COMMONWEALTH *financial network*®

VIA ELECTRONIC MAIL

March 5, 2013

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

RE: Regulatory Notice 13-02 Recruitment Compensation Practices

Dear Ms. Asquith:

In its Regulatory Notice 13-02 ("Notice"), FINRA has proposed requiring member firms to disclose recruitment compensation arrangements to address potential conflicts of interest that could occur when member firms recruit registered representatives ("RRs") to join their firms. The proposed rule would require member firms to specifically disclose "enhanced compensation," as defined in the proposal, to an RR's clients before the clients transfer their existing accounts from the RR's "previous firm" to the recruiting firm.

Commonwealth Financial Network® ("Commonwealth") is an independent broker/dealer and an SEC-registered investment adviser with home office locations in Waltham, Massachusetts, and San Diego, California, and more than 1,600 RRs who are independent contractors conducting business in all 50 states.

Commonwealth appreciates the opportunity to comment on the proposed rule. Although we understand FINRA's concerns regarding the potential conflicts of interest that may occur when an RR changes firms, we strongly oppose the proposed requirement to disclose "enhanced compensation" arrangements, as that term is defined in the proposed rule. FINRA cites no enforcement actions, cases, or other empirical evidence that "enhanced compensation" creates a conflict of interest between RRs and clients.

Proposed FINRA Rule

The proposed rule is based on the flawed assumption that when recruiting firms offer enhanced compensation in the form of loans and other transition assistance, it creates a potential conflict of interest between an RR and a client. Although there may be financial reasons for an RR to leave one member firm for another, for a firm to provide a loan or other means of transition assistance to an RR solely as a means to help offset the substantial costs transitioning RRs routinely incur is not enough incentive for an RR to change firms, nor does such transition assistance create a conflict of interest between RRs and their clients.

Leaving a firm to join another firm is a costly and major disruption for an RR's practice and personal life. It is a decision that is based on many factors, and it is not taken lightly. Among the varied reasons often cited by RRs who leave their existing firms to join Commonwealth are material ownership or management changes at the previous firm, limited product choice or pressure to sell proprietary products, inferior service from the previous firm's home office staff, outdated technology, or a desire for more independence to manage their practice in a way that best serves clients.

Transitioning from one firm to another generally takes approximately two to three months, during which time the RR is not generating substantial revenue or able to engage in normal business development activities. The transition assistance provided by Commonwealth and many other "independent contractor" broker/dealers to a transitioning RR does not provide a meaningful incentive for the RR to leave his or her firm to join Commonwealth. Rather, the transition assistance is simply designed to provide the RR with sufficient working capital to help offset the substantial costs incurred and the revenues lost as the RR works through the laborious and time-intensive process of changing broker/dealers. Even though RRs are not able to engage in substantial revenue-producing activity during the transition, they must continue to pay staff salaries and overhead; often incur costs associated with the acquisition of new office space, equipment, and furnishings; and must pay other associated up-front costs for printing new stationery, business cards, signage, and the like.

Commonwealth's transition assistance is therefore designed to help put the RR in roughly the same position as the RR would have been had he or she not changed broker/dealers. Such transition assistance is by no means sufficient enough to provide the RR with a material financial benefit that would rise to the level of creating a conflict of interest with clients.

Definition of "Enhanced Compensation"

FINRA's proposed definition of enhanced compensation is overly broad. The proposed definition, "enhanced compensation includes but is not limited to signing bonuses, upfront or back-end bonuses, loans, accelerated payouts, transition assistance, and similar arrangements, paid in connection with the transfer of securities employment (or association) to the recruiting member," should be narrowed to include only compensation that is substantial enough to present a material conflict of interest, after deducting all tangible costs incurred by the RR in making the transition.

FINRA must distinguish between signing bonuses and other cash payments that are intended to provide a material financial incentive to encourage RRs to switch firms, and loans and other transition assistance that are designed solely to help offset the substantial costs incurred by RRs when they transition from one firm to another. For example, transition assistance provided to RRs by firms in the form of reimbursements for account transfer fees or account closing fees that are charged to the RRs or their clients should be specifically excluded from the definition of enhanced compensation. Likewise, transition assistance that is designed to offset the loss of revenue that would have otherwise been earned by the RR were it not for making the transition, as well as new office acquisition, staffing, sales literature, mailing, and similar transition costs, should be excluded from the definition of enhanced compensation.

Loans to RRs transitioning from one member firm to another are usually either traditional loans with periodic payments of principal and interest or forgivable loans that are forgiven over time if the RR meets certain conditions, such as the length of time the RR remains associated with the new member firm. For example, a typical forgivable loan might forgive 20% of the principal for each year the RR remains registered with the new member firm. Firms may also offer loans to RRs based on the RRs' historical production at the previous firm. When these loans are provided as a means to help with the costs of transition and lost revenue, however, they do not create an incentive for RRs to engage in inappropriate sales conduct or, as described in the Notice, "an additional and significant layer of compensation on top of the commission payout grid compensation that the representative receives based on production at the new firm."

