

May 23, 2014

BY EMAIL To: (pubcom@finra.org)

Marcia E. Asquith
Office of Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

RE: FINRA Regulatory Notice 14-14
Retrospective Rule Review
(Communications with the Public)

Dear Ms. Asquith,

Charles Schwab & Co., Inc (“Schwab”) appreciates the opportunity to express its views on FINRA’s rules governing communications with the public and their effectiveness and efficiency as intended to meet investor-protection objectives.

Schwab supports FINRA’s initiative to retrospectively review the communications with the public rules and shares FINRA’s belief that it is appropriate to look back at certain rules to determine whether the existing rules are meeting their intended objectives in light of industry changes. Schwab believes this review offers an important opportunity to consider modifications to the rules with the intent of avoiding undue administrative and expense related burdens on member firms while still achieving investor protection. Our comments include the following, all of which are discussed in greater detail below:

- I. Consideration to revise the category definitions under FINRA Rule 2210(a) for greater clarity to avoid potential unintended consequences of an overly broad application of the language within the rule.
- II. Proposed modifications with respect to FINRA filing requirements and exemptions.
- III. Application of disclosure language with respect to specific product offers.
- IV. Communication of FINRA rule interpretations and transparency of comments.

I. Communications with the Public Category Definitions

FINRA Rule 2210(a) currently defines the three categories of communications with the public as correspondence, institutional communications and retail communications. Each specific category contains the following language excerpted from within the definition “means any written (including electronic) communication.” We believe that as written, the rule is overly broad since broker-dealers distribute written and electronic communications in the course of

conducting business to both retail and institutional investors that appear to fall outside of these categories.

As written, FINRA Rule 2210(a) implies that *any written or electronic communication* must fall into one of the three categories. In essence, the definitions take a “one size fits all approach” to communications distributed by member firms without taking into account the complexities of the firms structure and the broad types of communications, documents and other materials that they are required to distribute or make available to investors. These can include, but are not limited to, forms used to open and maintain client accounts, tax related communications, privacy notices, generic references with respect to corporate branding, website content that includes order entry screens, etc. We believe these types of materials should not be subject to the existing three categories and feel it is likely that some or all of these materials are being supervised inconsistently under FINRA Rule 2210 by member firms as an unintended consequence of the current text of the rule. For the purposes of this letter, such documents will be collectively referred to hereafter as other broker-dealer materials.

In Regulatory Notice 14-14 (“the Notice”), FINRA asks if the rules effectively addressed the problem(s) they were intended to mitigate and what ambiguities and challenges firms have found with the rules. We believe that the overly broad definitions coupled with the text of FINRA Rule 2210(b)(1)(D)(iii)¹ which requires supervision of those *retail* communications that do not make any recommendations or promote member products or services has not addressed the problems and has actually created additional challenges and potential unintended consequences. These challenges may include, but are not limited to, unnecessary policies and procedures designed to supervise all written and electronic communications as falling into one of the categories. The content standards of FINRA Rule 2210(d) will need to be applied to all communications and may be impractical given the nature of other broker-dealer materials. We do not believe that FINRA Rule 2210(b)(1)(D)(iii) was intended to be a supervisory catchall rule for *any* communications a member may distribute or make available.

The Notice requests that member firms provide specific suggestions as to how the rules should be changed. We suggest that FINRA consider revising Rule 2210(a) to remove the word “any” from the category definitions and specifically include the types of communications that more appropriately fall into these categories while clearly defining the types of communications that are excluded from these category definitions. FINRA should examine the applicability of FINRA Rule 2210(b)(1)(D)(iii) based upon any revisions that may be considered to Rule 2210(a). We believe that this rule exists in part because during the implementation of FINRA Rule 2210 there was a need to allow firms to continue to distribute market letters without the unnecessary delays of requiring prior approval. We further believe that a rule can be incorporated into 2210(b)(1) that addresses this and preserves a firm’s ability to continue to distribute without prior approval provided that effective supervisory controls are in place similar to the prior treatment of market letters under NASD Rule 2211.

