

To: Jennifer Piorko Mitchell  
Office of the Corporate Secretary  
FINRA

From: Chuck Millington  
Millington Investments, LLC  
CEO

Re: Response to the Special Notice titled "Engagement Initiative"

Date: April 7, 2017

## Introduction

I am writing in response to the Engagement Initiative Special Notice. I'm on FINRA's District Committee 8, I represent the small firms in that district. I've been in the industry since 1973, been the Controller and FinOp for a variety of firms; some doing only institutional business, some only broker to broker business and currently providing products to retail customers on an application way basis. I work with my son in Naperville Illinois, and we have only two registered reps. Our business is primarily fee based through our RIA. Commissioned products that are processed through our broker/dealer are a small part of our overall services to our clients.

My responses to the Special Notice are based on the type of services my business is currently providing. My son and I are CPAs and CFPs®, and we have a number of SEC security licenses. Our clients expect us to have an in-depth knowledge of their particular financial picture and be able to help them achieve their financial goals through tax planning, insurance needs, estate planning, as well as, recommending the most effective investments. Just like smaller community banks, smaller investment firms, that are dually registered as RIAs and B/Ds, strive to understand and provide needed and wanted services to their community. I believe that current regulations and regulatory structures are designed to regulate larger firms that are more commissioned basis then the dually registered firms that are more fee based. I believe that our industry needs to respond to changing investor requirements. Customers today expect advise on a variety of financial topics not just investment recommendations.

Nearly 50% of the small firms in District 8 have less than 10 registered reps. However, these smaller firms only employ about 1.5% of the total number of registered reps in that category. I believe that many of these smaller firms provide services to their clients through their RIA as well as their B/D. I also believe that the majority of the larger firms concentrate more on institutional and/or broker to broker business, and have the majority of their revenue earned through commissions not advisory fees. Looking at the structure of District 8; current FINRA rules may be adequate to cover overseeing the vast majority of the reps, but may not be properly structured to meet the needs of 50% of the firms.

My comments are based on the following assumptions;

- 1) Our industry will continue to evolve into more of a fee based business that puts an emphasis on financial services which seek lower cost customized investment solutions that includes tax and estate planning considerations,

- 2) The number of smaller firm structures will grow in the future in response to the changing needs of investors. These smaller firms will attract investment professionals with the education and broad professional backgrounds that can meet client requirements, and
- 3) Regulations and regulatory agencies will adopt very different strategies for;
  - a. Dual RIA and B/D structures that are smaller community focused,
  - b. Larger firms that are more commissioned based,
  - c. Larger firms that are more institutional based or more broker to broker based.

I believe that the current regulatory structure of FINRA tends to be more suited to regulate the firms described in 3)b and 3)c. Therefore, my following comments and suggestions are directed towards the needs of the firms described in 3)a.

## Comments

Over the last 50 years the investment industry has gone through significant changes, mostly due to investor changing needs and requirements. The 70s were dominated by large firms providing individual stocks and bonds on a commission basis. The 80s experienced great growth in investment company products providing efficient ways of obtaining a diversified portfolio on a commission basis. Over the past 20 years investors have become better educated and various products are designed to give investors a variety of lower cost products to match their investment needs. Investors have become more strategic in their thought process, having a longer term view of how they should position their investments. As a result, investors are now seeking professionals that can steer them towards more effective longer term investment strategies that includes tax and estate planning considerations.

The Special Notice states “FINRA must understand what it regulates” and the Special Notice asks for constructive feedback. My RIA is regulated more on certain principles, not so much on a variety of rules. Many of the professionals working for independent RIAs are certified financial planners, (“CFPs®”). CFPs® are required to pass tests that concentrate on the skills necessary to provide effective financial advice to clients. CFPs® are held to the standard that at all times the best interests of their clients must always be the overriding principle that governs their activities. FINRA, on the other hand, regulates through rules and specific procedures and brokers are tested more on their knowledge of those rules and procedures than their ability to identify the best investment strategies for their clients. While brokers are required to have licenses to sell certain types of products, they are not tested on how those products correlate to other products that the client may have. It would be like a Doctor is tested on how to prescribe a specific drug but is not tested on how well they can identify various drug interactions.

