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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2015 - * 054
Amendment No. (req. for Amendments *)

Filing by Financial Industry Regulatory Authority

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial *	Amendment *	Withdrawal	Section 19(b)(2) *	Section 19(b)(3)(A) *	Section 19(b)(3)(B) *
☑	☐	☐	☑	☐	☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule
☐ 19b-4(f)(1) ☐ 19b-4(f)(4)
☐ 19b-4(f)(2) ☐ 19b-4(f)(5)
☐ 19b-4(f)(3) ☐ 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐

Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document ☐

Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Proposed rule change to create a separate rule set that would apply to firms that meet the definition of capital acquisition broker and elect to be governed under this rule set.

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Joseph
Last Name * Savage
Title * Vice President and Counsel
E-mail * joseph.savage@finra.org
Telephone * (240) 386-4534
Fax (240) 386-4572

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 12/04/2015

By Philip Shaikun

(Name *)

(Title *)

Vice President and Associate General Counsel

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Philip Shaikun, Philip.Shaikun@Finra.org

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information * Add Remove View	The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.
Exhibit 1 - Notice of Proposed Rule Change * Add Remove View	The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)
Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies * Add Remove View	The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)
Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications Add Remove View Exhibit Sent As Paper Document ☐	Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.
Exhibit 3 - Form, Report, or Questionnaire Add Remove View Exhibit Sent As Paper Document ☐	Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.
Exhibit 4 - Marked Copies Add Remove View	The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.
Exhibit 5 - Proposed Rule Text Add Remove View	The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.
Partial Amendment Add Remove View	If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act, ” “Exchange Act” or “SEA”),[1] Financial Industry Regulatory Authority, Inc. (“FINRA”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to create a separate rule set that would apply to firms that meet the definition of “capital acquisition broker” and elect to be governed under this rule set.

The text of the proposed rule change is attached as Exhibit 5 to this rule filing.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

At its meeting on December 5, 2013, the FINRA Board of Governors authorized the filing of the proposed rule change with the SEC; no other action by FINRA is necessary for the filing of the proposed rule change.

If the Commission approves the proposed rule change, FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 180 days following publication of the Regulatory Notice announcing Commission approval.

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[1] 15 U.S.C. 78s(b)(1).

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

There are FINRA firms that are solely corporate financing firms that advise companies on mergers and acquisitions, advise issuers on raising debt and equity capital in private placements with institutional investors, or provide advisory services on a consulting basis to companies that need assistance analyzing their strategic and financial alternatives. These firms often are registered as broker-dealers because they may receive transaction-based compensation as part of their services.

Nevertheless, these firms do not engage in many of the types of activities typically associated with traditional broker-dealers. For example, these firms typically do not carry or act as an introducing broker with respect to customer accounts, handle customer funds or securities, accept orders to purchase or sell securities either as principal or agent for the customer, exercise investment discretion on behalf of any customer, or engage in proprietary trading of securities or market-making activities.

FINRA is proposing to establish a separate rule set that would apply exclusively to firms that meet the definition of "capital acquisition broker" ("CAB") and that elect to be governed under this rule set. CABs would be subject to the FINRA By-Laws, as well as core FINRA rules that FINRA believes should apply to all firms. The rule set would include other FINRA rules that are tailored to address CABs' business activities.

General Standards (CAB Rule 010 Series)

Proposed CAB Rule 014 provides that all persons that have been approved for membership in FINRA as a CAB and persons associated with CABs shall be subject to the Capital Acquisition Broker rules and the FINRA By-Laws (including the schedules thereto), unless the context requires otherwise. Proposed CAB Rule 015 provides that FINRA Rule 0150(b) shall apply to the CAB rules. FINRA Rule 0150(b) currently provides that the FINRA rules do not apply to transactions in, and business activities relating to, municipal securities as that term is defined in the Exchange Act.

CAB Rule 016 sets forth basic definitions modified as appropriate to apply to CABs. The proposed definitions of "capital acquisition broker" and "institutional investor" are particularly important to the application of the rule set.

The term "capital acquisition broker" would mean any broker that solely engages in any one or more of the following activities:

- advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions, valuation services, expert testimony, litigation support, and negotiation and structuring services;
- qualifying, identifying, soliciting, or acting as a placement agent or finder with respect to institutional investors in connection with purchases or sales of unregistered securities; and
- effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company through the purchase, sale,

exchange, issuance, repurchase, or redemption of, or a business combination involving, securities or assets of the company, to a buyer that will actively operate the company or the business conducted with the assets of the company, in accordance with the terms and conditions of an SEC rule, release, interpretation or "no-action" letter that permits a person to engage in such activities without having to register as a broker or dealer pursuant to Section 15(b) of the Exchange Act.[2]

A firm would be permitted to register as, or change its status to, a CAB only if the firm solely engages in one or more of these activities.

The term "capital acquisition broker" would not include any broker or dealer that:

- carries or acts as an introducing broker with respect to customer accounts;
- holds or handles customers' funds or securities;
- accepts orders from customers to purchase or sell securities either as principal or as agent for the customer (except as permitted by paragraphs (c)(1)(F) and (G) of CAB Rule 016);
- has investment discretion on behalf of any customer;
- engages in proprietary trading of securities or market-making activities; or
- participates in or maintains an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933.[3]

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2 See proposed CAB Rule 016(c)(1).

3 See proposed CAB Rule 016(c)(2).

The term “institutional investor” would have the same meaning as that term has under FINRA Rule 2210 (Communications with the Public), with one exception. The term would include any:

- bank, savings and loan association, insurance company or registered investment company;
- governmental entity or subdivision thereof;
- employee benefit plan, or multiple employee benefit plans offered to employees of the same employer, that meet the requirements of Section 403(b) or Section 457 of the Internal Revenue Code and in the aggregate have at least 100 participants, but does not include any participant of such plans;
- qualified plan, as defined in Section 3(a)(12)(C) of the Exchange Act, or multiple qualified plans offered to employees of the same employer, that in the aggregate have at least 100 participants, but does not include any participant of such plans;
- other person (whether a natural person, corporation, partnership, trust, family office or otherwise) with total assets of at least $50 million; and
- person acting solely on behalf of any such institutional investor.

The definition also would include any person meeting the definition of “qualified purchaser” as that term is defined in Section 2(a)(51) of the Investment Company Act of 1940 (“1940 Act”).[4]

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[4] See proposed CAB Rule 016(i). FINRA Rule 2210 does not include “qualified purchaser” within its definition of “institutional investor.”

Member Application and Associated Person Registration (CAB Rule 100 Series)

The proposed CAB Rule 100 Series sets forth the requirements for firms that wish to register as a CAB. The proposed CAB Rule 100 Series generally incorporates by reference FINRA Rules 1010 (Electronic Filing Requirements for Uniform Forms), and 1122 (Filing of Misleading Information as to Membership or Registration), and NASD Rules 1011 (Definitions), 1012 (General Provisions), 1013 (New Member Application and Interview), 1014 (Department Decision), 1015 (Review by National Adjudicatory Council), 1016 (Discretionary Review by FINRA Board), 1017 (Application for Approval of Change in Ownership, Control, or Business Operations), 1019 (Application to Commission for Review), 1090 (Foreign Members), 1100 (Foreign Associates) and IM-1011-1 (Safe Harbor for Business Expansions). Accordingly, a CAB applicant would follow the same procedures for membership as any other FINRA applicant, with four modifications.

- First, an applicant for membership that seeks to qualify as a CAB would have to state in its application that it intends to operate solely as such.
- Second, in reviewing an application for membership as a CAB, the FINRA Member Regulation Department would consider, in addition to the standards for admission set forth in NASD Rule 1014, whether the applicant's proposed activities are consistent with the limitations imposed on CABs under CAB Rule 016(c).
- Third, proposed CAB Rule 116(b) sets forth the procedures for an existing FINRA firm to change its status to a CAB. If an existing firm is already approved to engage in the activities of a CAB, and the firm does not intend to

change its existing ownership, control or business operations, it would not be required to file either a New Member Application ("NMA") or a Change in Membership Application ("CMA"). Instead, such a firm would be required to file a request to amend its membership agreement or obtain a membership agreement (if none exists currently) to provide that: (i) the firm's activities will be limited to those permitted for CABs under CAB Rule 016(c), and (ii) the firm agrees to comply with the CAB rules.[5]

- Fourth, proposed CAB Rules 116(c) and (d) set forth the procedures for an existing CAB to terminate its status as such and continue as a FINRA firm. Under Rule 116(c), such a firm would be required to file a CMA with the FINRA Member Regulation Department, and to amend its membership agreement to provide that the firm agrees to comply with all FINRA rules.[6]

Under Rule 116(d), however, if during the first year following an existing FINRA member firm's amendment to its membership agreement to convert a full-service broker-dealer to a CAB pursuant to Rule 116(b) a CAB seeks to terminate its status as such and continue as a FINRA member firm, the CAB may notify the FINRA Membership Application Program group of this change without having to file an application for approval of a material change in business operations pursuant to NASD Rule 1017. The CAB would instead file a request to amend its membership agreement to provide that the member firm agrees to comply with all FINRA rules, and execute an amended

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5 There would not be an application fee associated with this request.

6 Absent a waiver, such a firm would have to pay an application fee associated with the CMA. See FINRA By-Laws, Schedule A, Section 4(i).

membership agreement that imposes the same limitations on the member firm's activities that existed prior to the member firm's change of status to a CAB.[7]

The proposed CAB Rule 100 Series also would govern the registration and qualification examinations of principals and representatives that are associated with CABs. These Rules incorporate by reference NASD Rules 1021 (Registration Requirements – Principals), 1022 (Categories of Principal Registration), 1031 (Registration Requirements – Representatives), 1032 (Categories of Representative Registration), 1060 (Persons Exempt from Registration), 1070 (Qualification Examinations and Waiver of Requirements), 1080 (Confidentiality of Examinations), IM-1000-2 (Status of Persons Serving in the Armed Forces of the United States), IM-1000-3 (Failure to Register Personnel) and FINRA Rule 1250 (Continuing Education Requirements). Accordingly, CAB firm principals and representatives would be subject to the same registration, qualification examination, and continuing education requirements as principals and representatives of other FINRA firms. CABs also would be subject to FINRA Rule 1230(b)(6) regarding Operations Professional registration.

<u>Duties and Conflicts (CAB Rule 200 Series)</u>

The proposed CAB Rule 200 Series would establish a streamlined set of conduct rules. CABs would be subject to FINRA Rules 2010 (Standards of Commercial Honor and Principles of Trade), 2020 (Use of Manipulative, Deceptive or Other Fraudulent

[7] To the extent that the rules applicable to the member firm had been amended since it had changed its status to a CAB, FINRA would have the discretion to modify any limitations to reflect any new rule requirements.

Devices), 2040 (Payments to Unregistered Persons),[8] 2070 (Transactions Involving FINRA Employees), 2080 (Obtaining an Order of Expungement of Customer Dispute Information from the CRD System), 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information), 2263 (Arbitration Disclosure to Associated Persons Signing or Acknowledging Form U4), and 2268 (Requirements When Using Predispute Arbitration Agreements for Customer Accounts).

CAB Rules 209 and 211 would impose know-your-customer and suitability obligations similar to those imposed under FINRA Rules 2090 and 2111. CAB Rule 211(b) includes an exception to the customer-specific suitability obligations for institutional investors similar to the exception found in FINRA Rule 2111(b).

Proposed CAB Rule 221 is an abbreviated version of FINRA Rule 2210 (Communications with the Public), essentially prohibiting false and misleading statements.

Under proposed CAB Rule 240, if a CAB or associated person of a CAB had engaged in activities that would require the CAB to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on CABs under CAB Rule 016(c), FINRA could examine for and enforce all FINRA rules against such a broker or associated person, including any rule that applies to a FINRA broker-dealer that is not a CAB or to an associated person who is not a person associated with a CAB.

FINRA has determined not to subject CABs to FINRA Rules 2121 (Fair Prices and Commissions), 2122 (Charges for Services Performed), and 2124 (Net Transactions

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8 The SEC has approved FINRA's rule change to adopt rules relating to payments to unregistered persons for the consolidated FINRA rulebook. See Regulatory Notice 15-07 (March 2015). FINRA Rule 2040 became effective on August 24, 2015.

with Customers), since CABs' business model does not raise the same concerns that Rules 2121, 2122 and 2124 are intended to address.

Rule 2121 provides that, for securities in both listed and unlisted securities, a member that buys for its own account from its customer, or sells for its own account to its customer, shall buy or sell at a price which is fair, taking into consideration all relevant circumstances, including market conditions with respect to the security at the time of the transaction, the expense involved, and the fact that the member is entitled to a profit. Further, if the member acts as agent for its customer in any such transaction, the member shall not charge its customer more than a fair commission or service charge, taking into consideration all relevant circumstances, including market conditions with respect to the security at the time of the transaction, the expense of executing the order and the value of any service the member may have rendered by reason of its experience in and knowledge of such security and the market therefor.

CABs would not be permitted to act as a principal in a securities transaction. Accordingly, the provisions of Rule 2121 that govern principal transactions would not apply to a CAB's permitted activities.

