



FINANCIAL  
SERVICES  
ROUNDTABLE

*Via electronic mail at [pubcom@finra.org](mailto:pubcom@finra.org)*

May 22, 2014

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

**Re: Retrospective Rule Review of Gifts and Gratuities and Non-Cash Compensation Rules; and Communications With the Public Rules (the “Retrospective Review”)**

Dear Ms. Asquith:

The Financial Services Roundtable (“FSR”)<sup>1</sup> respectfully submits these comments concerning the Financial Industry Regulatory Authority’s (“FINRA”) Retrospective Rule Review<sup>2</sup> of the Effectiveness and Efficacy of FINRA’s (1) Communications With the

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<sup>1</sup> *As advocates for a strong financial future*<sup>TM</sup>, FSR represents the largest integrated financial services companies providing banking, insurance, payment and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. FSR member companies provide fuel for America’s economic engine, accounting directly for \$92.7 trillion in managed assets, \$1.2 trillion in revenue, and 2.3 million jobs. Learn more at [FSRoundtable.org](http://FSRoundtable.org).

<sup>2</sup> Retrospective Rule Review, FINRA Requests Comment on the Effectiveness and Efficiency of its Communications With the Public Rules, Regulatory Notice 14-14 (“Regulatory Notice 14-14”), *available at* <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p479810.pdf>; Retrospective Rule Review, FINRA Requests Comment on the Effectiveness and Efficiency of its Gifts and Gratuities and Non-Cash Compensation Rules, Regulatory Notice 14-15 (“Regulatory Notice 14-15”), *available at* <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p479811.pdf>.

Public Rules (“Communications Rules”)<sup>3</sup> and (2) Gifts and Gratuities and Non-Cash Compensation Rules (“Gifts Rules”).<sup>4</sup> The industry has identified several relevant issues since the adoption of these rules that hinder their effectiveness and efficacy. In this letter, FSR has proposed alternatives to resolve these issues, which we believe that FINRA should address as part of its Retrospective Review.

### **Introduction**

FSR supports FINRA’s role as a regulator and as a bulwark against unlawful behavior, and it applauds FINRA’s efforts on those fronts. FSR appreciates FINRA’s recognition of the need to look back at significant rulemakings and to determine whether those rules and rule sets are meeting their intended investor-protection objectives by reasonably efficient means. FSR agrees that by thoroughly assessing the impact of existing rules, FINRA will be able to ensure that its rules remain pertinent to current industry and market conditions and carefully tailored to protect the interests of the investing public. For these reasons, FSR takes this opportunity to comment on the Retrospective Review and suggest certain improvements that we believe would enhance the effectiveness and efficacy of these rules.

### **Communications With the Public Rules**

FINRA has asked for comment on its Communications Rules, which govern, among other things, advertising and marketing materials. FSR recommends that FINRA focus on three particular issues, as follows.

First, the content and application of the Communications Rules have shifted towards a product-by-product approach, instead of more principles-based concepts.<sup>5</sup> By developing new rules and interpretations of ever more complexity and specificity, FINRA has made compliance increasingly more difficult to administer. This result seems at odds with the idea that member firms should strive for more effective, intelligible communications with their customers and others. Instead, firms are subject to so many technical requirements in their communications with the public that it becomes harder to

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<sup>3</sup> FINRA Rules 2210, 2212, 2213, 2214, 2215, 2216.

<sup>4</sup> FINRA Rules 3220, 2310(c), 2320(g)(4), 5110(h) and NASD Rule 2830(l)(5).

<sup>5</sup> *See, e.g.*, FINRA Rule 2215, 2216.

write in plain English and present easily understood material that is not obscured by too many disclosures.

As an alternative, FSR proposes a principles-based approach that would provide guidance on written communications through the use of broad content standards that are flexible and forward-looking enough to address new products as they arise. Such an approach would give FINRA more flexibility in administering the rule, ease the compliance burden on its members and achieve more efficient outcomes. Most importantly, it would encourage more straightforward writing that is easier for customers to understand.

Second, FSR believes that the blanket prohibition in FINRA Rule 2210(d)(1)(F) against predictions or projections of investment performance inhibits customers from receiving the valuable information that they often demand. FSR believes that such a blanket restriction is overly burdensome, out of touch with customer requests (especially by institutional accounts) and inconsistent with the principles-based approach outlined in Rule 2210(d)(1) and advocated above.

