



VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS
AND INDEPENDENT FINANCIAL ADVISORS

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VIA ELECTRONIC MAIL

May 23, 2014

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

Re: Regulatory Notice 14-14: Retrospective Rule Review – Communications with the Public Rules

Dear Ms. Asquith:

On April 8, 2014 the Financial Industry Regulatory Authority (FINRA) published a request for comment on the effectiveness and efficiency of its rules regarding Communications with the Public. This retrospective review includes a review of the substance and application of the rules as well as FINRA's process to administer the rules in order to determine whether FINRA's rule set is meeting its intended investor-protection objectives by reasonably efficient means.

The Financial Services Institute¹ (FSI) appreciates the opportunity to comment on this Regulatory Notice. FSI is encouraged by FINRA's adoption of economic impact assessment and cost-benefit analysis with regard to rulemaking.² The utilization of retrospective review is a vital component of increasing the transparency and accountability of SRO rulemaking, and will ensure that rules remain relevant and are appropriately designed to achieve their objectives. As FINRA progresses through the findings and action phases of the review process, FSI looks forward to providing constructive feedback on the rule set that will assist in the retrospective rule review assessment.

Background on FSI Members

The independent broker-dealer (IBD) community has been an important and active part of the lives of American investors for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD firms also share a number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; primarily engage in the sale of packaged products, such as mutual funds and variable insurance products; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered

¹ The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has 100 Broker-Dealer member firms that have more than 138,000 affiliated registered representatives serving more than 14 million American households. FSI also has more than 35,000 Financial Advisor members.

² See Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking (September 2013); available at <http://www.finra.org/web/groups/industry/documents/industry/p346389.pdf>.

investment adviser firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial advisers are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their financial goals and objectives.

In the U.S., approximately 201,000 independent financial advisers – or approximately 64 percent of all practicing registered representatives – operate in the IBD channel.³ These financial advisers are self-employed independent contractors, rather than employees of the IBD firms. These financial advisers provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisers are typically “main street America” – it is, in fact, almost part of the “charter” of the independent channel. The core market of advisers affiliated with IBDs is comprised of clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisers are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other centers of influence.⁴ Independent financial advisers get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisers have a strong incentive to make the achievement of their clients’ investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisers. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is committed to preserving the valuable role that IBDs and independent advisers play in helping Americans plan for and achieve their financial goals. FSI’s primary goal is to ensure our members operate in a regulatory environment that is fair and balanced. FSI’s advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

Comments

FSI appreciates the opportunity to submit comments on FINRA’s Retrospective Rule Review. In preparing our comments, FSI engaged with various member firms to obtain a variety of views for FINRA to consider. These members vary in their size, resources, and use of technology. Despite these differences, the members converged on several areas that FINRA may find helpful in assessing the current set of rules regarding Communications with the Public. Correspondingly, FSI provides the following comments:

- **Have the Rules Effectively Addressed the Problem(s) They Were Intended to Mitigate?**
FSI and its members believe that, overall, the rules are effectively addressing the issues and problems they are intended to mitigate. Firms have also, generally, had good experience in implementing the changes to FINRA’s Communications with the Public Rules

³ Cerulli Associates at <http://www.cerulli.com/>.

⁴ These “centers of influence” may include lawyers, accountants, human resources managers, or other trusted advisers.

as approved by the SEC on March 29, 2012.⁵ Specifically, firms have observed the following with respect to the effectiveness of the current rules:

- **Pre-approval:** Principal pre-approval of communications is an effective control for protecting investors because it allows a trained professional to review material before it is released to the public. The requirements and process helps to ensure that investors are protected from false and misleading communications.
- **Correspondence Review:** Correspondence review is an extremely effective practice that allows firms to capture e-mail correspondence and identify potential compliance concerns. Firms have successfully identified and rectified issues related to undisclosed outside business activities, inappropriate marketing, and advertising through the reviews. Even if the requirement for correspondence review was abolished, firms would still continue the practice in order to identify and analyze operational risks.
- **FINRA Filing and Review Process:** Because of the sometimes lengthy filing and review process by FINRA (as discussed below, in more detail), some members feel that it functions as an audit rather than a process that protects investors from misleading or otherwise inappropriate communications and advertising.
- **What have been your experiences with implementation of the rule set, including any ambiguities in the rules or challenges to comply with them?**
 - **Turnaround Time:** FSI member firms commented on challenges faced due to long turnaround time for FINRA to review retail communications and provide a response to firms. Firms have experienced turnaround times as long as six months for certain materials. The result is that firms and advisors are incentivized to avoid filing with FINRA whenever possible, which results in more generalized materials being distributed to the public. In instances where firms are on a tight timeline, the expedited FINRA filing review fee is cost prohibitive and forces firms and advisors to remove pertinent information from the material to make it more generalized and less helpful to investors.
 - **Subjectivity and Ambiguity:** One of the largest issues with respect to the rules is the subjectivity of Rule 2210 and the review process by different FINRA analysts. Firms have received feedback from advisors that the responses provided by FINRA staff are often inconsistent with other material they see in the field. This increases confusion and frustration with the rules' requirements. Frustrations arise when members see an advisor from a different firm using marketing material similar to a piece that their home office or FINRA rejected. Firms also find the FINRA response letters to be vague and lacking in specific guidance. FSI members feel this subjectivity and confusion has undermined confidence in the rule, as firms do not believe there are sufficient defining criteria to direct review and ensure consistency among the industry. Firms would like to see FINRA's response letter offer alternatives to problematic images and language. Firms also expect FINRA analysts to be assigned to member firms based on the firms' main products. For example, firms that offer variable insurance products should have an assigned analyst who is familiar with the complexity of variable insurance products.
 - **Correspondence vs. Retail Communication:** Firms have also experienced challenges with respect to distinguishing between correspondence and advertisement. Under Rule 2210, any written letter or email message with 25 or fewer prospective retail

⁵ Securities Exchange Act Release No. 66681 (March 29, 2012), 77 Fed Reg. 20,452 (April 4, 2012) (Notice of Filing of Amendment No. 3 and Order Granting Approval of a Proposed Rule Change, File No. SR-FINRA-2011-035)

customers within any 30 calendar-day period is defined as correspondence. If the number of prospective retail customers exceeds this amount, a letter or email message is defined as retail communication. Many firms have experienced significant challenges when attempting to build compliance and review systems that can efficiently distinguish whether communications fall under one of these categories. Therefore, many firms have elected to treat any message sent to more than one recipient as retail communication and subject to review.

- **Promissory References:** Firms have also experienced considerable ambiguity with respect to whether pieces contain a “promissory” reference. While the context of each piece of marketing material is different, firms have been confused by instances where FINRA has deemed innocuous images and other material to be promissory. While firms understand that FINRA would prefer to retain flexibility in order to review and assess each individual communication, firms have been confused by a lack of clarity with respect to promissory references. The frustration firms have experienced in this area has contributed to decisions to generalize communications in order to avoid filing.
- **Third-Party Materials for Qualified Plans:** Many financial advisors provide investment services to qualified plans of small businesses. FINRA’s filing requirements allow an exception for “institutional investors,” which include qualified plans with more than 100 participants. Third-parties that create marketable materials targeted at qualified plans often do not file these materials with FINRA because of the institutional investor exception. However, firms and advisors will not use these materials because the specific qualified plans they work with have less than 100 participants, and will not file these materials with FINRA on a third-party’s behalf. This leaves a gap in marketable materials that firms and advisors can use for these plans.
- **Investment Advisor Communications:** Many FSI member firms are dually registered as both broker-dealers and investment advisors. In addition, many advisors have “hybrid” structures, whereby they maintain a broker-dealer affiliation as well as owning their own registered investment advisor (RIA). These advisors create a great deal of communications under their RIA and it is very challenging for firms to know when to apply FINRA’s rules concerning Communications with the Public. Specifically, Rule 2210(b)(1)(d)(3) defines materials that are exempt from pre-approval as any items that “do not promote a product or service of the firm.” Under the rule, it is not clear whether pieces that make mere mention of a service or contain a corporate logo are in fact “promoting the services” of the firm or advisor. Although RIAs may argue that their materials are exempt, FSI members who are dually-registered must determine whether those materials may be used to solicit registered investment products such as mutual funds. For example, many RIAs create or provide market or sector-specific commentary. A review of this rule should examine ways in which FINRA could provide additional clarity with respect to reviewing and pre-approval of communications created purely for an advisor’s RIA business.
- **What have been the costs and benefits arising from FINRA’s rules? Have the costs and benefits been in line with expectations described in the rulemaking?**
 - **Volume of communications:** The volume and time commitment of review is very expensive for firms. Firms also expect the volume of communications to increase as advisors and clients increase their adoption and use of electronic and social media communications. Firms employ staff and purchase products and services from

vendors to deal specifically with reviewing communications, with the costs increasing as the number of advisors associated with the firm increase. As advances in technology have made it easier and cheaper for advisors to create advertising materials in-house, this has also increased the volume of marketing materials requiring review by broker-dealer staff.