CABs would be permitted act as agent in a securities transaction only in very narrow circumstances. CABs would be allowed to act as an agent with respect to institutional investors in connection with purchases or sales of unregistered securities. CABs also would be permitted to effect securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company or the business conducted with the assets of the company in accordance with the terms and conditions of an SEC rule, release, interpretation or "no-action" letter.

In both instances, FINRA believes that these circumstances either involve institutional parties that negotiate the terms of permitted securities transactions without the need for the conditions set forth in Rule 2121, or involve the sale of a business as a going concern, which differs in nature from the types of transactions that typically raise issues under Rule 2121.

Rule 2122 provides that charges, if any, for services performed, including, but not limited to, miscellaneous services such as collections due for principal, dividends, or interest; exchange or transfer of securities; appraisals, safekeeping or custody of securities, and other services shall be reasonable and not unfairly discriminatory among customers. As discussed above, CABs typically provide services to institutional customers that generally do not need the protections that Rule 2122 offers, since these customers are capable of negotiating fair prices for the services that CABs provide. Moreover, CABs are not permitted to provide many of the services listed in Rule 2122, such as collecting principal, dividends or interest, or providing safekeeping or custody services.

Rule 2124 sets forth specific requirements for executing transactions with customers on a "net" basis. "Net" transactions are defined as a type of principal transaction, and CABs may not trade securities on a principal basis. For these reasons, FINRA does not believe it is necessary to include FINRA Rules 2121, 2122 and 2124 as part of the CAB rule set.

CAB Rule 201 would subject CABs to FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade), which requires a member, in the conduct of its business, to observe high standards of commercial honor and just and equitable principles of trade. Depending on the facts, other rules, such as Rule 2010, may apply in situations in which a CAB charged a commission or fee that clearly is unreasonable under the circumstances.

<u>Supervision and Responsibilities Related to Associated Persons (CAB Rule 300 Series)</u>

The proposed CAB Rule 300 Series would establish a limited set of supervisory rules for CABs. CABs would be subject to FINRA Rules 3220 (Influencing or Rewarding Employees of Others), 3240 (Borrowing from or Lending to Customers), and 3270 (Outside Business Activities of Registered Persons).

Proposed CAB Rule 311 would subject CABs to some, but not all, of the requirements of FINRA Rule 3110 (Supervision) and, consistent with Rule 3110, is designed to provide CABs with the flexibility to tailor their supervisory systems to their business models. CABs would be subject to many of the provisions of Rule 3110 concerning the supervision of offices, personnel, customer complaints, correspondence and internal communications. However, CABs would not be subject to the provisions of Rule 3110 that require annual compliance meetings (paragraph (a)(7)), review and investigation of transactions (paragraphs (b)(2) and (d)), specific documentation and supervisory procedures for supervisory personnel (paragraph (b)(6)), and internal inspections (paragraph (c)).

FINRA does not believe that the annual compliance meeting requirement in FINRA Rule 3110(a)(7) should apply to CABs given the nature of CABs' business model and structure. FINRA has observed that most current FINRA member firms that would qualify as CABs tend to be small and often operate out of a single office. In addition, the range of rules that CABs would be subject to is narrower than the rules that apply to other broker-dealers. Moreover, as noted above, CABs would be subject to both the Regulatory and Firm Element continuing education requirements. Accordingly, FINRA does not believe that CABs need to conduct an annual compliance meeting as required under FINRA Rule 3110(a)(7).[9] The fact that the annual compliance meeting requirement would not apply to CABs or their associated persons in no way would reduce their responsibility to have knowledge of and comply with applicable securities laws and regulations and the CAB rule set.

FINRA does not believe that FINRA Rule 3110(b)(2), which requires members to adopt and implement procedures for the review by a registered principal of all transactions relating to the member's investment banking or securities business, or FINRA Rule 3110(d), which imposes requirements related to the investigation of securities transactions and heightened reporting requirements for members engaged in investment banking services, should apply to CABs. CABs would not be permitted to carry or act as an introducing broker with respect to customer accounts, hold or handle customers' funds or securities, accept orders from customers to purchase or sell securities except under the narrow circumstances discussed above, have investment discretion on behalf of any customer, engage in proprietary trading or market-making activities, or

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[9] For the same reasons, FINRA does not believe that FINRA Rule 3110.04 should apply to CABs.

participate in Crowdfunding or Regulation A securities offerings. Accordingly, due to these restrictions, FINRA does not believe a CAB's business model necessitates the application of these provisions, which primarily address trading and investment banking functions that are beyond the permissible scope of a CAB's activities.[10]

FINRA does not believe that the requirements of FINRA Rule 3110(b)(6) should apply to CABs. Paragraph (b)(6) generally requires a member to have procedures to prohibit its supervisory personnel from (1) supervising their own activities; and (2) reporting to, or having their compensation or continued employment determined by, a person the supervisor is supervising.[11] FINRA also does not believe that FINRA Rule 3110(c), which requires members to conduct internal inspections of their businesses, should apply to CABs.

FINRA believes that a CAB's business model, which is geared toward acting as a consultant in capital acquisition transactions, or acting as an agent solely in connection with purchases or sales of unregistered securities to institutional investors, or with the transfer of ownership and control of a privately-held company, does not give rise to the same conflicts of interest and supervisory concerns that paragraph (b)(6) is intended to

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[10] For the same reasons, FINRA does not believe that FINRA Rule 3110.05 should apply to CABs.

[11] FINRA Rule 3110(b)(6)(C)(i) and (ii). FINRA Rule 3110(b)(6) also requires that a member's supervisory procedures include the titles, registration status and locations of the required supervisory personnel and the responsibilities of each supervisory person as these relate to the types of business engaged in, applicable securities laws and regulations, and FINRA rules, as well as a record of the names of its designated supervisory personnel and the dates for which such designation is or was effective. FINRA Rule 3110(b)(6)(A) and (B). In addition, paragraph (b)(6) requires a member to have procedures reasonably designed to prevent the standards of supervision required pursuant to FINRA Rule 3110(a) from being compromised due to the conflicts of interest that may be present with respect to an associated person being supervised. FINRA Rule 3110(b)(6)(D).

address. As discussed above, many CABs operate out of a single office with a small staff, which reduces the need for internal inspections of numerous or remote offices. In addition, part of the purpose of creating a separate CAB rule set is to streamline and reduce existing FINRA rule requirements where it does not hinder investor protection. FINRA believes that the remaining provisions of FINRA Rule 3110, coupled with the CAB Rule 200 Series addressing duties and conflicts, will sufficiently protect CABs' customers from potential harm due to insufficient supervision.[12]

Proposed CAB Rule 313 would require CABs to designate and identify one or more principals to serve as a firm's chief compliance officer, similar to the requirements of FINRA Rule 3130(a). CAB Rule 313 would not require a CAB to have its chief executive officer ("CEO") certify that the member has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable federal securities laws and regulations, and FINRA and MSRB rules, which are required under FINRA Rules 3130(b) and (c). FINRA does not believe the CEO certification is necessary given a CAB's narrow business model and smaller rule set.

Proposed Rule 328 would prohibit any person associated with a CAB from participating in any manner in a private securities transaction as defined in FINRA Rule

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12 For the same reasons, FINRA does not believe that FINRA Rules 3110.10, .12, .13, or .14 should apply to CABs. FINRA also believes that it is unnecessary to apply FINRA Rule 3110.15 to CABs, since the temporary program authorized by the rule expired on December 1, 2015.

3280(e).[13] FINRA does not believe that an associated person of a CAB should be engaged in selling securities away from the CAB, nor should a CAB have to oversee and review such transactions, given its limited business model. This restriction would not prohibit associated persons from investing in securities on their own behalf, or engaging in securities transactions with immediate family members, provided that the associated person does not receive selling compensation.

Proposed CAB Rule 331 would require each CAB to implement a written anti-money laundering ("AML") program. This is consistent with the SEC's requirements and Chapter X of Title 31 of the Code of Federal Regulations. Accordingly, the proposed rule is similar to FINRA Rule 3310 (Anti-Money Laundering Compliance Program); however, the proposed rule contemplates that all CABs would be eligible to conduct the required independent testing for compliance every two years.

Financial and Operational Rules (CAB Rule 400 Series)

The proposed CAB Rule 400 Series would establish a streamlined set of rules concerning firms' financial and operational obligations. CABs would be subject to FINRA Rules 4140 (Audit), 4150 (Guarantees by, or Flow through Benefits for, Members), 4160 (Verification of Assets), 4511 (Books and Records – General Requirements), 4513 (Records of Written Customer Complaints), 4517 (Member Filing

[13] FINRA Rule 3280(e) defines "private securities transaction" as "any securities transaction outside the regular course or scope of an associated person's employment with a member, including, though not limited to, new offerings of securities which are not registered with the Commission, provided however that transactions subject to the notification requirements of NASD Rule 3050, transactions among immediate family members (as defined in FINRA Rule 5130), for which no associated person receives any selling compensation, and personal transactions in investment company and variable annuity securities, shall be excluded."

and Contact Information Requirements), 4524 (Supplemental FOCUS Information), 4530 (Reporting Requirements), and 4570 (Custodian of Books and Records).

Proposed CAB Rule 411 includes some, but not all, of the capital compliance requirements of FINRA Rule 4110. CABs would be required to suspend business operations during any period a firm is not in compliance with the applicable net capital requirements set forth in SEA Rule 15c3-1, and the rule also would authorize FINRA to direct a CAB to suspend its operation under those circumstances. Proposed CAB Rule 411 also sets forth requirements concerning withdrawal of capital, subordinated loans, notes collateralized by securities, and capital borrowings.

CABs would not be subject to FINRA Rules 4370 (Business Continuity Plans and Emergency Contact Information) or 4380 (Mandatory Participation in FINRA BC/DR Testing Under Regulation SCI). FINRA does not believe it would be necessary for a CAB to maintain a business continuity plan (BCP), given a CAB's limited activities, particularly since a CAB would not engage in retail customer account transactions or clearance, settlement, trading, underwriting or similar investment banking activities. Moreover, FINRA Rule 4380 relates to Rule SCI under the Exchange Act, which is not applicable to a member that limits its activities to those permitted under the CAB rule set.

Because CABs would not carry or act as an introducing broker with respect to customer accounts, they would have more limited customer information requirements than is imposed under FINRA Rule 4512.[14] CABs would have to maintain each customer's name and residence, whether the customer is of legal age (if applicable), and the names of any persons authorized to transact business on behalf of the customer.

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[14] See proposed CAB Rule 451(b).

CABs would still have to make and preserve all books and records required under SEA Rules 17a-3 and 17a-4.

CAB Rule 452(a) establishes a limited set of requirements for the supervision and review of a firm's general ledger accounts.

Securities Offerings (CAB Rule 500 Series)

The proposed CAB Rule 500 Series would subject CABs to certain rules concerning securities offerings. CABs would be subject to FINRA Rules 5122 (Private Placements of Securities Issued by Members) and 5150 (Fairness Opinions).

Investigations and Sanctions, Code of Procedure, and Arbitration and Mediation (CAB Rules 800, 900 and 1000)

CABs would be subject to the FINRA Rule 8000 Series governing investigations and sanctions of firms, other than FINRA Rules 8110 (Availability of Manual to Customers), 8211 (Automated Submission of Trading Data Requested by FINRA), and 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA).

CABs would not be subject to FINRA Rule 8110 (Availability of Manual to Customers), which requires members to make available a current copy of the FINRA manual for examination by customers upon request. If the Commission approves this proposed rule change, the CAB rule set would be available through the FINRA website. Accordingly, FINRA does not believe this rule is necessary for CABs.

CABs also would not be subject to FINRA Rules 8211 (Automated Submission of Trading Data Requested by FINRA) or 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA). Given that these rules are intended to assist FINRA in requesting trade data from firms engaged in securities trading, and that CABs would not engage in securities trading, FINRA does not believe that these rules should apply to CABs.

CABs would be subject to the FINRA Rule 9000 Series governing disciplinary and other proceedings involving firms, other than the FINRA Rule 9700 Series (Procedures on Grievances Concerning the Automated Systems). Proposed CAB Rule 900(c) would provide that any CAB may be subject to a fine under FINRA Rule 9216(b) with respect to an enumerated list of FINRA By-Laws, CAB rules and SEC rules under the Exchange Act. Proposed CAB Rule 900(d) would authorize FINRA staff to require a CAB to file communications with the FINRA Advertising Regulation Department at least ten days prior to use if the staff determined that the CAB had departed from CAB Rule 221's standards.

CABs would be subject to the FINRA Rule 12000 Series (Code of Arbitration Procedure for Customer Disputes), 13000 Series (Code of Arbitration Procedure for Industry Disputes) and 14000 Series (Code of Mediation Procedure).

As noted in Item 2 of this filing, if the Commission approves the proposed rule change, FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 180 days following publication of the Regulatory Notice announcing Commission approval.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,[15] which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will improve efficiency and reduce regulatory burden by reducing the range of rules that apply to capital acquisition brokers given their limited activities and institutional business model, while maintaining necessary investor protections.

4. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. FINRA has undertaken an economic impact assessment, as set forth below, to analyze the regulatory need for the proposed rulemaking, its potential economic impacts, including anticipated costs and benefits, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

Economic Impact Assessment

A. Regulatory Need

As discussed above, many firms solely engage in corporate financing activities, including advising companies on mergers and acquisitions, advising issuers on raising debt and equity capital in private placements with institutional investors, or providing advisory services on a consulting basis. These firms often register as broker-dealers

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[15] 15 U.S.C. 78o–3(b)(6).

because they may receive transaction-based compensation as part of their services, but unlike traditional broker-dealers, they do not handle customer funds or securities, carry or act as an introducing broker with respect to customer accounts, or provide products and services to retail customers. As a result, many FINRA rules are not applicable to the business activities of these firms. The proposed rule change establishes a separate set of streamlined rules that would apply exclusively to these firms and is tailored to address their business activities, while maintaining necessary investor protections.

B. Economic Impacts

The proposed rule change would impact member firms that engage in CAB-related business activities, discussed above. As a baseline and based on staff experience, FINRA preliminarily estimates that the number of member firms that meet this definition would range from 650 to 750 firms.[16] Thus, it is possible that between 16 and 19 percent of all FINRA member firms may be eligible to operate under this proposed rule set.[17] These firms currently are required to comply with all applicable FINRA rules. These firms currently may incur costs to evaluate new FINRA rules and interpretations to ensure that they are not applicable for their business.

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16 FINRA notes that a commenter reported a higher estimate of 906 member firms that would meet the CAB definition based on information available on BrokerCheck® (See comment of 3PM). This estimate is based on the number of firms that report their business line (in Form BD) only as "Private Placement," "Other," or "Private Placement" *and* "Other." FINRA notes that these business lines may overlap with some of the business activities of CABs, but do not exactly correspond to the activities that would meet the CAB definition.

17 There are 4,031 firms that are registered with FINRA as broker-dealers. Accordingly, 650 and 750 firms account for 16% and 19%, respectively, of the total FINRA membership. See https://www.finra.org/newsroom/statistics (accessed June 29, 2015).

FINRA anticipates that some firms provide similar services but are not currently registered as broker-dealers with the SEC or FINRA. For example, some firms may currently limit activities, such as not accepting transaction-based compensation for their services, to avoid broker-dealer registration requirements and attendant costs. Others may accept transaction-based compensation, but may be relying on SEC no-action relief to avoid broker-dealer registration.[18] It is possible that some of these firms would reconsider their non-registered status if the new rules were in effect.

(i) Anticipated Benefits

The proposed rule change would reduce the regulatory burden for CABs by decreasing the range and scope of current FINRA rules that would be applicable to them given their limited activities and institutional business model. For example, as discussed above, the proposed rule change would establish a streamlined set of conduct rules. Similarly, the proposed CAB rules would establish a limited set of supervisory rules that are better designed to provide CABs with the flexibility to tailor their supervisory systems to their business models. As discussed above, CABs also would be subject to more limited customer information requirements than those applicable to other broker-dealers.

The reduction in these regulatory requirements is anticipated to reduce compliance costs for member firms that would register as CABs without diminishing investor protections. These cost savings would include reduction in costs associated with maintaining FINRA membership, including ongoing compliance activities such as maintaining policies and procedures. These firms also would likely benefit from more

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18 See M&A Brokers, 2014 SEC No-Act. LEXIS 92 (January 31, 2014).

focused examinations that are tailored to their business activities. To avail themselves of these benefits, firms would, however, be required to maintain their CAB status and as a result limit their activities to those permitted under the CAB rules.

As discussed above, CAB rules also may encourage non-member firms that engage in similar kinds of services as CABs to register with FINRA. FINRA membership would benefit these non-member firms by allowing them to expand their securities business and engage in activities permitted under the CAB rules. FINRA membership would subject these firms to certain FINRA rules, including conduct rules, supervisory rules, and rules concerning financial and operational obligations of the firms. As a result, FINRA membership would increase regulatory oversight of these firms, thereby enhancing investor protection of their customers.

(ii) Anticipated Costs

A member firm that seeks to register as a CAB would incur initial legal and other compliance costs associated with effectively completing the application to amend its membership agreement to elect CAB status. Such a firm also would incur administrative costs associated with updating its policies and procedures. FINRA, however, anticipates that these costs would likely be minimal relative to the cost savings from the streamlined CAB rules. As firms would have discretion to determine whether to apply for the amended status, FINRA anticipates that only those firms that anticipate net benefits to them would do so.

Non-member firms that choose to register as a CAB would incur implementation and ongoing costs associated with joining and maintaining their broker-dealer registrations with FINRA. The initial implementation costs would include FINRA application fees, costs associated with adapting technology infrastructure for regulatory data reporting requirements, as well as other legal or consulting costs associated with developing policies and procedures to ensure continued compliance with SEC and CAB rules. The ongoing costs would include annual fees associated with FINRA membership, costs of maintaining data reporting, costs of legal work relating to FINRA membership, and other costs associated with additional compliance activities. FINRA notes, however, that the proposed rule change would not impose these costs on non-member firms because registering as a broker-dealer and electing CAB status is optional. Non-member firms would likely only choose to register as a CAB broker-dealer and incur these costs if the anticipated benefits of registering exceed the costs of doing so.

C. Alternatives

In considering how to best meet its regulatory objectives, FINRA considered several alternatives to particular features of this proposal. For example, the initial proposal would have allowed CABs to solicit only institutional investors as that term is defined in FINRA Rule 2210. As discussed in more detail below, several commenters suggested that the proposed rule change also allow CABs to provide products and services to accredited investors or qualified purchasers. FINRA's regulatory programs have uncovered significant concerns associated with the ways in which firms sell private placements to accredited investors. Accordingly, FINRA does not believe it is appropriate to lower the institutional investor threshold for the CAB rules to the accredited investor standard.

Nonetheless, FINRA agrees that the definition of institutional investor under the CAB rules should include qualified purchasers as that term is defined under the 1940 Act, since qualified purchasers are required to own significantly more investments than those required for accredited investors, and as a result qualified purchasers are more likely to have the resources necessary to protect themselves from potential sales practice problems. Accordingly, FINRA has revised the institutional investor definition to include qualified purchasers, which would allow CABs to offer interests in private funds that are excluded from the definition of "investment company" and thus exempt from registration under the 1940 Act, such as hedge funds or private equity funds.

In developing this proposal, FINRA also considered expanding the scope of permissible activities for CABs. For example, as discussed below, commenters suggested that FINRA allow CABs to engage in activities related to the transfer of ownership or control of a privately-held company consistent with the SEC's M&A Brokers no-action letter. FINRA agrees that CABs should be permitted to engage in merger and acquisition transactions to the same extent as an unregistered broker-dealer pursuant to the M&A Brokers no-action letter and has revised the definition of CAB to allow such activities.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Background

In February 2014, FINRA published Regulatory Notice 14-09 (the "Notice"), requesting comment on a proposed rule set for firms that meet the definition of "limited corporate financing broker" ("LCFB") (the "Notice proposal"). A copy of the Notice is attached as Exhibit 2a. The comment period expired on April 28, 2014. FINRA received 51 comments in response to the Notice.[19] A list of the commenters in response to the

[19] Twenty-one of the comments were short emails or letters endorsing the comments of 3PM.

Notice is attached as Exhibit 2b, and copies of the comment letters received in response to the Notice are attached as Exhibit 2c.[20] A summary of the comments and FINRA's response is provided below.

As discussed below, most of the comments opposed the Notice proposal on the ground that it did not go far enough to relieve LCFBs of their current regulatory burdens. This concern, combined with the limitations in activities that the proposal's rules would impose, would lead most firms commenting on the proposal not to change their status to an LCFB.[21]

Application of LCFB Rules to Municipal Securities

LCFB Rule 015 would have stated that the LCFB rules do not apply to transactions in, and business activities relating to, municipal securities as defined in Section 3(a)(29) of the Exchange Act. One commenter noted that some FINRA member firms provide financial advisory services only to municipalities or municipal agencies, including recommending the timing and type of offering and to assist in the selection of an underwriter. The commenter stated that if this type of firm does not engage in the sale of municipal securities and would otherwise qualify, it should be eligible to be an LCFB.[22]

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20 See Exhibit 2b for a list of abbreviations assigned to commenters.

21 As noted above, the proposal would have referred to firms subject to the proposed rule set as "limited corporate financing brokers" ("LCFBs") rather than "capital acquisition brokers" ("CABs"). Similarly, this discussion refers to the rules proposed in the Notice as the "LCFB rules" rather than the "CAB rules." The CAB rules which are submitted as part of this proposed rule change have been revised from the prior LCFB rules, but maintain the same rule numbers as the LCFB rules.

22 See Sutter.

LCFB Rule 015 would not prevent an LCFB from engaging in municipal securities activities. Rather, as revised, it simply would clarify that FINRA Rule 0150(b) applies to the CAB rules. FINRA Rule 0150(b) currently provides that the FINRA rules do not apply to transactions in, and business activities relating to, municipal securities as defined in the Exchange Act.

Definition of "Customer"

LCFB Rule 016(d) would have defined the term "customer" as "any natural person and any entity receiving corporate financing services from an LCFB." It also would have specified that the term "customer" does not include a broker or dealer.

One commenter stated that this definition is unclear and should be replaced with other terms, such as "issuer," "investor," "qualified investor," and "intermediary," since these terms better describe the counterparties involved in an LCFB's business.[23] Two other commenters recommended that FINRA use the term "client" rather than "customer."[24] Another commenter suggested that FINRA be clearer as to what types of corporate financing services a customer may receive from an LCFB.[25]

FINRA does not believe it would be appropriate to replace the term "customer" with other terms such as issuer, investor, or intermediary. The meaning of the term "customer" depends on the context in which it is used, such as the requirements to know your customer or to recommend a suitable investment to a customer. Terms such as "issuer" or "investor" would not be appropriate in these contexts. However, FINRA does

[23] See 3PM.

[24] See Achates and Q Advisors.

[25] See CFSC.

believe that the term customer should be interpreted in a manner consistent with the way it is interpreted under the FINRA rules. Accordingly, FINRA has revised this term to have the same definition as it has under the FINRA rules.[26]

Institutional Investor Definition

LCFB Rule 016(h) would have allowed an LCFB to solicit only institutional investors. LCFB Rule 016(g) would have defined the term "institutional investor" to include banks, savings and loan associations, insurance companies, registered investment companies, governmental entities and their subdivisions, employee benefit plans and qualified plans with at least 100 participants (but not including the participants themselves), any other person with at least $50 million in assets, and persons acting on an institutional investor's behalf.

Seven commenters recommended that the LCFB rules allow LCFBs to offer interests in privately placed companies to accredited investors, as that term is defined in SEC Regulation D.[27] One commenter noted that requiring an LCFB to pre-qualify potential investors to meet the LCFB rules' definition of institutional investor, rather than the Regulation D accredited investor definition, would be difficult, since an LCFB may not know the financial status of a potential buyer, and could potentially harm an LCFB client seller by diminishing the pool of prospective investors.[28] Three other commenters recommended that the term "institutional investor" be replaced with a new term,

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26 See FINRA Rule 0160(b)(4) ("The term 'customer' shall not include a broker or dealer").

27 See Achates, LIATI, SFA, Dole, RWI, HighBank, and EYCA. See also 17 CFR 230.501(a).

28 See SFA.

"qualified investor," which would include "qualified investors" as that term is defined under the 1940 Act.[29] One commenter questioned whether an LCFB would be permitted to accept an unsolicited offer from a non-institutional investor.[30] Another commenter inquired as to the documents that FINRA would require an LCFB to retain to confirm an investor's institutional status.[31]

As discussed in the Notice, FINRA purposely did not propose to define "institutional investor" based on a more inclusive standard, such as the definition of "accredited investor" in Regulation D under the Securities Act of 1933. FINRA's regulatory programs have uncovered serious concerns with the manner in which firms market and sell private placements to accredited investors. Application of the CAB rules to firms that market and sell private placements to accredited investors would require FINRA to expand the applicable conduct rules and other provisions. Therefore, lowering the threshold of "institutional investor" to the accredited investor standard would frustrate the purposes of a streamlined rule set.

Nevertheless, FINRA agrees that the definition of "institutional investor" should include persons that meet the definition of "qualified purchaser" under the 1940 Act.[32] Persons that meet the definition of "qualified purchaser" in most cases must own not less than $5 million in investments, far greater than the minimum assets required by the accredited investor standard. FINRA believes that it is much less likely that a CAB

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29 See 3PM, Q Advisors, and M&A Brokers Letter Attorneys.

30 See SFA.

31 See EYCF.

32 See 15 U.S.C. 80a-2(a)(51).

would commit the types of sales practice problems that FINRA has observed in connection with the sale of Regulation D private placements to accredited investors if an investor is required to meet the qualified purchaser standard, since a qualified purchaser likely would have the resources necessary to protect itself from potential sales practice problems. In addition, by defining "institutional investor" to include qualified purchasers, CABs would be able to offer interests in private issuers, such as hedge funds or private equity funds, that are excepted from the definition of "investment company" pursuant to Section 3(c)(7) of the 1940 Act.

