Stephanie R. Nicolas

+1 202 663 6825 (t)
+1 202 663 6363 (f)
stephanie.nicolas@wilmerhale.com

VIA ELECTRONIC FILING ***(pubcom@finra.org)***

June 13, 2008

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

Re: Proposed Consolidated FINRA Rules Governing Supervision and Supervisory Controls (Regulatory Notice 08-24)

Dear Ms. Asquith:

This letter is submitted on behalf of our client, one of the largest independent broker-dealer networks in the United States, in response to the Financial Industry Regulatory Authority's ("FINRA") request for comment on proposals relating to the FINRA supervision and supervisory control rules (the "Proposed Rules").[1/]

I. Overview

At the outset, we would like to commend FINRA for its efforts to develop a new, consolidated rulebook and provide firms with greater flexibility to tailor their supervisory and supervisory control procedures to reflect their respective business, size, and organizational structure. We also thank FINRA for the opportunity to comment on this very important proposal. That being said, we have concerns regarding certain of the Proposed Rules, which appear to contain significant, substantive changes to the existing regulatory framework and expand broker-dealers' supervisory obligations and FINRA's jurisdiction. In particular, and for the reasons discussed more fully below, we are concerned by the following provisions:

(A) The apparent expansion of member firms' obligations to supervise outside business activities pursuant to proposed Rule 3110(b)(3); and

---

1/ Regulatory Notice 08-24, Supervision and Supervisory Controls: Proposed Consolidated FINRA Rules Governing Supervision and Supervisory Controls ("Notice 08-24").

(B) The apparent expansion of FINRA's jurisdiction to non-securities/non-investment banking products and activities pursuant to proposed Rule 3110(a)(2).

Although the provisions noted above appear to represent a departure from the status quo, FINRA has characterized them as a "streamlining" and consolidation of existing rules, and has not provided any rationale or justification for more expansive regulation. FINRA may benefit from requesting industry feedback regarding the perceived regulatory concerns supporting FINRA's proposal. Accordingly, we urge FINRA to reconsider these proposals and revise them so that they are consistent with the current regulatory regime and the flexible, principles-based approach that FINRA stated is a goal of the Proposed Rules.[2/] To the extent that FINRA does intend to change the existing regulatory framework, we respectfully request that FINRA provide the bases for the changes and attendant costs and burdens, and provide member firms with an opportunity to comment on the Proposed Rules, before they are filed with the Securities and Exchange Commission.[3/]

II. Concerns Relating to the Proposed Rules

A. Proposed Rule 3110(b)(3) Appears to Significantly Expand Member Firms' Supervisory Obligations and FINRA's Jurisdiction and, As Such, Should Be Rewritten or Clarified.

As currently drafted, Proposed Rule 3110(b)(3) appears to significantly expand member firms' supervisory obligations and FINRA's jurisdiction. Under this proposed rule, a firm would determine whether to allow its associated persons to "*conduct any investment banking or securities business*" away from it. If the firm decides to approve any such activity, then the activity must be supervised by the firm as if it were conducted on the firm's behalf. Neither Notice 08-24 nor the Proposed Rules, however, address the scope of the new approval and supervision requirements or the definition of "securities business" for purposes of these requirements.

Given the uncertainty and potential breadth regarding the meaning of the term "securities business," Proposed Rule 3110(b)(3) appears to expand firms' responsibility for outside

---

2/ *See* Notice 08-24, at 1 ("The proposed rules would re-write certain provisions of the existing supervision and supervisory control rules in a manner that provides firms with greater flexibility to tailor their supervisory and supervisory control procedures to reflect their business, size, and organizational structure.")

3/ While we acknowledge that Section 15A of the Exchange Act does not require FINRA to generate a competitive impact statement or otherwise engage in a cost/benefit analysis in its rulemaking, we note that FINRA is bound by Section 15A(b)(6), which provides that a national securities association may only impose burdens that are necessary and appropriate to further the purposes of the Exchange Act. *See* 15 U.S.C. § 78o-3.

securities-related activities and FINRA's jurisdiction over these activities.[4/] This is an issue of particular concern for our client, whose dual registrants engage in many outside securities-related activities, such as providing investment advisory services through their own, independent investment adviser entities. It also is a significant departure from the long-standing guidance included in NASD Rule 3040 (Private Securities Transactions of an Associated Person) and NASD Notices to Members 94-44 and 96-33,[5/] which provide that member firms must supervise activities by their associated persons conducted "away" from the firm, *only* to the extent those associated persons participate in securities transactions and receive selling compensation. This rule and the NASD's related guidance strike an appropriate balance between allowing associated persons to conduct activities apart from their member firms, and ensuring that associated persons' participation in securities transactions is appropriately supervised.