Existing FINRA Rules Addressing Conflicts of Interest

In the Notice, FINRA described the specific concerns regarding enhanced compensation packages and cited a 2009 open letter to broker/dealer CEOs from SEC Chairman Mary Schapiro[i]. Chairman Schapiro's letter stated that, ". . . if a registered representative is aware that he or she will receive enhanced compensation for hitting increased commission targets, the registered representative could be motivated to *churn customer accounts, recommend unsuitable investment products or otherwise engage in activity that generates commission revenue but is not in investors' interest.*" [emphasis added]

FINRA Rule 2111 already addresses churning, unsuitable recommendations, or other activity not in investors' interest. In addition, FINRA Rule 3010 requires member firms to maintain a system to supervise each RR that is reasonably designed to comply with applicable rules. These rules complement each other and create an effective regulatory framework to address the purported conflicts of interest outlined in Chairman Schapiro's letter. FINRA's proposed rule is unnecessary and redundant and overlaps existing Rules 2111 and 3010.

Investor Impact

The proposed rule would add more disclosures to an already overwhelming amount of paperwork clients must complete. Moreover, requiring disclosure of legitimate transition assistance that merely helps offset transition costs that are personally incurred by an RR and provide no net benefit to the RR would be materially misleading to the detriment of the RR, as it would imply that the RR had a financial incentive to make the switch when that simply was not the case. Additionally, FINRA runs the risk of creating a situation in which investors are bombarded with so much information that it becomes impossible to distinguish between truly important, material disclosure and misleading or factually inaccurate legalese. FINRA must exercise great care in its rulemaking to ensure that proposed rules provide for meaningful disclosures of material information. Investors deserve quality disclosures of material information rather than a vast quantity of disclosures of immaterial conflicts of interest.

Specific Requests for Comment

In addition to our general comments above, the following are Commonwealth's responses to FINRA's specific requests for comment regarding whether the proposed rule should:

- **Require written disclosure at first individualized contact in all instances, rather than allowing oral disclosure at this point.**

  Although we do not believe the disclosure of recruitment compensation is warranted, if FINRA adopts the rule, it should not require written disclosure at first individualized contact in all instances. When changing firms, some RRs notify their clients via telephone. If FINRA were to require written disclosure of compensation packages at the first individualized contact, it would force RRs to either meet with each client in person or provide the disclosure in a mass mailing. For large practices with hundreds of clients, this would make an already lengthy and burdensome process even more so. If FINRA adopts the rule, we urge you to allow RRs to provide the disclosures orally.

- **Apply to all customers recruited by the transferring registered person during the year after transfer.**

  There is no logical reason why the rule should apply to all customers. To do so would suggest that all recommendations or advice an RR provides to his or her clients in the year following a change of broker/dealer is somehow tainted by the enhanced compensation. Again, FINRA provides no evidence or basis for such an assumption.

- **Apply to a time period different from the proposed one year following the date the registered person associates with the recruiting member.**

  If FINRA adopts the rule, it should require the disclosure for no more than 90 days, which is the usual amount of transition time when RRs change firms.

- **Establish an amount different from the proposed $50,000 for a de minimis exception**.

  FINRA should adopt a much higher de minimis exception amount based upon a reasonable formula. The proposed $50,000 de minimis exception is a completely arbitrary figure that fails to consider the real and substantial costs incurred by many RRs who transition firms, and, depending upon the number of accounts an RR has, it may not even cover the costs of transfer fees (usually $75 or more per account), let alone the other costs discussed above. Instead of an arbitrary flat dollar amount, FINRA should exclude all reimbursements for customer account transfer and closing fees. In addition, since it often takes up to 90 days to substantially complete the transfer of an RR's business from one firm to another, FINRA should either exclude from the definition of enhanced compensation any form of transition assistance that is designed to offset costs and lost revenue during the transition period or, alternatively, create a de minimis exception for enhanced compensation packages that total less than 30% of an RR's gross dealer concession in the 12 months prior to the RR changing firms.

Again, we appreciate the opportunity to comment on the proposed rule, and we hope that FINRA reconsiders the proposal, as it would only create an additional disclosure to clients that is unnecessary and would provide no material benefit to investors.

If you have any questions regarding our comments or concerns, please contact me at 781.736.0700.

Sincerely,
Commonwealth Financial Network

/s/ Andrew Daniels
Managing Principal, Field Development

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[i] See "Open Letter to Broker-Dealer CEOs from SEC Chairman Mary L. Schapiro," dated August 31, 2009