Moreover, as discussed below, FINRA has proposed to expand the permissible activities of CABs to include effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company in accordance with the terms and conditions of an SEC rule, release, interpretation or no-action letter.[33] By expanding CABs' proposed activities to include these kinds of M&A transactions, CABs would not be limited to selling ownership or control of a privately-held company only to institutional investors as defined by the CAB rules, since the SEC's M&A Brokers no-action letter[34] does not contain this limitation. FINRA believes this expansion should address many of the commenters' concerns with the institutional investor definition.

Limited Corporate Financing Broker Definition

The proposed definition of LCFB would have allowed firms meeting this definition to engage in:

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33 See proposed CAB Rule 016(c)(1)(G).

34 See M&A Brokers, 2014 SEC No-Act. LEXIS 92 (January 31, 2014).

- advising an issuer, including a private fund concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions; and
- qualifying, identifying, or soliciting potential institutional investors.

The proposed definition of LCFB would have excluded any broker or dealer that carries or maintains customer accounts, holds or handles customers' funds or securities, accepts orders from customers to purchase or sell securities either as principal or agent for the customer, possesses investment discretion on behalf of any customer, or engages in proprietary trading of securities or market making activities.

Although one commenter felt that the definition of LCFB was appropriate,[35] others recommended that the definition of LCFB be amended specifically to permit an LCFB to provide valuation services,[36] expert testimony and litigation support.[37] Other commenters recommended that the definition be clarified to permit LCFBs to engage in

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35 See 3PM.

36 See CFSC.

37 See Sutter and RWI.

negotiation of transactions,[38] and to act as a placement agent for a buyer or seller.[39] Another commenter urged FINRA to revise the definition so that it spells out in more detail the types of advice that an LCFB may provide to a client (e.g., preparing a business for sale, financial modeling, financial alternatives, evaluating competing offers, structuring transactions, due diligence and transition issues) and that it should allow an LCFB to act as a finder (introducing parties to a transaction).[40] Others recommended that LCFBs be permitted to provide research and engage in public company transactions in connection with their advisory work.[41]

Commenters also suggested that FINRA allow LCFBs to advise controlling or minority shareholders in a private business in connection with the sale of stock,[42] and that FINRA look to the SEC's M&A Brokers letter for a description of appropriate LCFB activities.[43] The latter commenter also recommended that LCFBs be allowed to solicit non-institutional investors if both the seller and buyer are or will be actively involved in running the business (which also is consistent with the M&A Brokers letter).

FINRA intended to allow CABs to provide valuation, expert testimony, litigation support, negotiation and structuring services, and to act as a placement agent for, or finder of, institutional investors. Accordingly, FINRA has revised the definition of CAB

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[38] See Q Advisors.

[39] See Q Advisors and M&A Brokers Letter Attorneys.

[40] See RWI.

[41] See Fells and EYCF.

[42] See Harris.

[43] See ABA.

to make this clearer. FINRA does not agree, however, that CABs should be allowed to produce research for the investing public. If a CAB produced research reports, FINRA would need to consider whether to add FINRA Rule 2241 and potentially other rules to the list of CAB rules, which currently do not include these rules.

FINRA agrees that CABs should be permitted to engage in M&A transactions to the same extent as an unregistered broker pursuant to the M&A Brokers no-action letter. Accordingly, FINRA has revised the definition of CAB to allow such firms to effect securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company in accordance with the terms and conditions of an SEC rule, release, interpretation or no-action letter that permits a person to engage in such activities without registering as a broker under Section 15(b) of the Exchange Act.[44]

One commenter argued that the term "limited corporate financing broker" itself is problematic because it may confuse clients into thinking that a firm has reduced its servicing offerings when in fact they remain unchanged.[45] In response to this concern, FINRA has changed the name of this defined term, and the name of the rule set, from "limited corporate financing broker" to "capital acquisition broker."

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[44] FINRA also revised the list of activities that a CAB may not engage in to clarify that a CAB may not carry or act as an introducing broker with respect to customer accounts or participate in or maintain an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933. See proposed CAB Rule 016(c)(2).

[45] See McCracken.

New Member and Change of Business Applications

LCFB Rule 112 would have subjected LCFBs to NASD Rule 1013, which governs new FINRA membership applications. LCFB Rule 112 also would have required applicants for FINRA membership that seek to qualify as LCFBs to state in their applications that they intend to operate as an LCFB.

LCFB Rule 116 would have subjected LCFBs to NASD Rule 1017, which governs applications for approval of change in ownership, control, or business operations. Rule 116 also would have allowed an existing FINRA member firm that seeks to change its status to an LCFB, and that is already approved to engage in the activities of an LCFB, but which does not intend to change its existing ownership, control, or business operations, to file a request to amend its membership agreement or obtain a membership agreement (if none exists), to provide that: (i) the member firm's activities will be limited to those permitted for LCFBs under LCFB Rule 016(h); and (ii) the member firm agrees to comply with the LCFB rules. Rule 116 further specified that an LCFB that seeks to terminate its status as such and continue as a FINRA member firm would have to file an application for approval of a material change in business operations pursuant to NASD Rule 1017 (a "CMA"), and would have to amend its membership agreement to provide that it agrees to comply with all FINRA rules.

One commenter also recommended that FINRA streamline the new member and change in membership process for LCFBs, reduce the time period for decisions, and lower the application fees.[46] Other commenters stated that any request to change a firm's membership agreement to elect LCFB status should be without a fee, and that firms

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46 See M&A Brokers Letter Attorneys.

should be allowed to revert back to their original non-LCFB status without having to file a change in membership application during the firm's first year of operation as an LCFB.[47] Commenters also noted that the proposed requirement to pay a $5000 fee as part of the CMA in order to buy back a firm's full broker status is a substantial disincentive to become an LCFB.[48]

FINRA does not agree that it should create a different new member process for applicants that are not already registered broker-dealers and that seek to become CABs. Although CABs would be subject to fewer FINRA requirements than other broker-dealers, FINRA still believes that it is important for investor protection and industry confidence reasons that FINRA have an opportunity to vet new CAB firms in the same manner that FINRA vets other new firm applicants. Similarly, if a firm wishes to change its ownership, control or business operations, FINRA believes that it is important that these changes receive the same review as any other registered firm. FINRA has modified CAB Rule 112, however, to clarify that a CAB applicant must state in its application that it intends to operate solely as a CAB.[49]

CAB Rule 116 already permits an existing FINRA member firm to elect CAB status by requesting a change in its membership agreement, and without filing a CMA or paying a filing fee. However, FINRA agrees that Rule 116 should provide some more flexibility to a CAB that seeks to revert to its full broker status within the first year after

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47 See 3PM and RWI.

48 See Achates and RWI.

49 FINRA also has modified CAB Rules 111, 112, 113, 114, and 115 to clarify that they apply to persons applying for membership in FINRA as a CAB as well as to the CABs themselves.

electing CAB status. Accordingly, FINRA has amended Rule 116 to provide that, if during the first year following an existing FINRA member firm's amendment to its membership agreement to elect CAB status, the firm seeks to terminate its CAB status and continue as a FINRA member firm, the firm may notify the Membership Application Program group of this change without having to file a CMA. The member firm seeking this change would have to file a request to amend its membership agreement to provide that the firm agrees to comply with all FINRA rules, and execute an amended membership agreement that imposes the same limitations on the firm's activities that existed prior to the firm's change to CAB status.

Registration Categories

Proposed LCFB Rule 123 would have allowed persons registered with LCFBs to hold only a limited set of registrations that relate to an LCFB's business.[50] The proposal also would have subjected LCFBs to the Operations Professional (Series 99) registration requirement.

Commenters objected to limiting the types of registrations that an associated person of an LCFB may retain.[51] Commenters noted that registered persons may be

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[50] Registered principals of LCFBs would have been permitted to hold the General Securities Principal (Series 24), Limited Principal – Financial and Operations (Series 27), Limited Principal – Introducing Broker/Dealer Financial and Operations (Series 28), and Limited Principal – General Securities Sales Supervisor (Series 9 and 10) registrations. Registered representatives of LCFBs would have been permitted to hold the General Securities Representative (Series 7), Limited Representative – Direct Participation Programs (Series 22), Limited Representative – Private Securities Offerings (Series 82), and Limited Representative – Investment Banking (Series 79) registrations.

[51] See 3PM, Achates, Signal Hill, Sutter, LIATA, RWI, HighBank, M&A Brokers Letter Attorneys, and EYCA.

required to hold other registrations under state law.[52] In addition, commenters argued that this restriction would penalize individuals who may want to change jobs later and return to a full service broker-dealer, where other registrations would be required. They favored allowing registered persons to retain their registrations while employed with an LCFB. Commenters also opposed requiring LCFBs to employ an Operations Professional.[53] Two commenters encouraged FINRA, as part of this process, to re-examine the permissible scope of activities of various registration categories, such as Series 22, 62, 79 and 82 registrations.[54]

However, one commenter supported the restrictions. It recommended that LCFB representatives be required to obtain the Series 79 registration, and that LCFB representatives not be permitted to obtain other registration categories or retain other existing registrations during the time they are associated with an LCFB.[55] Another commenter suggested that LCFB principals and representatives not be permitted to hold other registrations unless a firm can adequately supervise the activities covered by those registrations.[56]

FINRA is persuaded that not allowing registered principals and representatives to obtain and hold the full range of registration categories could potentially penalize individuals who have already obtained those registration categories, and that the

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52 See 3PM, Achates, Sutter, and Q Advisors.

53 See 3PM and M&A Brokers Letter Attorneys.

54 See ABA and LeGaye.

55 See CFSC.

56 See Harris.

limitations of proposed LCFB Rule 123 also could potentially conflict with state law requirements. Accordingly, FINRA is amending CAB Rule 123 to eliminate the prior restrictions on the types of registrations persons associated with CABs may hold. Associated persons still would only be permitted to retain registrations that are appropriate to their functions under the registration rules.

FINRA continues to believe that CABs should be subject to FINRA Rule 1230(b)(6) regarding Operations Professional (Series 99) registration. FINRA believes the Operations Professional registration category enhances the regulatory structure surrounding the specified (or "covered" functions), including contributing to the process of preparing and filing financial regulatory reports, and has noted that for some firms the Operations Professional often may be the firm's Financial and Operations Principal.[57] FINRA also is not re-examining the range of permissible activities for principals and representatives in various registration categories, as those issues are beyond the scope of this proposed rule change.

Continuing Education Requirements

Proposed LCFB Rule 125 would have required any person registered with an LCFB who has direct contact with customers in the conduct of the broker's corporate financing activities, and the immediate supervisors of such persons, to be subject to many of the same requirements contained in the Firm Element provisions of FINRA Rule 1250. Proposed LCFB Rule 125 would not have subjected persons registered with an LCFB to the Regulatory Element provisions of FINRA Rule 1250, however.

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[57] See Regulatory Notice 11-33 (July 2011).

One commenter stated that it was not opposed to requiring registered persons to undergo additional training and continuing education testing to keep an associated person's registration active, but proposed that these requirements be imposed only once every two years.[58] Another commenter questioned exempting LCFB personnel from the Regulatory Element requirements of FINRA Rule 1250, and noted that investment bankers need to keep up with current rules and regulations as much as other types of brokers.[59]

Given that FINRA has revised the proposed registration rules to allow persons registered with a CAB to hold and retain any principal and representative registrations that are appropriate to their functions under the registration rules, FINRA believes it is appropriate to subject associated persons to all of the continuing education requirements of FINRA Rule 1250, including the Regulatory Element provisions. FINRA has amended CAB Rule 125 accordingly.

Expungement of Customer Dispute Information

Proposed LCFB Rule 208 (Obtaining an Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD) System) would have subjected LCFBs to FINRA Rule 2080, which sets forth requirements for members or associated persons seeking to expunge information from the CRD system arising from disputes with customers. FINRA did not receive any comments on this proposed rule.

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58 See 3PM.

59 See Washington U.

Since the Notice was published, FINRA Rule 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information) became effective.[60] FINRA Rule 2081 prohibits members and associated persons from conditioning or seeking to condition settlement of a customer dispute on, or otherwise compensating the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer information from the CRD system. The rule directly addresses any concerns about parties to a settlement "bargaining for" expungement relief as a condition to settlement and should apply equally to any CAB or its associated persons seeking to expunge information from the CRD system. Accordingly, FINRA has amended LCFB Rule 208 also to subject CABs and their associated persons to FINRA Rule 2081.

Know Your Customer and Suitability

Proposed LCFB Rules 209 (Know Your Customer) and 211 (Suitability) would have included slightly modified versions of the know your customer ("KYC") and suitability requirements of FINRA Rules 2090 and 2111. Proposed LCFB Rule 211(b) specified that an LCFB or its associated person fulfills the customer-specific suitability obligations for an institutional account, as defined by FINRA Rule 4512(c), if (1) the broker or associated person has a reasonable basis to believe that the institutional customer is capable of evaluating investment risks independently, both in general and with regard to particular transactions and investment strategies involving a security or securities and (2) the institutional customer affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's

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60 See Regulatory Notice 14-31 (July 2014).

recommendations. Where an institutional customer has delegated decision-making authority to an agent, such as an investment adviser or bank trust department, the rule would have applied these factors to the agent.