¹ FINRA Rule 2210(b)(1)(D)(iii) exempts retail communications that do not make any financial or investment recommendation or otherwise promote a product or service of the member from approval by a registered principal prior to use provided that the member supervises and reviews such communications in the same manner as required for supervising and reviewing correspondence pursuant to NASD Rule 3010(d).

II. Filing Requirements

Schwab appreciates that FINRA Rule 2210 exempted certain communications from requiring filing requirements; most notably, removing the prior filing requirement for communications concerning government securities. Rule 2210 also provided a filing exemption for retail communications that are posted on an online interactive forum. However, we believe that it would be beneficial to modernize the filing requirements to be principles-based where communications that are higher in risk would require filing and lower risk communications would be excluded from filing.

Member firms that file a substantial amount of communications are subject to the time and expense associated with required filings, which includes the cost of the filing and the time spent submitting communications for review. Filing fewer communications with FINRA Advertising Regulation will allow FINRA to more efficiently use its resources to concentrate on providing meaningful comments and more efficient response times to member firms concerning complex and high-risk communications that have the potential for investor harm.

FINRA should consider revisions to FINRA Rule 2210(c)(7) to include retail communications that meet the standards set forth under Rule 135a of the Securities Act of 1933² (“the 1933 Act”) as well as closely examining the filing requirements imposed on member firms per the standards set forth under FINRA Rule 2210(c) with a goal of a *principles-based filing requirement largely based upon risk* versus the current rules that cause firms to file large volumes of low-risk retail communications. We believe consideration should be given to revising the filing requirements as follows:

1. Communications that are subject to the limitations of Rule 135a (“Rule 135a communications”) are often used by member firms to provide generic explanatory information to the public concerning various types of investment companies and cannot be used to offer specific securities. For example, explanatory information relating to different types of funds, including their various investment objectives, i.e., balanced funds, bond funds, etc. and within the limitations of Rule 135a trigger filing with FINRA Advertising Regulation when not posted on an online interactive forum given the restrictive filing requirements firms must comply with under FINRA Rule 2210(c). We do not believe filing this type of content for review by FINRA staff is beneficial to member firms and the filing of this type of content does not appear to provide significant investor protection.
2. The suggestion to exclude 135a communications from filing was previously addressed in NASD Notice to Members 99-79 at which time NASD staff believed that due to the potential misclassification of 135a communications by member firms that a filing exemption would not be pursued. However, we believe this issue does warrant additional consideration and that member firms deal with a number of rule complexities on a frequent and recurring basis and should be able to properly determine if a communication truly is a 135a communication. We have concerns at the same time that FINRA staff

² A retail communication complying with Rule 135(a) is deemed to not constitute an offer for sale of a security and, therefore is not a prospectus within the meaning of Section 2(10) of the Securities Act of 1933.

may be reviewing communications that do qualify as 135a communications but interpreting such communications as Rule 482 communications and requesting firms treat such communications as such when the communication was not intended to be treated as a prospectus under Section 10(b) of the 1933 Act.

3. We believe Rule 135a communications present less risk to the public than communications concerning specific investment company offers subject to the filing requirement of Section 24(b) of the Investment Company Act of 1940 (“Section 24(b)”). However, we also believe that communications related to investments that are subject to Section 24(b) *vary widely with respect to the level of risk they present to investors* and a “one size fits all” approach to the filing requirements is outdated, not beneficial or efficient for member firms and FINRA staff alike. As an example, an S&P 500 index fund communication generally poses less risk to investors than leveraged and inverse ETF communications. We believe the filing requirements concerning Section 24(b) communications should be principles-based and largely dependent upon risk as a factor. Communications distributed by member firms that are not subject to any filing requirements including, but not limited to, communications concerning penny stocks, debt securities with low credit ratings and non-traded REITs³ appear to present higher risk than communications subject to the limitations of Rule 135a and certain communications that are filed to comply with Section 24(b).
4. Communications concerning investment companies that are subject to the limitations of Rule 135a that are posted on an online interactive electronic forum are not subject to filing per FINRA Rule 2210(c)(7)(M). However, if the same communications were to be distributed through channels that are not an online interactive electronic forum, the communications are subject to filing. Under current FINRA rules, it is not the content of the communication that determines the filing requirements; rather it is the distribution method. Given the increasing shift in the industry to engage with retail investors through social media and other channels that offer an online interactive forum, this is an area of continued growth for member firms. Large financial services firms have a significant and growing number of investors that follow their communications through these channels resulting in the communications posted through these channels being viewed by a wide audience and excluded from filing but not exempt from supervision by member firms. This further reinforces the view that communications distributed through channels other than online interactive forums should be treated in a similar manner.
5. Member firms must comply with the content standards set forth under FINRA Rule 2210(d) in all retail communications regardless of whether the retail communication has been filed with the department. Additionally, member firms must have a supervisory structure and written supervisory procedures designed to achieve compliance with rules concerning communications with the public. If 135a communications, communications

