

VIA ELECTRONIC MAIL

December 18, 2008

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1500

RE: FINRA Regulatory Notice 08-68: Circulation of Rumors

Dear Ms. Asquith:

On November 11, the Financial Industry Regulatory Authority, Inc. (FINRA) requested comment on a proposed rule regarding the circulation of rumors (Proposed Rule). The Proposed Rule combines aspects of FINRA Rule 6140¹ and Incorporated NYSE Rule 435(5)² and extends the prohibitions on the origination and circulation of rumors to cover all securities. The Proposed Rule is part of a larger regulatory effort to determine whether traders have intentionally circulated rumors in an effort to manipulate the price of securities. FINRA's request for comment follows the Securities and Exchange Commission's July 13, 2008 announcement that its Office of Compliance Inspections and Examinations and FINRA would immediately conduct examinations aimed at the prevention of the intentional spread of false information intended to manipulate securities prices.³

The Financial Services Institute⁴ (FSI) commends FINRA for its efforts to curb the circulation of false and misleading rumors that could affect the prices of securities. We recognize that the Proposed Rule is an attempt to supplement existing federal prohibitions against disseminating false rumors about a security.⁵ We believe those who engage in such activities do irreparable harm to the U.S. securities markets by undermining the investing public's confidence in their legitimacy. Nevertheless, we have concerns about the Proposed Rule in its current form. Those concerns are outlined in this letter.

Background on FSI Members

The Independent Broker-Dealer (IBD) community has been an important and active part of the lives of American consumers for more than 30 years. The IBD business model focuses on

¹ See FINRA Rule 6140 at http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4322.

² See NYSE Rule 435(5) at http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=6565.

³ See SEC Press Release 2008-140 at <http://www.sec.gov/news/press/2008/2008-140.htm>. FINRA also warned its members to in a March 31, 2008 news release that can be seen at <http://www.finra.org/Newsroom/NewsReleases/2008/P038211>.

⁴ 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 116 Broker-Dealer member firms that have more than 130,000 affiliated registered representatives serving more than 14 million American households. FSI also has more than 12,000 Financial Advisor members.

⁵ Disseminating a false rumor about a security, particularly when accompanied by profitable trading, can result in actions under Section 17(a) of the Securities Act of 1933 as well as Sections 9(a)(4) and 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder.

comprehensive financial planning services and unbiased investment advice. IBD members 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, by “check and application”; take a comprehensive approach to their clients’ financial goals and objectives; and provide investment advisory services through either affiliated registered investment advisor firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial advisors 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 98,000 independent financial advisors – or approximately 42.3% percent of all practicing registered representatives – operate in the IBD channel.⁶ These financial advisors are independent contractors, rather than employees of the IBD firms. Independent financial advisors 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 advisors are typically “Main Street America” – it is, in fact, almost part of the “charter” of the independent channel. The core market for advisors affiliated with IBDs is clients with a net worth of \$250,000. Independent financial advisors are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Independent financial advisors get to know their clients personally and provide them investment advice in face-to-face meetings. Most of their new clients come through referrals from existing clients or other centers of influence.⁷ Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisors 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 advisors. 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 advisors play in helping Americans plan for and achieve their financial goals. FSI’s primary goal is to insure 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 offers the following comments on the Proposed Rule:

- Scope of the Proposed Rule Should Be Narrowed – Curbing the circulation of false and misleading rumors that could affect the price of securities is a laudable regulatory goal. However, it must be balanced against the natural inclination of investors, broker-dealers, and financial advisors to engage in legitimate conjecture and speculation about the performance and prospects for securities prices. Therefore, we believe the scope of the Proposed Rule should be only as broad as necessary to insure investor protection without

⁶ Cerulli Associates Quantitative Update: Advisor Metrics 2007, Exhibit 2.04. Please note that this figure represents a subset of independent contractor financial advisors. In fact, more than 138,000 financial advisors are affiliated with FSI member firms. Cerulli Associates categorizes the majority of these additional advisors as part of the bank or insurance channel.