One commenter recommended that proposed LCFB Rule 209 be redrafted to remove any reference to "customer," instead suggesting that LCFBs should be required to perform due diligence of issuers, as well as reviews of investors and intermediaries considering whether to invest in an issuer to ensure qualified status.[61] Another commenter argued that the rule as written is too vague, and that an examiner would be unable to know if a firm had met its obligations to effectively service a customer.[62]

Commenters also were largely critical of proposed LCFB Rule 211. One commenter stated that it was inappropriate to require a suitability analysis before any recommendation, and that the rule was written as if an LCFB services retail customers. This commenter suggested that any suitability analysis should only be required before a subscription or purchase agreement is signed, and only where an investor is not represented by a qualified intermediary.[63] Another commenter encouraged FINRA to more clearly define a "recommendation" in this context and reconsider the definition of "customer" under the proposed rules.[64]

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[61] See 3PM.

[62] See Sutter.

[63] See 3PM.

[64] See ABA.

On the other hand, one commenter stated that LCFBs advise issuers, and that the KYC and suitability requirements should apply to these types of firms.[65] Two other commenters agreed that LCFBs advise both sell-side and buy-side M&A clients, but do not make recommendations to customers in the traditional sense.[66]

FINRA believes that the KYC and suitability rules should apply to CABs. The KYC rule requires CABs to use reasonable diligence to know and retain the essential facts concerning every customer and concerning the authority of each person acting on behalf of such customer. Facts essential to knowing a firm's customer are those required to (a) effectively service the customer, (b) understand the authority of each person acting on behalf of the customer, and (c) comply with applicable laws, regulations and rules.

The rule is flexible in that it recognizes that the determination of what is required to service a particular client will always be based on the facts and circumstances of a firm's relationship with its client. Likewise, the fact that a firm's client is a party to an M&A or other private equity transaction does not alter the need to understand the authority of each person acting on behalf of the customer, or facts necessary to comply with applicable laws, regulations and rules. Again, these facts will depend on each transaction's facts and circumstances, and the rule recognizes this flexibility.

Likewise, FINRA also believes that CABs should be subject to suitability requirements. If a CAB does not recommend a securities transaction, as some commenters assert, then the suitability requirements would not apply. Likewise, the proposed rule specifies that a CAB or associated person fulfills the customer specific

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65 See RWI.

66 See HighBank and CSP.

suitability requirements for institutional investors if (1) the broker or associated persons has a reasonable basis to believe that the institutional investor is capable of evaluating investment risks independently and (2) the institutional investor affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's recommendations. If the institutional investor has delegated decision-making authority to an agent, these factors apply to the agent. FINRA believes that this provision largely addresses concerns expressed by commenters that the proposed rule applies retail investor requirements to transactions involving institutional investors. It also recognizes that a CAB or its associated person may look to an institutional investor's agent if the investor is represented by an agent.

FINRA has added supplementary material to proposed Rule 211 to clarify that a CAB still must have a reasonable basis to believe, based on reasonable diligence, that a recommendation is suitable for at least some investors. FINRA also has added supplemental material providing guidance with regard to the institutional investor exemption from the customer specific suitability requirements. The text of both of these supplementary materials is taken from similar supplementary materials that follow FINRA Rule 2111. FINRA believes that these additions will help clarify the scope of a CAB's suitability responsibilities under proposed Rule 211.

FINRA also has revised the definition of "customer" to reflect the definition of this term under FINRA Rule 0160(b)(4). As revised, customer is defined as not including a broker or dealer. FINRA is making this change to make clear that the definition of customer under the CAB rules has the same meaning as under the FINRA rules.

Communications with the Public

Proposed LCFB Rule 221 would have required LCFB communications to meet the general principles-based content standards of FINRA Rule 2210, although it also would have prohibited LCFB communications from projecting or predicting performance. Proposed LCFB Rule 221 would not have required LCFBs to approve communications prior to use, nor would it have imposed any filing requirements for LCFB communications.

One commenter recommended that the proposed rule's content standards include a "realistic approach" to setting fair and balanced content standards to meet the realities of representing issuers of securities.[67] Another commenter argued that the proposed rule does not sufficiently protect investors, and that it should require new firms to file communications with FINRA and require registered principals to approve firm communications prior to use.[68] Another commenter argued that the cost of archiving emails for three years and reviewing emails periodically is burdensome.[69]

FINRA believes that proposed CAB Rule 221 is already sufficiently general to take into account the institutional nature of CABs' business models. However, FINRA recognizes that firms may need to include projections of an issuer's performance in communications that are sent to prospective investors, such as pro forma financial statements related to a business acquisition or combination. For this reason, FINRA has removed the prohibition on predictions or projections of performance. The proposed rule

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[67] See 3PM.

[68] See CFSC.

[69] See Colonnade.

would continue to prohibit communications from implying that past performance will recur or making any exaggerated or unwarranted claim, opinion or forecast.

FINRA does not believe it is necessary to include either principal pre-use approval or filing requirements for CABs given the institutional nature of their business. CABs will be required to supervise communications, but FINRA intends to allow CABs the flexibility to determine the best means of such supervision given each firm's business model. LCFBs will be subject to the SEC's record-keeping requirements for emails under Exchange Act Rules 17a-3 and 17a-4, which FINRA has no authority to alter.

Engaging in Impermissible Activities

Proposed LCFB Rule 240 provided that, upon finding that an LCFB or associated person of an LCFB has engaged in activities that require the firm to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on LCFBs under LCFB Rule 016(h), FINRA may examine for and enforce all FINRA rules against such a broker or associated person, including any rule that applies to a FINRA member broker-dealer that is not an LCFB or to an associated person who is not a person associated with an LCFB. One commenter argued that an LCFB that engages in impermissible activities should be given a defined remedial period and process for any unintentional activities of an LCFB until the rules have been in place for a while, given the potential for rule ambiguity.

FINRA does not believe it is necessary to include within the rule a specific remedial period for engaging in impermissible activities. FINRA believes that unintentional violations during a transition period are best handled through the examination and enforcement process on a case-by-case basis. Accordingly, FINRA is not proposing to amend the rule.

Outside Business Activities of Registered Persons

Proposed LCFB Rule 327 would have required LCFBs to be subject to FINRA Rule 3270 (Outside Business Activities). One commenter urged FINRA to clarify an LCFB's supervisory responsibilities when an associated person engages in private securities transactions away from the firm under NASD Rule 3040, and an LCFB's supervisory obligations when an associated person either is also registered with an affiliated or unaffiliated full-service broker-dealer or refers a customer to a full-service firm in return for a referral fee.[70]

An associated person of a CAB would not be permitted to engage in private securities transactions away from the firm, since such activities would be beyond the scope of permissible activities for a CAB under proposed CAB Rule 016(c).[71] However, in order to make this restriction more clear, FINRA has added CAB Rule 328, which would expressly prohibit associated persons of CABs from engaging in private securities transactions as defined in FINRA Rule 3280(e).

For the same reasons, an associated person of a CAB also would not be allowed to register with an affiliated or unaffiliated full-service broker-dealer. An associated person could receive a fee for referring business to another broker-dealer, provided that the proposed transaction would be permissible for the CAB to conduct itself.

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70 See CFSC.

71 See CAB Rule 014 ("Persons associated with a capital acquisition broker shall have the same duties and obligations as a capital acquisition broker under the Capital Acquisition Broker rules").

Anti-Money Laundering Compliance Program

Proposed LCFB Rule 331 would require an LCFB to develop and implement a written AML program reasonably designed to achieve and monitor its compliance with the requirements of the Bank Secrecy Act and the Department of Treasury regulations thereunder. The AML program would have to meet many of the same standards that full-service broker-dealers must meet under FINRA Rule 3310, except that the program would provide for independent testing for compliance no less frequently than every two years, rather than every year.

Five commenters stated that AML audits should not be required for LCFBs, since such firms receive no customer deposits and have no customer accounts.[72] Another commenter argued that LCFBs should only have to implement a customer identification program ("CIP") for issuers and intermediaries with which the LCFB does business, and for investors where there is no intermediary.[73] However, another commenter stated that there is no reason to exempt an LCFB from the one-year AML testing requirement.[74]

Because the Bank Secrecy Act imposes AML obligations on all broker-dealers, FINRA does not believe it has the authority to exempt CABs from the requirement to adopt and implement an AML program. However, due to the limited nature of CABs' securities transactions, FINRA believes it is appropriate to allow CABs to conduct independent compliance testing of their AML programs every two years rather than every year.

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72 See Growth Venture, Signal Hill, Q Advisors, CSP, and LeGaye.

73 See 3PM.

74 See CFSC.

Capital Compliance

Proposed LCFB Rule 411 would impose on LCFBs certain requirements imposed on full-service broker-dealers under FINRA Rule 4110 (Capital Compliance). Unless otherwise permitted by FINRA, an LCFB would have to suspend all business operations during any period in which it is not in compliance with the applicable net capital requirements set forth in Exchange Act Rule 15c3-1. The proposed rule also would authorize FINRA to issue a notice pursuant to FINRA Rule 9557 directing a non-compliant LCFB to suspend all or a portion of its business. The proposed rule would impose requirements related to withdrawal of equity capital, subordinated loans, and notes collateralized by securities and capital borrowings similar to provisions in FINRA Rule 4110.

Numerous commenters recommended that FINRA either eliminate or substantially reduce net capital requirements for LCFBs,[75] and that FINRA overhaul the net capital and FOCUS reporting requirements to better apply these requirements to LCFBs' business model.[76]

The SEC, however, sets these standards under its net capital rules and FINRA believes that the SEC would have to adjust its net capital requirements before FINRA could alter the net capital requirements that it imposes under its rules. In this regard, FINRA has clarified the CAB rules to note that CABs would be required to file supplemental FOCUS reports pursuant to FINRA Rule 4524 as FINRA may deem necessary or appropriate for the protection of investors or in the public interest.

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75 See Growth Venture and LIATI.

76 See 3PM, Colonnade, Bridge 1, CMC, McCracken, RWI, M&A Brokers Letter Attorneys, IMS, and Stonehaven.

Audit

Numerous commenters urged FINRA to work with the SEC and the Public Company Accounting Oversight Board ("PCAOB") to carve out LCFBs from the requirement to produce audited financial statements.[77] Two commenters recommended that, as an alternative to an audit, LCFBs' financials could be subject to an AICPA "review."[78] Another commenter recommended that audits not be required unless a firm has 20 or more employees or $10 million in net revenues.[79]

FINRA believes that it does not have the authority to reduce or eliminate the requirement to obtain audited financial statements.

Fidelity Bonds

The proposal would subject LCFBs to FINRA Rule 4360, which requires each member firm required to join the Securities Investor Protection Corporation ("SIPC") to maintain blanket fidelity bond coverage that provides against loss and have insuring agreements covering at least six enumerated areas. The minimum required fidelity bond amount varies depending on a firm's net capital requirements, but in any case it must be at least $100,000.

Some commenters argued this requirement should not apply to LCFBs, since fidelity bonds protect against theft of a customer's funds. Because LCFBs may not accept or hold customer funds, these commenters argue that the bond requirement makes

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77 See 3PM, Achates, Colonnade, Growth Venture, Signal Hill, Sutter, LIATA, Bridge 1, Q Advisors, Dole, McCracken, HighBank, CSP, M&A Brokers Letter Attorneys, LeGaye, and IMS.

78 See Achates and RWI.

79 See Anderson.

no sense.[80] One commenter noted that an LCFB that issues a fairness opinion should be required to carry a larger fidelity bond than $100,000.[81]

In response to these comments, FINRA has determined not to subject CABs to FINRA Rule 4360 because of CABs' unique business model. CABs' clients would be limited to issuers of unregistered securities, institutional investors, and parties to a transaction involving the change of control of a privately held company. CABs would act as agent only in transactions in which funds flow directly from a purchaser of securities to the issuer or shareholder of such securities, and would not carry or act as an introducing broker in connection with customer accounts. In addition, CABs would belong to a separate FINRA membership category that would make them unique among all other FINRA member firms. For these reasons, FINRA believes it would be appropriate not to require CABs to maintain a fidelity bond under Rule 4360.

SIPC Dues

Thirteen commenters argued that an LCFB should not have to pay dues to SIPC on the ground that an LCFB would not carry or act as an introducing broker with respect to customer accounts or hold or handle customer funds.[82]

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80 See 3PM, Colonnade, Growth Venture, LIATI, Bridge 1, Q Advisors, Dole, McCracken, RWI, HighBank, CSP, LeGaye, IMS, and Stonehaven.

81 See Sutter.

82 See 3PM, Anderson, LIATI, Bridge 1, Q Advisors, Dole, McCracken, RWI, HighBank, CSP, LeGaye, IMS, and Stonehaven.

Almost all persons registered as brokers or dealers under Section 15(b) of the Exchange Act must be members of SIPC.[83] Because these requirements are imposed by statute, FINRA has no authority to exempt any CAB from SIPC membership.