Accordingly, we urge FINRA to clarify that the Proposed Rules will not change the existing regulatory framework, *i.e.*, that associated persons will be deemed to "conduct securities business" only in so far as they "participate in securities transactions and receive selling compensation," as interpreted by NASD Rule 3040 and related NASD guidance. Indeed, FINRA's failure to clarify Proposed Rule 3110(b)(3) as we have advocated could lead to unmanageable regulatory consequences and significant burdens on member firms. For example, as currently written, this proposal may contemplate that members should take responsibility for supervising all of their independent registered investment advisers' investment recommendations – even when the customer is not a customer of the member firm and those recommendations occur away from the member firm and do not result in a securities transaction. This proposal also may contemplate that member firms must review all of their associated persons' outside investment advisory activities – such as recommendations in financial plans, interactions with customers, and assessment of advisory fees.

The application of Proposed Rule 3110(b)(3) to these scenarios would create additional uncertainty regarding the issue of whether these securities activities effectively would make a dual registrant's investment advisory clients also customers of the dual registrant's member firm, thus triggering attendant suitability, anti-money laundering, supervision and record-keeping obligations – even when an adviser's recommendation does not lead to a securities transaction. Such an outcome would create unmanageable compliance burdens and costs for firms. For these reasons, we urge FINRA to clarify that Proposed Rule 3110(b)(3) is only intended to address securities activities where an associated person participates in a securities transaction and receives selling compensation, consistent with the long-standing requirements in NASD Rule 3040 and the related NASD guidance.

4/ In this regard, while there is a definition of "investment banking or securities business" in the NASD By-Laws, which appears to exclude investment advisory activities, it is not clear whether FINRA intends to use this definition for purposes of Proposed Rule 3110(b)(3). *See* NASD By-Laws, Article I(u).

5/ NASD Notice to Members 99-44: Board Approves Clarification On Application of Article III, Section 40 of Rules of Fair Practice to Investment Advisory Activities of Registered Representatives (May 1994); NASD Notice to Members 96-33: NASD Clarifies Rules Governing RR/IAs (May 1996).

B. Proposed Rule 3110(a)(2) Appears to Expand FINRA's Jurisdiction to Non-Securities and Non-Investment Banking Activities and Products and, As Such, Should Be Rewritten or Clarified.

We believe that Proposed Rule 3110(a)(2) is overly broad, in so far as it requires firms to designate "an appropriately registered principal(s) with authority to carry out the supervisory responsibilities of the member *for each type of business in which it engages*."[6/] The breadth of this language raises concerns because it suggests that member firms must designate registered principals with supervisory responsibilities for business activities that bear no relation to securities or investment banking activities (*e.g.*, fixed insurance product sales). Through this proposal, FINRA appears to be expanding its jurisdiction into areas that are the responsibility of other regulators, and that are adequately covered by other regulatory regimes. Although FINRA justifies this proposal as consistent with the current regulatory framework, the language of Proposed Rule 3110(a)(2) is broader because it appears to apply the principal designation requirement beyond activities requiring broker-dealer registration.

While we recognize that existing NASD Rule 3010(b)(1) requires written supervisory procedures for each type of business in which the member engages, we do not believe it is appropriate to require a securities principal to have supervisory responsibility over areas that are wholly unrelated to securities or investment banking products or activities.[7/] We therefore strongly urge FINRA to revert to the language of current NASD Rule 3010(a), which reads, in relevant part: "The designation, where applicable, of an appropriately registered principal(s) with authority to carry out the supervisory responsibilities of the member for each type of business in which it engages *for which registration as a broker/dealer is required*."[8/]

Alternatively, if FINRA does not retain the language in the current rules, we ask that FINRA clarify that its jurisdiction does not extend to these non-securities, non-investment banking activities of member firms, and that it will defer to other regulators for these business areas. We believe that such recognition is critical to avoid overlapping, potentially inconsistent regulatory regimes and in the interest of streamlined regulation. If FINRA does not adopt these recommendations, we respectfully request that FINRA provide a rationale – beyond that of "rule harmonization" – for appearing to expand its jurisdiction to non-securities and non-investment banking activities.

6/ Proposed Rule 3110(a)(2) (emphasis added).

7/ To that end, we believe there is a question of whether FINRA has the power to promulgate regulations relating to non-securities, non-investment banking activities. Section 15A of the Exchange Act specifically prohibits national securities associations from "regulat[ing] by virtue of any authority conferred by this title matters not related to the purposes of this title . . . ." 15 U.S.C. § 78o-3(b)(6). Here, the proposal effectively would allow FINRA to regulate the non-broker-dealer activities of member firms.

8/ NASD Rule 3010(a)(2) (emphasis added).

* * * * *

Thank you for providing us with the opportunity to comment on this important matter. Should you have any questions, please contact me at 202.663.6825.

Very truly yours,

Stephanie R. Nicolas

Stephanie R. Nicolas