Financial projections play an important role in educating investors and allowing them to compare products. They provide an important insight into what an investment manager seeks to achieve. The Securities and Exchange Commission (“SEC”) permits investment advisers to give projections of investment performance,<sup>6</sup> and the same should be true of broker-dealers, particularly if they are simply passing along materials produced by investment advisers. Of course, the rules should require that such projections meet the other content standards, including that they have a reasonable basis, are fair and balanced, and include a discussion of downside possibilities, consistent with the approach taken in Section 21E of the Securities Exchange Act of 1934<sup>7</sup> and Section 27A of the Securities Act of 1933.<sup>8</sup> FSR does not see any reason why properly developed and explained projections should not be permissible in communications to the public, especially to institutional accounts.

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<sup>6</sup> See Clover Capital Management, Inc., SEC No-Action Letter, (October 28, 1986), *available at* <http://www.sec.gov/divisions/investment/noaction/clovercapital102886.htm>.

<sup>7</sup> 15 U.S.C. § 78u-5 (Application of safe harbor for forward-looking statements).

<sup>8</sup> 15 U.S.C. § 77z-2 (Application of safe harbor for forward-looking statements).

Finally, FSR believes that the current interpretation of FINRA Rule 2210, which prohibits disclosure of “related performance” in sales material<sup>9</sup> with limited exceptions, overly restricts investors’ access to information crucial to the decision-making process. While FSR recognizes the dangers of fraudulent advertising, information concerning related performance offers investors a powerful tool that allows them to evaluate a fund manager’s strategies and the fund’s compatibility with their investment goals. Additionally, related performance is one of the only ways an investor can evaluate a new fund; restricting access to such information can make it difficult for investors to make an informed decision with respect to such funds.

Both the SEC<sup>10</sup> and the Commodities Futures Trading Commission (“CFTC”)<sup>11</sup> permit disclosure of related performance subject to certain limitations; the CFTC even requires disclosure of related performance for commodity pool operators under certain circumstances.<sup>12</sup> In addition, current interpretations of FINRA Rule 2210 permit disclosure of related performance information by private funds to “qualified purchasers” under Section 2(a)(51) of the 1940 Act.<sup>13</sup> FSR is aware of the heightened investor protection concerns relating to retail investors, but believes that the blanket restriction on the disclosure of related performance information to retail investors is overly broad so as to restrict investors’ access to entire classes of information that do not pose a heightened risk of manipulation but that may be highly relevant to the decision-making process.

To that end, FSR proposes that FINRA revive its 1998 proposal to allow for disclosure of related performance information in the context of “Clone” Performance, “Predecessor” Performance and “Comparison Portfolio” Performance.<sup>14</sup> The 1998

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<sup>9</sup> See FINRA Rule 2210; Interpretive Letter from Gary L. Goldsholle, FINRA to Michael D. Udoff, Securities Industry Association (Oct. 2, 2003).

<sup>10</sup> See 12 CFR 275.206(4)-1 (Advertisements by investment advisers).

<sup>11</sup> See 12 CFR 4.24(n), 4.25.

<sup>12</sup> See *id.*

<sup>13</sup> See FINRA Rule 2210; Interpretive Letter from Thomas M. Selman, FINRA to Yukako Kawata, Davis Polk & Wardwell on behalf of Credit Suisse First Boston (Dec. 30, 2003).

<sup>14</sup> Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1, 2, and 3 by the National Association of Securities Dealers, Inc. Concerning Related Performance Information, 65 Fed. Reg. 67025 (Nov. 8, 2000) (the “1998 Proposal”).

proposal correctly identifies three classes of related performance in the context of mutual funds that, given their characteristics, provide minimal opportunity for abuse while greatly enhancing investor access to relevant information. FSR believes the 1998 proposal is a step in the right direction in balancing the twin objectives of investor protection and investor access to information.

### **Gifts and Gratuities**

FINRA also has asked for comments on its Gifts and Gratuities Rules. While FSR supports the investor-protection objectives of the adopted rules, it has concerns about the unintended consequences of the rules, which are outlined below.