Other Comments

Commenters had a number of other observations and recommendations regarding the proposed rule set, which FINRA addresses below.

One commenter recommended that FINRA relieve LCFBs from the requirement to review and file hard copies of employees' stock trading records.[84] Another commenter recommended that FINRA impose the requirements of NASD Rule 3050 on LCFBs.[85] NASD Rule 3050 imposes certain obligations on a member firm that knowingly executes a transaction for the purchase or sale of a security for the account of a person associated with another member firm, or any account over which such associated person has discretionary authority, and on an associated person who opens an account with another member firm. Among other things, upon written request by the employer member firm, the associated person must request that the executing member firm transmit duplicate account confirmations, statements or other information.

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83 See Section 3(a)(2)(A) of the Securities Investor Protection Act, 15 U.S.C. 78ccc(a)(2)(A). The only exceptions to this requirement are for: (i) firms whose principal business is conducted outside the United States, as determined by SIPC; (ii) firms whose business as a broker or dealer consists exclusively of (I) the distribution of open-end investment companies or unit investment trusts; (II) the sale of variable annuities; (III) the business of insurance; or (IV) advising investment companies or insurance company separate accounts; and (iii) firms that are registered as brokers or dealers solely for the purpose of trading security futures on an exchange.

84 See Colonnade.

85 See CFSC.

The CAB rules would not apply NASD Rule 3050 to CABs. FINRA believes that, due to the limited institutional activities of CABs and their associated persons, it is not necessary to impose this rule's obligations on CABs.

Three commenters urged FINRA to eliminate or reduce its assessments on LCFBs due to the limited level of FINRA oversight of these firms.[86] FINRA derives its revenues from a number of sources, many of which are user fees, such as fees imposed on firms that file communications with FINRA's Advertising Regulation Department, or public offerings with FINRA's Corporate Financing Department. CABs would not be subject to many of these user fees since they would not be subject to these filing requirements. However, CABs would be subject to fees and assessments that apply to all FINRA member firms, such as the gross income assessment or the new member filing fees. FINRA believes that it is appropriate to impose these more generalized assessments on CABs to cover the costs of regulating and examining CAB activities.

One commenter expressed concern that the proposed rule set will lead to differing interpretations of rules, and will create an uneven playing field with full-service broker-dealers. This commenter believes that the proposed rule set is contrary to FINRA's mission of market integrity and investor protection, and that FINRA and the industry would be better served by expanding existing rules rather than creating a new rule set.[87]

FINRA staff strives to interpret all of its rules in a consistent manner, and it will make similar efforts to interpret rules consistently if the proposal is approved. To the extent a CAB rule requires compliance with an existing FINRA rule that applies to full-

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86 See Anderson, RWI, and LeGaye.

87 See CFSC.

service broker-dealers, the staff anticipates that it will interpret the CAB rule in the same manner as the corresponding FINRA rule. If the CAB rule differs from its FINRA rule counterpart, the staff intends to interpret the rule consistently with respect to all CABs. FINRA does not agree that the proposed rule set would be contrary to FINRA's mission of market integrity and investor protection. FINRA has carefully crafted the rule set to include rules that should apply to all broker-dealers, or to broker-dealers that engage in M&A and other private equity activities with institutional investors, while excluding from the proposal rules that have no applicability to CABs' business model, or that would impose unnecessary burdens given the kinds of activities in which CABs engage.

One commenter suggested that the Federal Trade Commission Red Flag Rules should apply to LCFBs. This commenter noted that LCFBs may be in possession of confidential and sensitive information concerning their customers, and that these customers could be exposed to risks resulting from identity theft.[88] The proposal would not impact whether a CAB is subject to the Red Flag Rules adopted pursuant to the Fair Credit Reporting Act of 1970, as amended.[89] The application of the Red Flag Rules depends on whether a broker or dealer falls within the requirements of the SEC's Regulation S-ID.[90]

One commenter noted that the proposed rule set omits FINRA Rule 5150 (Fairness Opinions) and a reference to information barriers, such as the guidance provided in NASD Notice to Members 91-45 (July 1991). The commenter also

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[88] See RWI.

[89] Pub. L 91-508, 84 Stat. 1114 (1970), codified at 15 U.S.C. 1681-1681x.

[90] 17 CFR 248 Subpart C. See also Securities Exchange Act Release No. 69359 (April 10, 2013), 78 FR 23637 (April 19, 2013).

recommended that FINRA clarify that the proposed rule set would apply only to broker-dealers whose enterprise-wide activities fit within the definition of LCFB, and not to affiliates of large financial conglomerates, even if the LCFB itself only engages in activities permissible for an LCFB.[91]

FINRA agrees that FINRA Rule 5150 should apply to a CAB that provides a fairness opinion that is subject to that rule. Although this rule generally applies to fairness opinions that are provided or described to public shareholders, it is possible that a CAB could serve as an advisor in connection with a public offering of securities and provide a fairness opinion in connection with the offering. In such a case, it would make sense to require the same disclosures regarding potential conflicts of interest in connection with the fairness opinion. Accordingly, FINRA is adding new CAB Rule 515 (Fairness Opinions), which would subject CABs to FINRA Rule 5150.

NASD Notice to Members 91-45 was a joint memorandum prepared by the National Association of Securities Dealers, Inc., the New York Stock Exchange, and a committee of the Securities Industry Association that explained the minimum elements of adequate information barrier policies and procedures pursuant to the requirements of the Insider Trading and Securities Fraud Enforcement Act of 1988. To the extent a CAB deals with information that would trigger application of this statute or any other insider trading law, the CAB would be required to have in place adequate information barriers necessary to meet these requirements.

FINRA disagrees that a CAB may not be affiliated with a broker-dealer that engages in activities that are not permitted for CABs. As discussed previously, the CAB

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91 See Washington U.

rules would prohibit both a CAB firm and its associated persons from engaging in activities that are not permitted under the definition of CAB. However, FINRA does not believe that it would be inconsistent for an affiliate of a CAB to engage in a wider array of activities; in those cases, the affiliate would be subject to all FINRA rules, and not the CAB rules.

One commenter urged FINRA to collaborate with the North American Securities Administrators Association ("NASAA") to further reduce regulatory burdens on LCFBs.[92] FINRA cooperates with NASAA representatives on securities regulatory issues, and expects that its staff will continue to discuss matters of mutual interest regarding CABs with NASAA representatives in the future.

Another commenter requested that FINRA confirm that LCFBs may serve as "chaperones" for non-U.S. broker-dealers under Exchange Act Rule 15a-6 by performing activities that are described in Rule 15a-6(a)(3) and related no-action letters. The same commenter recommended that FINRA confirm with the states that an LCFB would be eligible for an exemption from state business broker licensing laws, to the extent that they exempt other registered broker-dealers.[93]

FINRA is not prepared at this time to confirm that all activities listed in Rule 15a-6(a)(3) and related no-action letters would be permissible for a CAB. For example, these activities include effecting securities transactions and issuing all required confirmations and statements, which appear to be activities beyond what would be permitted under the

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92 See M&A Brokers Letter Attorneys.

93 See EYCF.

CAB definition. Likewise, the question of whether a CAB would be subject to a particular state's business broker licensing laws would be better directed to that state.

Another commenter recommended that FINRA work with the SEC, NASAA, the Commodity Futures Trading Commission, the National Futures Association, and the industry to develop a unified simple regulatory approach to regulating broker-dealer activities on the basis of risk rather than on transaction-based compensation.[94] The commenter's suggestion is beyond the scope of this proposed rulemaking and would likely require changes to the federal securities laws.

6. Extension of Time Period for Commission Action

FINRA does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.[95]

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

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[94] See IMS.

[95] 15 U.S.C. 78s(b)(2).

11. Exhibits

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 2a. FINRA Regulatory Notice 14-09 (February 2014)

Exhibit 2b. List of comments received in response to FINRA Regulatory Notice 14-09.

Exhibit 2c. Copies of comment letters received in response to FINRA Regulatory Notice 14-09.

Exhibit 5. Text of the proposed rule change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-FINRA-2015-054)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Adopt the Capital Acquisition Broker Rules

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act," "Exchange Act" or "SEA")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on , Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to create a separate rule set that would apply to firms that meet the definition of "capital acquisition broker" and elect to be governed under this rule set.

The text of the proposed rule change is available on FINRA's website at http://www.finra.org, at the principal office of FINRA and at the Commission's Public Reference Room.

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

There are FINRA firms that are solely corporate financing firms that advise companies on mergers and acquisitions, advise issuers on raising debt and equity capital in private placements with institutional investors, or provide advisory services on a consulting basis to companies that need assistance analyzing their strategic and financial alternatives. These firms often are registered as broker-dealers because they may receive transaction-based compensation as part of their services.

Nevertheless, these firms do not engage in many of the types of activities typically associated with traditional broker-dealers. For example, these firms typically do not carry or act as an introducing broker with respect to customer accounts, handle customer funds or securities, accept orders to purchase or sell securities either as principal or agent for the customer, exercise investment discretion on behalf of any customer, or engage in proprietary trading of securities or market-making activities.

FINRA is proposing to establish a separate rule set that would apply exclusively to firms that meet the definition of "capital acquisition broker" ("CAB") and that elect to be governed under this rule set. CABs would be subject to the FINRA By-Laws, as well as core FINRA rules that FINRA believes should apply to all firms. The rule set would include other FINRA rules that are tailored to address CABs' business activities.

General Standards (CAB Rule 010 Series)

Proposed CAB Rule 014 provides that all persons that have been approved for membership in FINRA as a CAB and persons associated with CABs shall be subject to the Capital Acquisition Broker rules and the FINRA By-Laws (including the schedules thereto), unless the context requires otherwise. Proposed CAB Rule 015 provides that FINRA Rule 0150(b) shall apply to the CAB rules. FINRA Rule 0150(b) currently provides that the FINRA rules do not apply to transactions in, and business activities relating to, municipal securities as that term is defined in the Exchange Act.

CAB Rule 016 sets forth basic definitions modified as appropriate to apply to CABs. The proposed definitions of "capital acquisition broker" and "institutional investor" are particularly important to the application of the rule set.

The term "capital acquisition broker" would mean any broker that solely engages in any one or more of the following activities:

- advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;

- providing fairness opinions, valuation services, expert testimony, litigation support, and negotiation and structuring services;
- qualifying, identifying, soliciting, or acting as a placement agent or finder with respect to institutional investors in connection with purchases or sales of unregistered securities; and
- effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company through the purchase, sale, exchange, issuance, repurchase, or redemption of, or a business combination involving, securities or assets of the company, to a buyer that will actively operate the company or the business conducted with the assets of the company, in accordance with the terms and conditions of an SEC rule, release, interpretation or "no-action" letter that permits a person to engage in such activities without having to register as a broker or dealer pursuant to Section 15(b) of the Exchange Act.[3]

A firm would be permitted to register as, or change its status to, a CAB only if the firm solely engages in one or more of these activities.

The term "capital acquisition broker" would not include any broker or dealer that:

- carries or acts as an introducing broker with respect to customer accounts;
- holds or handles customers' funds or securities;
- accepts orders from customers to purchase or sell securities either as principal or as agent for the customer (except as permitted by paragraphs (c)(1)(F) and (G) of CAB Rule 016);

3 See proposed CAB Rule 016(c)(1).

- has investment discretion on behalf of any customer;
- engages in proprietary trading of securities or market-making activities; or
- participates in or maintains an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933.[4]

The term "institutional investor" would have the same meaning as that term has under FINRA Rule 2210 (Communications with the Public), with one exception. The term would include any:

- bank, savings and loan association, insurance company or registered investment company;
- governmental entity or subdivision thereof;
- employee benefit plan, or multiple employee benefit plans offered to employees of the same employer, that meet the requirements of Section 403(b) or Section 457 of the Internal Revenue Code and in the aggregate have at least 100 participants, but does not include any participant of such plans;
- qualified plan, as defined in Section 3(a)(12)(C) of the Exchange Act, or multiple qualified plans offered to employees of the same employer, that in the aggregate have at least 100 participants, but does not include any participant of such plans;
- other person (whether a natural person, corporation, partnership, trust, family office or otherwise) with total assets of at least $50 million; and
- person acting solely on behalf of any such institutional investor.

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4 See proposed CAB Rule 016(c)(2).

The definition also would include any person meeting the definition of "qualified purchaser" as that term is defined in Section 2(a)(51) of the Investment Company Act of 1940 ("1940 Act").[5]

Member Application and Associated Person Registration (CAB Rule 100 Series)

The proposed CAB Rule 100 Series sets forth the requirements for firms that wish to register as a CAB. The proposed CAB Rule 100 Series generally incorporates by reference FINRA Rules 1010 (Electronic Filing Requirements for Uniform Forms), and 1122 (Filing of Misleading Information as to Membership or Registration), and NASD Rules 1011 (Definitions), 1012 (General Provisions), 1013 (New Member Application and Interview), 1014 (Department Decision), 1015 (Review by National Adjudicatory Council), 1016 (Discretionary Review by FINRA Board), 1017 (Application for Approval of Change in Ownership, Control, or Business Operations), 1019 (Application to Commission for Review), 1090 (Foreign Members), 1100 (Foreign Associates) and IM-1011-1 (Safe Harbor for Business Expansions). Accordingly, a CAB applicant would follow the same procedures for membership as any other FINRA applicant, with four modifications.