- **Costs to File:** FINRA filing fees can become cost-prohibitive for firms and advisors, leading to less materials being filed and more generalized communications. If advertising material needs to be filed with FINRA, the cost is often passed on to advisors. In most cases, advisors will elect not to incur the cost of filing the material with FINRA and elect to change the content of the material to remove even conservative references to products or services. The home office staff of broker-dealers is often put in the position where they are editing the content of advisor communications in order to avoid triggering the filing requirements. The result is more generalized communications, which advisors find frustrating and investors find unhelpful.
- **Can FINRA make the rules more efficient and effective, including FINRA's administrative process?**
 - **Additional Guidance:** Some firms have suggested that FINRA provide a list of marketing terms that are acceptable, as well as a firm stance on what terms would not be deemed acceptable. Some firms also believe that FINRA should provide a system to members which contains marketing materials that have been reviewed and received a "clean letter." Because advisors use a great deal of static content provided by third parties, especially in the independent channel, a system allowing firms to quickly verify whether a piece has been reviewed and view the FINRA response letter would be highly beneficial. A member database containing images and FINRA response letters for specific pieces may be an effective method of achieving this goal. Another step FINRA can take is to provide information to firms on the types of material being filed erroneously by firms due to a misunderstanding of FINRA's rules.
 - **Service-Oriented Materials and Existing Shareholders:** Another area that FINRA could improve is the principal pre-approval of material that is service-oriented and sent to existing shareholders. Firms need more information and guidance on instances where service-oriented materials are not considered a recommendation or a promotion of a product or service. For example, firms that provide service-oriented overviews of different types of annuities to existing holders of fixed annuities trigger FINRA's filing requirements, however the firm's goal in mentioning variable annuities is to give clients a fair and balanced discussion of the different types of annuities available. Even a mention of sub-accounts in marketing materials would trigger the filing requirement, despite the fact that the goal of these materials is solely to provide general education. Another issue arises when advisors want to send communications to existing shareholders about a fund in their account. An example of this may be when a non-traded real estate investment trust (REIT) is going public and an advisor seeks to send emails to all his or her clients who hold the REIT stating that the advisor and client should meet and discuss the implications. Due to the length of time required to file and review the advisor's communication, the relationship between the client and advisor can become strained. The rules are not operating efficiently if advisors cannot promptly provide clients with effective and complete communication with respect to a product in their portfolio. Another area FINRA can investigate is whether FINRA

filing and review requirements can be triggered based upon the risk rating of specific products. For example, mutual funds with low risk would have lower thresholds versus higher risk products such as some alternative investments.

- **New Technology:** As more pressure is put on firms and FINRA due to the increased adoption of social media and other emerging technologies, FINRA can enhance its own understanding and use of technology to reduce resource burdens and increase effectiveness. FINRA should also share the results of FINRA's Spot-Check of Social Media Communications.⁶ This information will allow firms to understand and adopt existing best practices for addressing new technologies in the industry. Another area FINRA can investigate is a more efficient means for firms to submit social media material to FINRA.
- **FINRA Conference:** Although the FINRA Advertising Conference is a helpful opportunity for new employees, seasoned audiences are finding the conference stale and in need of improvement. FINRA should develop programs targeted at those with significant experience. An example would be for FINRA to provide specific examples of complex materials that are considered compliant versus non-compliant.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with FINRA on this and other important regulatory efforts.

Thank you for your consideration of our comments. Should you have any questions, please contact me at (202) 803-6061.

Respectfully submitted,



David T. Bellaire, Esq.
Executive Vice President & General Counsel

⁶ FINRA Targeted Examination Letters, Spot-Check of Social Media Communications (June 2013); available at <http://www.finra.org/Industry/Regulation/Guidance/TargetedExaminationLetters/P282569>.