#### Rule 3220(a)

FINRA Rule 3220(a) places an annual \$100 hard cap on gifts and gratuities by a member or associated person to each recipient. This limit has been unmodified since its inception. FSR recognizes the inherent danger of excessive gifts and gratuities, but it believes that such a low cap is overly burdensome and has, in practice, required members to dedicate an excessive amount of compliance resources to reviewing such gifts, many of which have not historically presented compliance problems.

FSR proposes two non-exclusive alternative approaches. The first alternative would be a higher cap, for example \$500, which would be indexed for inflation so that the cap would not have the unintended effect of decreasing in real terms from year-to-year. A higher cap would alleviate the compliance burden on members while simultaneously addressing concerns relating to truly excessive gifts and gratuities.

The second alternative would be to apply a principles-based approach, similar to the approach implemented with respect to “ordinary and usual business entertainment.”<sup>15</sup> Under this alternative, each member firm would establish its own policies and limitations with respect to gifts, just as it does with respect to entertainment. This approach would allow members to take account of their varying businesses to establish appropriate limits by, for example, type of customer, product line or other relevant category. Firms could implement approvals for gifts over amounts they would determine. By allowing firms to tailor their policies on gifts to meet the needs of their business, FINRA would create

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<sup>15</sup> See FINRA Rule 2310(c); Interpretive Letter from R. Clark Hooper, FINRA to Henry H. Hopkins & Sarah McCafferty, T. Rowe Price Investment Services, Inc. (June 10, 1999).

incentives for reasonable behavior, rather than a “one size fits all” mentality. This approach also would relieve the burden on compliance departments by allowing them to take a risk-based approach to reviewing gift and gratuities transactions, and allocate their resources to more significant transactions.

FINRA Rule 2320(g)

FINRA Rule 2320(g)(4)(C) provides that, in connection with the sale and distribution of variable contracts, non-cash compensation is permitted in the form of payment of reimbursement by offerors in connection with training or education meetings of the associated persons of a member. The rule does not, however, permit any kind of entertainment in connection with these meetings. While FSR agrees that lavish entertainment is inappropriate in this context, offerors should be permitted, for example, to take associated persons to a sporting event or to the theater, provided that the meetings themselves are in fact training and educational. Permitting such forms of entertainment would not foster abuses and would be consistent with the purposes of the rule, including Rule 2320(g)(4)(B). FSR proposes that entertainment in connection with training or education meetings be subject to a principles-based approach, similar to the alternative approach suggested above with respect to gifts and gratuities under Rule 3220(a). Such an approach should allay any concerns relating to lavish entertainment and is consistent with FINRA’s approach towards “ordinary and usual business entertainment”.<sup>16</sup>

FINRA Rule 2320(g)(4)(D) permits non-cash compensation arrangements between a broker-dealer and its associated persons relating to variable securities. It imposes several conditions, including (i) that such arrangements are based on the total production of the relevant associated person with respect to all variable contract securities distributed by the member, and (ii) that credit received for each such variable contract security arrangements are equally weighted.

FSR believes that it should be permissible for a broker-dealer to contribute all or a portion of the cost for its associated person(s) to attend permissible training or education meetings under this rule. However, the conditions of the rule make it impractical to do so, because the cost of a training or education seminar ordinarily is standardized and does not take account of an associated person’s production. Thus, if the broker-dealer seeks to send two associated persons to the event, there is no way to weight their production in paying the cost. FSR recommends that the rule be modified to either allow the payor to

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<sup>16</sup> *See id.*

rely on the event review by the member holding the event, or, in the alternative, to require the member to certify to the payor that the event meets all of the requirements of FINRA Rule 2320(g)(4)(D).

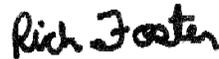
## **Conclusion**

We commend FINRA for undertaking the Retrospective Review of its Communications Rules and its Gifts and Gratuities Rules. FSR believes its proposals for resolving the issues raised in this letter would contribute significantly to the effectiveness and efficacy of these rules.

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FSR appreciates the opportunity to submit comments on FINRA's Retrospective Review. If it would be helpful to discuss FSR's specific comments or general views on this issue, please contact [Richard.Foster@FSRoundtable.org](mailto:Richard.Foster@FSRoundtable.org).

Sincerely Yours,



Richard Foster  
Vice President and Senior Counsel for Legal  
and Regulatory Affairs  
Financial Services Roundtable