- First, an applicant for membership that seeks to qualify as a CAB would have to state in its application that it intends to operate solely as such.
- Second, in reviewing an application for membership as a CAB, the FINRA Member Regulation Department would consider, in addition to the standards for admission set forth in NASD Rule 1014, whether the applicant's proposed

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5 See proposed CAB Rule 016(i). FINRA Rule 2210 does not include "qualified purchaser" within its definition of "institutional investor."

activities are consistent with the limitations imposed on CABs under CAB Rule 016(c).

- Third, proposed CAB Rule 116(b) sets forth the procedures for an existing FINRA firm to change its status to a CAB. If an existing firm is already approved to engage in the activities of a CAB, and the firm does not intend to change its existing ownership, control or business operations, it would not be required to file either a New Member Application ("NMA") or a Change in Membership Application ("CMA"). Instead, such a firm would be required to file a request to amend its membership agreement or obtain a membership agreement (if none exists currently) to provide that: (i) the firm's activities will be limited to those permitted for CABs under CAB Rule 016(c), and (ii) the firm agrees to comply with the CAB rules.[6]
- Fourth, proposed CAB Rules 116(c) and (d) set forth the procedures for an existing CAB to terminate its status as such and continue as a FINRA firm. Under Rule 116(c), such a firm would be required to file a CMA with the FINRA Member Regulation Department, and to amend its membership agreement to provide that the firm agrees to comply with all FINRA rules.[7]

Under Rule 116(d), however, if during the first year following an existing FINRA member firm's amendment to its membership agreement to convert a full-service broker-dealer to a CAB pursuant to Rule 116(b) a CAB seeks to terminate its status as such and continue as a FINRA member firm, the CAB may notify the FINRA Membership

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[6] There would not be an application fee associated with this request.

[7] Absent a waiver, such a firm would have to pay an application fee associated with the CMA. See FINRA By-Laws, Schedule A, Section 4(i).

Application Program group of this change without having to file an application for approval of a material change in business operations pursuant to NASD Rule 1017. The CAB would instead file a request to amend its membership agreement to provide that the member firm agrees to comply with all FINRA rules, and execute an amended membership agreement that imposes the same limitations on the member firm's activities that existed prior to the member firm's change of status to a CAB.[8]

The proposed CAB Rule 100 Series also would govern the registration and qualification examinations of principals and representatives that are associated with CABs. These Rules incorporate by reference NASD Rules 1021 (Registration Requirements – Principals), 1022 (Categories of Principal Registration), 1031 (Registration Requirements – Representatives), 1032 (Categories of Representative Registration), 1060 (Persons Exempt from Registration), 1070 (Qualification Examinations and Waiver of Requirements), 1080 (Confidentiality of Examinations), IM-1000-2 (Status of Persons Serving in the Armed Forces of the United States), IM-1000-3 (Failure to Register Personnel) and FINRA Rule 1250 (Continuing Education Requirements). Accordingly, CAB firm principals and representatives would be subject to the same registration, qualification examination, and continuing education requirements as principals and representatives of other FINRA firms. CABs also would be subject to FINRA Rule 1230(b)(6) regarding Operations Professional registration.

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8 To the extent that the rules applicable to the member firm had been amended since it had changed its status to a CAB, FINRA would have the discretion to modify any limitations to reflect any new rule requirements.

Duties and Conflicts (CAB Rule 200 Series)

The proposed CAB Rule 200 Series would establish a streamlined set of conduct rules. CABs would be subject to FINRA Rules 2010 (Standards of Commercial Honor and Principles of Trade), 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices), 2040 (Payments to Unregistered Persons),[9] 2070 (Transactions Involving FINRA Employees), 2080 (Obtaining an Order of Expungement of Customer Dispute Information from the CRD System), 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information), 2263 (Arbitration Disclosure to Associated Persons Signing or Acknowledging Form U4), and 2268 (Requirements When Using Predispute Arbitration Agreements for Customer Accounts).

CAB Rules 209 and 211 would impose know-your-customer and suitability obligations similar to those imposed under FINRA Rules 2090 and 2111. CAB Rule 211(b) includes an exception to the customer-specific suitability obligations for institutional investors similar to the exception found in FINRA Rule 2111(b).

Proposed CAB Rule 221 is an abbreviated version of FINRA Rule 2210 (Communications with the Public), essentially prohibiting false and misleading statements.

Under proposed CAB Rule 240, if a CAB or associated person of a CAB had engaged in activities that would require the CAB to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on CABs under CAB Rule 016(c), FINRA could examine for and enforce all FINRA rules against such a

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9 The SEC has approved FINRA's rule change to adopt rules relating to payments to unregistered persons for the consolidated FINRA rulebook. See Regulatory Notice 15-07 (March 2015). FINRA Rule 2040 became effective on August 24, 2015.

broker or associated person, including any rule that applies to a FINRA broker-dealer that is not a CAB or to an associated person who is not a person associated with a CAB.

FINRA has determined not to subject CABs to FINRA Rules 2121 (Fair Prices and Commissions), 2122 (Charges for Services Performed), and 2124 (Net Transactions with Customers), since CABs' business model does not raise the same concerns that Rules 2121, 2122 and 2124 are intended to address.

Rule 2121 provides that, for securities in both listed and unlisted securities, a member that buys for its own account from its customer, or sells for its own account to its customer, shall buy or sell at a price which is fair, taking into consideration all relevant circumstances, including market conditions with respect to the security at the time of the transaction, the expense involved, and the fact that the member is entitled to a profit. Further, if the member acts as agent for its customer in any such transaction, the member shall not charge its customer more than a fair commission or service charge, taking into consideration all relevant circumstances, including market conditions with respect to the security at the time of the transaction, the expense of executing the order and the value of any service the member may have rendered by reason of its experience in and knowledge of such security and the market therefor.

CABs would not be permitted to act as a principal in a securities transaction. Accordingly, the provisions of Rule 2121 that govern principal transactions would not apply to a CAB's permitted activities.

CABs would be permitted act as agent in a securities transaction only in very narrow circumstances. CABs would be allowed to act as an agent with respect to institutional investors in connection with purchases or sales of unregistered securities.

CABs also would be permitted to effect securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company or the business conducted with the assets of the company in accordance with the terms and conditions of an SEC rule, release, interpretation or "no-action" letter.

In both instances, FINRA believes that these circumstances either involve institutional parties that negotiate the terms of permitted securities transactions without the need for the conditions set forth in Rule 2121, or involve the sale of a business as a going concern, which differs in nature from the types of transactions that typically raise issues under Rule 2121.

Rule 2122 provides that charges, if any, for services performed, including, but not limited to, miscellaneous services such as collections due for principal, dividends, or interest; exchange or transfer of securities; appraisals, safekeeping or custody of securities, and other services shall be reasonable and not unfairly discriminatory among customers. As discussed above, CABs typically provide services to institutional customers that generally do not need the protections that Rule 2122 offers, since these customers are capable of negotiating fair prices for the services that CABs provide. Moreover, CABs are not permitted to provide many of the services listed in Rule 2122, such as collecting principal, dividends or interest, or providing safekeeping or custody services.

Rule 2124 sets forth specific requirements for executing transactions with customers on a "net" basis. "Net" transactions are defined as a type of principal transaction, and CABs may not trade securities on a principal basis. For these reasons, FINRA does not believe it is necessary to include FINRA Rules 2121, 2122 and 2124 as part of the CAB rule set.

CAB Rule 201 would subject CABs to FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade), which requires a member, in the conduct of its business, to observe high standards of commercial honor and just and equitable principles of trade. Depending on the facts, other rules, such as Rule 2010, may apply in situations in which a CAB charged a commission or fee that clearly is unreasonable under the circumstances.

Supervision and Responsibilities Related to Associated Persons (CAB Rule 300 Series)

The proposed CAB Rule 300 Series would establish a limited set of supervisory rules for CABs. CABs would be subject to FINRA Rules 3220 (Influencing or Rewarding Employees of Others), 3240 (Borrowing from or Lending to Customers), and 3270 (Outside Business Activities of Registered Persons).

Proposed CAB Rule 311 would subject CABs to some, but not all, of the requirements of FINRA Rule 3110 (Supervision) and, consistent with Rule 3110, is designed to provide CABs with the flexibility to tailor their supervisory systems to their business models. CABs would be subject to many of the provisions of Rule 3110 concerning the supervision of offices, personnel, customer complaints, correspondence and internal communications. However, CABs would not be subject to the provisions of Rule 3110 that require annual compliance meetings (paragraph (a)(7)), review and investigation of transactions (paragraphs (b)(2) and (d)), specific documentation and supervisory procedures for supervisory personnel (paragraph (b)(6)), and internal inspections (paragraph (c)).

FINRA does not believe that the annual compliance meeting requirement in FINRA Rule 3110(a)(7) should apply to CABs given the nature of CABs' business model and structure. FINRA has observed that most current FINRA member firms that would qualify as CABs tend to be small and often operate out of a single office. In addition, the range of rules that CABs would be subject to is narrower than the rules that apply to other broker-dealers. Moreover, as noted above, CABs would be subject to both the Regulatory and Firm Element continuing education requirements. Accordingly, FINRA does not believe that CABs need to conduct an annual compliance meeting as required under FINRA Rule 3110(a)(7).[10] The fact that the annual compliance meeting requirement would not apply to CABs or their associated persons in no way would reduce their responsibility to have knowledge of and comply with applicable securities laws and regulations and the CAB rule set.

FINRA does not believe that FINRA Rule 3110(b)(2), which requires members to adopt and implement procedures for the review by a registered principal of all transactions relating to the member's investment banking or securities business, or FINRA Rule 3110(d), which imposes requirements related to the investigation of securities transactions and heightened reporting requirements for members engaged in investment banking services, should apply to CABs. CABs would not be permitted to carry or act as an introducing broker with respect to customer accounts, hold or handle customers' funds or securities, accept orders from customers to purchase or sell securities

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[10] For the same reasons, FINRA does not believe that FINRA Rule 3110.04 should apply to CABs.

except under the narrow circumstances discussed above, have investment discretion on behalf of any customer, engage in proprietary trading or market-making activities, or participate in Crowdfunding or Regulation A securities offerings. Accordingly, due to these restrictions, FINRA does not believe a CAB's business model necessitates the application of these provisions, which primarily address trading and investment banking functions that are beyond the permissible scope of a CAB's activities.[11]

FINRA does not believe that the requirements of FINRA Rule 3110(b)(6) should apply to CABs. Paragraph (b)(6) generally requires a member to have procedures to prohibit its supervisory personnel from (1) supervising their own activities; and (2) reporting to, or having their compensation or continued employment determined by, a person the supervisor is supervising.[12] FINRA also does not believe that FINRA Rule 3110(c), which requires members to conduct internal inspections of their businesses, should apply to CABs.

FINRA believes that a CAB's business model, which is geared toward acting as a consultant in capital acquisition transactions, or acting as an agent solely in connection with purchases or sales of unregistered securities to institutional investors, or with the

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[11] For the same reasons, FINRA does not believe that FINRA Rule 3110.05 should apply to CABs.

[12] FINRA Rule 3110(b)(6)(C)(i) and (ii). FINRA Rule 3110(b)(6) also requires that a member's supervisory procedures include the titles, registration status and locations of the required supervisory personnel and the responsibilities of each supervisory person as these relate to the types of business engaged in, applicable securities laws and regulations, and FINRA rules, as well as a record of the names of its designated supervisory personnel and the dates for which such designation is or was effective. FINRA Rule 3110(b)(6)(A) and (B). In addition, paragraph (b)(6) requires a member to have procedures reasonably designed to prevent the standards of supervision required pursuant to FINRA Rule 3110(a) from being compromised due to the conflicts of interest that may be present with respect to an associated person being supervised. FINRA Rule 3110(b)(6)(D).

transfer of ownership and control of a privately-held company, does not give rise to the same conflicts of interest and supervisory concerns that paragraph (b)(6) is intended to address. As discussed above, many CABs operate out of a single office with a small staff, which reduces the need for internal inspections of numerous or remote offices. In addition, part of the purpose of creating a separate CAB rule set is to streamline and reduce existing FINRA rule requirements where it does not hinder investor protection. FINRA believes that the remaining provisions of FINRA Rule 3110, coupled with the CAB Rule 200 Series addressing duties and conflicts, will sufficiently protect CABs' customers from potential harm due to insufficient supervision.[13]

Proposed CAB Rule 313 would require CABs to designate and identify one or more principals to serve as a firm's chief compliance officer, similar to the requirements of FINRA Rule 3130(a). CAB Rule 313 would not require a CAB to have its chief executive officer ("CEO") certify that the member has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable federal securities laws and regulations, and FINRA and MSRB rules, which are required under FINRA Rules 3130(b) and (c). FINRA does not believe the CEO certification is necessary given a CAB's narrow business model and smaller rule set.