³ In May, 2013 FINRA issued Regulatory Notice 13-18 to provide guidance to member firms concerning communications associated with unlisted real estate investment trusts (REITs) and unlisted direct participation programs (DPPs) that invest in real estate. The Regulatory Notice indicated that FINRA staff noticed deficiencies with respect to these communications not meeting content standards. These offers are not required filings under FINRA Rule 2210(c).

subject to the filing requirements of Section 24(b), or some combination of both were to be excluded from the filing requirements in a principles-based approach, this would not remove or lessen the supervisory responsibilities of member firms to ensure that these communications comply with content standards.

6. In lieu of the broad number of filings undertaken by member firms today, FINRA has many ways to review a member firm's communications including, but not limited to, cyclical firm-wide examinations, targeted examinations and Advertising Regulation sweeps. FINRA Rule 2210(b)(6) grants FINRA the authority to spot-check a member firm's communications which allows FINRA staff to determine if member firms are complying with FINRA rules. Should FINRA determine that a member firm's communications do not comply with content standards, FINRA Rule 2210(c)(1)(B) provides FINRA staff the discretion to require the member firm to pre-file communications. A significant reduction in the number of required filings by member firms would allow FINRA to better utilize the Advertising Regulation staff to assist other FINRA staff members in proactively reviewing high-risk communications of member firms through the aforementioned ways of collecting member communications in lieu of the filing process.

We encourage FINRA to take this opportunity to modernize the filing requirements by considering a rule revision to FINRA Rule 2210(c)(7) for the exclusion of Rule 135a communications regardless of the distribution channel, i.e., print as well as online interactive forums. Concurrently, we also urge FINRA to work with the SEC to examine the filing requirements of Section 24(b) to determine the types of communications that clearly present a greater degree of risk to investors versus those communications concerning investment companies that present lower risks. Factors that can be considered in a principles-based approach to the filing requirements include, but may not be limited to, the nature of the securities offered, new products or new features added to existing products, industry trends and disciplinary history of the member.

We take this opportunity to express a concern over the use of limited review letters. While we appreciate that FINRA has a large volume of communications that are reviewed, we believe that sending member firms limited review letters are inconsistent with one of the reasons the filing requirements exist. It is problematic and creates uncertainty for a member firm to file a communication and not be clear as to the opinion of FINRA staff as it creates potential for the firm to continue to distribute potentially problematic communications. We believe that with rule revisions designed to lessen the number of required filings firms must undertake, FINRA will have the opportunity to review the practicality of issuing limited review letters in the Advertising Regulation Department.

III. Application of Disclosure Language

Product specific communications distributed by member firms where the communication may be used prior to the delivery of the offering document often contain a significant amount of disclosure language concerning the products offered. In fact, it is not uncommon to see retail communications for offers such as target date funds, variable annuities and inverse ETFs where

the amount of risk disclosure present eclipses the amount of copy used to alert investors to the availability of the offer.

Schwab believes that in order for communications to be fair and balanced that there will always be a need for disclosures. However, we have concerns that placing a disproportionate amount of risk disclosure in relation to body copy promoting a product may have unintended consequences. For example, investors may be overwhelmed with the amount of disclosure language present which could lead them to not read it at all, or to falsely believe the amount of disclosure indicates that the risks outweigh any potential benefits. We believe that the overuse of risk language in product communications is not beneficial to investors and member firms alike.