⁷ These “centers of influence” may include lawyers, accountants, human resources managers, or other trusted advisors.

the unintended consequence of limiting the exchange of thoughts and opinions about the value of particular securities. The Proposed Rule has the potential to stifle conversations involving legitimate conjecture and speculation because it lacks reasonable limitations on its applicability. Specifically, we believe the Proposed Rule's prohibition on the origination or circulation of rumors should be limited to statements that are false or misleading and intended to influence the market price of a security. As a result, we proposed the following amendments:

No member shall originate or circulate in any manner a rumor concerning any security which the member knows or has reasonable grounds for believing is false or misleading ~~or would improperly~~ and is intended to influence the market price of such security.

We have no objection to the Proposed Rule being applied to all securities.

- Proposed Rule's Reporting Requirement is Overly Broad – The Proposed Rule would require broker-dealer firms to report promptly to FINRA any circumstance that reasonably would lead the member to believe that a rumor might have been originated or circulated. Since the source and validity of rumors are often difficult, if not impossible to verify, the Proposed Rule will require broker-dealers to make a difficult choice among unattractive options. These include reporting all potentially qualifying speculation and conjecture they are aware of, dedicating important resources to researching all such statements to determine whether they meet the reporting criteria, or neglecting their reporting obligations altogether. As a result, we believe the current reporting provision is overly broad and, therefore, will fail to achieve FINRA's goal of providing timely information on rumors impacting securities prices. However, we believe these problems can be alleviated by limiting the reporting criteria to the origination of rumors by an associated person of the member. Therefore, we propose the following amendment to the Proposed Rule's reporting provision:

A member must promptly report to FINRA any circumstance which reasonably would lead the member to believe that any such rumor might have been originated ~~or circulated by an associated person of the member.~~

In addition, we note that the Proposed Rule fails to specify the content of the report, the method of reporting, or the individual or group within FINRA to whom the information should be reported. We believe each of these details should be specified in the Proposed Rule.

Finally, if you choose not to amend the Proposed Rule as we suggest above, we believe reporting firms should be granted qualified immunity to encourage accurate reporting without repercussions associated with a good faith report that is later determined to be unfounded.

- Proposed Rule Fails to Include the NYSE Exception for Widely Published Rumors – FSI believes the Proposed Rule should retain the NYSE's exception for unsubstantiated information published by a widely circulated public media if the source of the information and its unsubstantiated nature are disclosed. We believe it is unreasonable to prohibit member firms from discussing information of this type with clients due to its inherent ability to impact share prices. Investors have a right to know that such rumors exist and may have an impact on the market price of a security. Investors reasonably expect their

financial advisor to provide them with information of this type. An unwillingness to discuss such matters will be perceived by investors as poor customer service or worse – a lack of necessary due diligence. As currently written, the Proposed Rule will restrict these important discussions between financial advisors and their clients. As a result, we urge FINRA to retain the NYSE exception in the Proposed Rule.

- Proposed Rule Should Not Mandate Policies and Procedures – FINRA asked commenters to offer their thoughts on whether the Proposed Rule should place a greater emphasis on firm level policies and procedures. The Proposed Rule's current language prohibits the origination and circulation of rumors and requires firms to report rumors to FINRA. FSI believes the Proposed Rule's general approach to the regulatory challenge is sound. By prohibiting the activity without mandating specific policies and procedures that must be adopted by member firms, FINRA provides its diverse membership the freedom to develop appropriate compliance measures for their unique business model. These compliance efforts will be subject to periodic review by FINRA examination staff. We believe this is the appropriate approach.
- Support Efforts to Quash Rumors – Finally, we would encourage FINRA and/or the SEC to provide firms with guidance on the steps they can take if they are the subject of false and misleading rumors that could affect the price of their securities. We believe firms must be allowed to discuss such rumors in their effort to quash them. We encourage FINRA to clarify that the Proposed Rule is not intended to interfere with these efforts.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with you to achieve further efficiency while maintaining investor protection.

Thank you for your consideration of our comments. Should you have any questions, please contact me at 770 980-8487.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Dale Brown", written in a cursive, flowing style.

Dale E. Brown, CAE
President & CEO