow vary widely. A safeguard such as this should be a minimum requirement.

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Cetera continues to support the majority of the RSL proposal, but we are concerned about the aspects mentioned above. They should be amended or removed before proceeding further.

If you have questions or we may offer any further information with respect to our comments or this topic in general, please do not hesitate to contact me. My thanks for your consideration.

Sincerely,

Mark Quinn
Director of Regulatory Affairs
Cetera Financial Group