FINRA has established many rules and many specific procedures. I believe that most rules and procedures were created with the best of intentions and were created to meet certain needs. Over the years, more rules and procedures were added making it now a world of many, many rules and procedures. A small firm like mine is required to have a Written Supervisor Procedure (“WSP”) document that exceeds 115 pages in order to meet FINRA’s requirements. The WSP ends up being a legal document, not a useful management tool. Today’s rules and procedures have been created to meet what was going on over the past 50 years, but times have changed. Even though commissioned products are a small part of my business, I spend significant time and money meeting FINRA requirements. Financial audit and AML audit requirements saddle my firm with significant unnecessary

costs. In addition, FINRA exams tend to focus too much on the specific elements highlighted in the Annual Regulatory and Examination Priorities Letter, regardless of how material those issues may be to the firm or the firm's clients. By focusing on the trees and not the overall forest, firms may not be judged on their overall merits. Advisors tend to want to be under the RIA umbrella because they believe that they will be judged on their overall relationship with their client, not on particular issues that FINRA has decided to focus on.

## Suggestions

I've been asked to respond to the Special Notice by commenting on the many subsections of the 30 page notice. Within the 30 page notice there are a number of committees and procedures listed for my review and comment. My overriding comment is there are way too many committees and procedures imbedded in FINRA and FINRA should be organized around business types and not on the size of the firm. Institutional business is very different then broker to broker business or the large retail broker firm that is primarily commissioned based. And the small dually registered firm is very different than any of these other firms. A lot of FINRA's organization efforts has been directed around the size of the firm, but the type of firm's business is much more important. For instance, a large retail broker which primarily offers products on a commissioned basis, may actually be easier to regulate based on the limited activity they have with each customer. On the other hand, the smaller dually registered firm has a continuous relationship with the retail customer and deals with a variety of products and complicated financial issues.

Regulating the large retail broker may be better regulated using a rule based environment. The dually registered firm may be better served by regulators that use a principle based mindset. Interestingly, the smaller firms that are dually registered may require the more experienced examiner, one that has a greater breath of knowledge about portfolio construction, taxes and estate planning. The larger retail firms may only need the less experienced regulator who is trained in specific rules and procedures.

It's been my experience that the most valued regulatory relationship is one that I can call on a regular basis to ask questions about best practices or to bounce off some ideas I may be entertaining. This would require a regulator who has a background in the type of firm they interface with. It wouldn't be based on how large but the type. Again, I can make an argument that the smaller firms that are multi faceted may actually need more experienced regulators than the larger firms that are more one dimensional.

I would find it more productive responding to an initiative that tries to breakdown how FINRA should be organized in response to the various types of firms that exist in today's environment. Many of the rules, procedures and initiatives listed in the notice are not particularly relevant to a firm like mine. A firm like mine would greatly appreciate reducing the regulatory burden it currently experiences. It's difficult to make money on the broker side due to audit expenses and time spent responding to regulatory requirements. FINRA should evaluate their cost effectiveness when dealing with firms like mine. Should time and procedures be the same when dealing with the various types of firms that exist today? Would it make more sense to customize the exam staff so it is tailored to properly address each type of firm? How should FINRA interface with the regulators on the RIA side? A good analysis breaking down the costs of providing these customized services may show where FINRA can better use their resources.

## Conclusion

Thank you for reaching out to get input from the industry. My overriding premise is; "Since there are various types of firms, there should be an approach and structure that recognizes that there are different regulatory challenges depending on the type, not so much on the size of a firm". I recognize that it could be quite a challenge to take a step back and reevaluate and potentially restructure an organization and a set of rules and procedures that have developed over the past several years. However, there have been significant changes in the industry. Many of these changes are exciting since they are designed to better serve the needs and desires of investors.

My hope is that FINRA and other regulatory agencies can get together to figure out how best to coordinate their efforts related to effectively providing oversight of firms like mine. Even when the vast majority of our clients' portfolios are fee based, there are times when commissioned based products make sense for a portion of their investments. However, it has become very costly to provide these investments due to the many rules and procedures imposed on firms like mine.

Again, thank you for the opportunity to respond to this initiative, please let me know if you have any questions or need anything else.