It appears that some FINRA staff may take a position with product communications that such communications must be self-contained and present many of the significant risks found in the offering documents directly on the communication. It also appears that member firms are placing a large amount of disclosure language on communications where it appears that the level of disclosure language applied is not warranted. This is likely done by member firms out of concern that their communications may be deemed to not comply with the content standards set forth in FINRA Rule 2210(d). While FINRA Rule 2210(d)(1)(A) requires that communications are fair and balanced, we believe that FINRA has the opportunity to look at the existing rules in an effort to ensure that they are being applied by both FINRA staff and the industry in a consistent manner and the application is not done in a manner that is counterproductive to the intent of the rules.

We further believe that opportunity exists to rethink how firms present disclosure language on product communications. Exploring creative ways to simplify the application of disclosures such as through providing a prominent and direct link to offering documents with respect to online product communications and treating the communications as supplemental sales material is just one example for consideration. We believe FINRA would get an overwhelmingly positive response from member firms if they were to form a task force comprised of FINRA staff and industry participants to meet and discuss the challenges with the application of disclosures. There is an opportunity in the current environment to design proposals to address better ways to serve investors through the use of abbreviated disclosures and to leverage evolving technology for use to enhance the investor experience while meeting the intended objectives of securities rules. For example, while just a few years ago firms relied upon their websites to promote their products and services, today firms are seeing a shift away from traditional websites to tablets and mobile devices which is already causing challenges to firms with respect to the application and use of disclosures.

IV. FINRA Interpretations, Communications & Rule Making

Schwab understands and appreciates the importance of FINRA review letters as well as Regulatory Notices; however, we believe there are two separate but related issues with current usage.

Individual comment letters should not be the venue for rule-making without consistent application and communication of standards industry-wide. We believe this can be achieved in a

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couple of ways. First, FINRA might consider working with the industry to make available a searchable database of comment letters sent to member firms (similar to the current availability of Regulatory Notices). We believe it would be extremely beneficial for member firms to be able to view FINRA review letters and communications from a database as an additional resource to help understand the applicability of the rules to certain products and services. To better understand the challenges with this proposal, such as confidentiality, we believe a task force comprised of FINRA staff and member firms could be assembled to explore this proposal. Second, for wide-spread, novel, or high-risk issues, FINRA should consider communicating with the industry, as a whole, through a Regulatory Notice or similar publication (i.e. a dedicated section on FINRA's website) which would help ensure that all firms receive the same message concurrently as well as alleviate issues created by scope creep in individual letters⁴.

The use of Regulatory Notices is important to address the first issue above. However, Regulatory Notices are not helpful if they are not clear, concise, and applicable across members. Historically, Regulatory Notices have led to substantial industry debate about the meaning and application of the Notice. In order to address this inconsistency and confusion, Schwab suggests implementing an industry committee to work with FINRA during the drafting phase of Notices as well as a focus group following implementation to assess the value of the Notice, similar to this process of rule reevaluation.

Schwab understands the importance of allowing for FINRA to provide comments regarding material filed with FINRA Advertising Regulation and appreciates FINRA clarifying their positions in the review letter; however, we believe there should be consideration to more effectively communicate new interpretations or rule clarification comments provided in review letters to member firms. This effort may assist in ensuring consistent application of the rules and socialization of current positions that FINRA staff has taken with respect to specific trends and issues, enabling member firms to uniformly apply the information to their communications, decrease the potential for investors to be misled and allow for more equitable standards.

Schwab thanks you for consideration of the points raised in this letter and welcomes any further discussions or questions.

Very truly yours,



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⁴ For example, it appears that FINRA is citing Regulatory Notice 13-23 when making comments to member firms through review letters concerning fees associated with products such as ETFs when it appears that the intent of Regulatory Notice 13-23 was to provide guidance to member firms concerning the disclosure of fees associated with IRAs and retail brokerage accounts.