Proposed Rule 328 would prohibit any person associated with a CAB from participating in any manner in a private securities transaction as defined in FINRA Rule

[13] For the same reasons, FINRA does not believe that FINRA Rules 3110.10, .12, .13, or .14 should apply to CABs. FINRA also believes that it is unnecessary to apply FINRA Rule 3110.15 to CABs, since the temporary program authorized by the rule expired on December 1, 2015.

3280(e).[14] FINRA does not believe that an associated person of a CAB should be engaged in selling securities away from the CAB, nor should a CAB have to oversee and review such transactions, given its limited business model. This restriction would not prohibit associated persons from investing in securities on their own behalf, or engaging in securities transactions with immediate family members, provided that the associated person does not receive selling compensation.

Proposed CAB Rule 331 would require each CAB to implement a written anti-money laundering ("AML") program. This is consistent with the SEC's requirements and Chapter X of Title 31 of the Code of Federal Regulations. Accordingly, the proposed rule is similar to FINRA Rule 3310 (Anti-Money Laundering Compliance Program); however, the proposed rule contemplates that all CABs would be eligible to conduct the required independent testing for compliance every two years.

Financial and Operational Rules (CAB Rule 400 Series)

The proposed CAB Rule 400 Series would establish a streamlined set of rules concerning firms' financial and operational obligations. CABs would be subject to FINRA Rules 4140 (Audit), 4150 (Guarantees by, or Flow through Benefits for, Members), 4160 (Verification of Assets), 4511 (Books and Records – General Requirements), 4513 (Records of Written Customer Complaints), 4517 (Member Filing

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14 FINRA Rule 3280(e) defines "private securities transaction" as "any securities transaction outside the regular course or scope of an associated person's employment with a member, including, though not limited to, new offerings of securities which are not registered with the Commission, provided however that transactions subject to the notification requirements of NASD Rule 3050, transactions among immediate family members (as defined in FINRA Rule 5130), for which no associated person receives any selling compensation, and personal transactions in investment company and variable annuity securities, shall be excluded."

and Contact Information Requirements), 4524 (Supplemental FOCUS Information), 4530 (Reporting Requirements), and 4570 (Custodian of Books and Records).

Proposed CAB Rule 411 includes some, but not all, of the capital compliance requirements of FINRA Rule 4110. CABs would be required to suspend business operations during any period a firm is not in compliance with the applicable net capital requirements set forth in SEA Rule 15c3-1, and the rule also would authorize FINRA to direct a CAB to suspend its operation under those circumstances. Proposed CAB Rule 411 also sets forth requirements concerning withdrawal of capital, subordinated loans, notes collateralized by securities, and capital borrowings.

CABs would not be subject to FINRA Rules 4370 (Business Continuity Plans and Emergency Contact Information) or 4380 (Mandatory Participation in FINRA BC/DR Testing Under Regulation SCI). FINRA does not believe it would be necessary for a CAB to maintain a business continuity plan (BCP), given a CAB's limited activities, particularly since a CAB would not engage in retail customer account transactions or clearance, settlement, trading, underwriting or similar investment banking activities. Moreover, FINRA Rule 4380 relates to Rule SCI under the Exchange Act, which is not applicable to a member that limits its activities to those permitted under the CAB rule set.

Because CABs would not carry or act as an introducing broker with respect to customer accounts, they would have more limited customer information requirements than is imposed under FINRA Rule 4512.[15] CABs would have to maintain each customer's name and residence, whether the customer is of legal age (if applicable), and the names of any persons authorized to transact business on behalf of the customer.

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[15] See proposed CAB Rule 451(b).

CABs would still have to make and preserve all books and records required under SEA Rules 17a-3 and 17a-4.

CAB Rule 452(a) establishes a limited set of requirements for the supervision and review of a firm's general ledger accounts.

Securities Offerings (CAB Rule 500 Series)

The proposed CAB Rule 500 Series would subject CABs to certain rules concerning securities offerings. CABs would be subject to FINRA Rules 5122 (Private Placements of Securities Issued by Members) and 5150 (Fairness Opinions).

Investigations and Sanctions, Code of Procedure, and Arbitration and Mediation (CAB Rules 800, 900 and 1000)

CABs would be subject to the FINRA Rule 8000 Series governing investigations and sanctions of firms, other than FINRA Rules 8110 (Availability of Manual to Customers), 8211 (Automated Submission of Trading Data Requested by FINRA), and 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA).

CABs would not be subject to FINRA Rule 8110 (Availability of Manual to Customers), which requires members to make available a current copy of the FINRA manual for examination by customers upon request. If the Commission approves this proposed rule change, the CAB rule set would be available through the FINRA website. Accordingly, FINRA does not believe this rule is necessary for CABs.

CABs also would not be subject to FINRA Rules 8211 (Automated Submission of Trading Data Requested by FINRA) or 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA). Given that these rules are intended to assist FINRA in requesting trade data from firms engaged in securities trading, and that CABs would not engage in securities trading, FINRA does not believe that these rules should apply to CABs.

CABs would be subject to the FINRA Rule 9000 Series governing disciplinary and other proceedings involving firms, other than the FINRA Rule 9700 Series (Procedures on Grievances Concerning the Automated Systems). Proposed CAB Rule 900(c) would provide that any CAB may be subject to a fine under FINRA Rule 9216(b) with respect to an enumerated list of FINRA By-Laws, CAB rules and SEC rules under the Exchange Act. Proposed CAB Rule 900(d) would authorize FINRA staff to require a CAB to file communications with the FINRA Advertising Regulation Department at least ten days prior to use if the staff determined that the CAB had departed from CAB Rule 221's standards.

CABs would be subject to the FINRA Rule 12000 Series (Code of Arbitration Procedure for Customer Disputes), 13000 Series (Code of Arbitration Procedure for Industry Disputes) and 14000 Series (Code of Mediation Procedure).

If the Commission approves the proposed rule change, FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 180 days following publication of the Regulatory Notice announcing Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,[16] which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will improve efficiency and reduce regulatory burden by reducing the range of rules that apply to capital acquisition brokers given their limited activities and institutional business model, while maintaining necessary investor protections.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. FINRA has undertaken an economic impact assessment, as set forth below, to analyze the regulatory need for the proposed rulemaking, its potential economic impacts, including anticipated costs and benefits, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

Economic Impact Assessment

A. Regulatory Need

As discussed above, many firms solely engage in corporate financing activities, including advising companies on mergers and acquisitions, advising issuers on raising debt and equity capital in private placements with institutional investors, or providing advisory services on a consulting basis. These firms often register as broker-dealers

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16 15 U.S.C. 78o–3(b)(6).

because they may receive transaction-based compensation as part of their services, but unlike traditional broker-dealers, they do not handle customer funds or securities, carry or act as an introducing broker with respect to customer accounts, or provide products and services to retail customers. As a result, many FINRA rules are not applicable to the business activities of these firms. The proposed rule change establishes a separate set of streamlined rules that would apply exclusively to these firms and is tailored to address their business activities, while maintaining necessary investor protections.

B. Economic Impacts

The proposed rule change would impact member firms that engage in CAB-related business activities, discussed above. As a baseline and based on staff experience, FINRA preliminarily estimates that the number of member firms that meet this definition would range from 650 to 750 firms.[17] Thus, it is possible that between 16 and 19 percent of all FINRA member firms may be eligible to operate under this proposed rule set.[18] These firms currently are required to comply with all applicable FINRA rules. These firms currently may incur costs to evaluate new FINRA rules and interpretations to ensure that they are not applicable for their business.

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17 FINRA notes that a commenter reported a higher estimate of 906 member firms that would meet the CAB definition based on information available on BrokerCheck® (See comment of 3PM). This estimate is based on the number of firms that report their business line (in Form BD) only as “Private Placement,” “Other,” or “Private Placement” and “Other.” FINRA notes that these business lines may overlap with some of the business activities of CABs, but do not exactly correspond to the activities that would meet the CAB definition.

18 There are 4,031 firms that are registered with FINRA as broker-dealers. Accordingly, 650 and 750 firms account for 16% and 19%, respectively, of the total FINRA membership. See https://www.finra.org/newsroom/statistics (accessed June 29, 2015).

FINRA anticipates that some firms provide similar services but are not currently registered as broker-dealers with the SEC or FINRA. For example, some firms may currently limit activities, such as not accepting transaction-based compensation for their services, to avoid broker-dealer registration requirements and attendant costs. Others may accept transaction-based compensation, but may be relying on SEC no-action relief to avoid broker-dealer registration.[19] It is possible that some of these firms would reconsider their non-registered status if the new rules were in effect.

(i) Anticipated Benefits

The proposed rule change would reduce the regulatory burden for CABs by decreasing the range and scope of current FINRA rules that would be applicable to them given their limited activities and institutional business model. For example, as discussed above, the proposed rule change would establish a streamlined set of conduct rules. Similarly, the proposed CAB rules would establish a limited set of supervisory rules that are better designed to provide CABs with the flexibility to tailor their supervisory systems to their business models. As discussed above, CABs also would be subject to more limited customer information requirements than those applicable to other broker-dealers.

The reduction in these regulatory requirements is anticipated to reduce compliance costs for member firms that would register as CABs without diminishing investor protections. These cost savings would include reduction in costs associated with maintaining FINRA membership, including ongoing compliance activities such as maintaining policies and procedures. These firms also would likely benefit from more

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19 See M&A Brokers, 2014 SEC No-Act. LEXIS 92 (January 31, 2014).

focused examinations that are tailored to their business activities. To avail themselves of these benefits, firms would, however, be required to maintain their CAB status and as a result limit their activities to those permitted under the CAB rules.

As discussed above, CAB rules also may encourage non-member firms that engage in similar kinds of services as CABs to register with FINRA. FINRA membership would benefit these non-member firms by allowing them to expand their securities business and engage in activities permitted under the CAB rules. FINRA membership would subject these firms to certain FINRA rules, including conduct rules, supervisory rules, and rules concerning financial and operational obligations of the firms. As a result, FINRA membership would increase regulatory oversight of these firms, thereby enhancing investor protection of their customers.

(ii) Anticipated Costs

A member firm that seeks to register as a CAB would incur initial legal and other compliance costs associated with effectively completing the application to amend its membership agreement to elect CAB status. Such a firm also would incur administrative costs associated with updating its policies and procedures. FINRA, however, anticipates that these costs would likely be minimal relative to the cost savings from the streamlined CAB rules. As firms would have discretion to determine whether to apply for the amended status, FINRA anticipates that only those firms that anticipate net benefits to them would do so.

Non-member firms that choose to register as a CAB would incur implementation and ongoing costs associated with joining and maintaining their broker-dealer registrations with FINRA. The initial implementation costs would include FINRA application fees, costs associated with adapting technology infrastructure for regulatory data reporting requirements, as well as other legal or consulting costs associated with developing policies and procedures to ensure continued compliance with SEC and CAB rules. The ongoing costs would include annual fees associated with FINRA membership, costs of maintaining data reporting, costs of legal work relating to FINRA membership, and other costs associated with additional compliance activities. FINRA notes, however, that the proposed rule change would not impose these costs on non-member firms because registering as a broker-dealer and electing CAB status is optional. Non-member firms would likely only choose to register as a CAB broker-dealer and incur these costs if the anticipated benefits of registering exceed the costs of doing so.

C. Alternatives

In considering how to best meet its regulatory objectives, FINRA considered several alternatives to particular features of this proposal. For example, the initial proposal would have allowed CABs to solicit only institutional investors as that term is defined in FINRA Rule 2210. As discussed in more detail below, several commenters suggested that the proposed rule change also allow CABs to provide products and services to accredited investors or qualified purchasers. FINRA's regulatory programs have uncovered significant concerns associated with the ways in which firms sell private placements to accredited investors. Accordingly, FINRA does not believe it is appropriate to lower the institutional investor threshold for the CAB rules to the accredited investor standard.

Nonetheless, FINRA agrees that the definition of institutional investor under the CAB rules should include qualified purchasers as that term is defined under the 1940 Act, since qualified purchasers are required to own significantly more investments than those required for accredited investors, and as a result qualified purchasers are more likely to have the resources necessary to protect themselves from potential sales practice problems. Accordingly, FINRA has revised the institutional investor definition to include qualified purchasers, which would allow CABs to offer interests in private funds that are excluded from the definition of "investment company" and thus exempt from registration under the 1940 Act, such as hedge funds or private equity funds.

In developing this proposal, FINRA also considered expanding the scope of permissible activities for CABs. For example, as discussed below, commenters suggested that FINRA allow CABs to engage in activities related to the transfer of ownership or control of a privately-held company consistent with the SEC's M&A Brokers no-action letter. FINRA agrees that CABs should be permitted to engage in merger and acquisition transactions to the same extent as an unregistered broker-dealer pursuant to the M&A Brokers no-action letter and has revised the definition of CAB to allow such activities.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Background

In February 2014, FINRA published Regulatory Notice 14-09 (the "Notice"), requesting comment on a proposed rule set for firms that meet the definition of "limited corporate financing broker" ("LCFB") (the "Notice proposal"). A copy of the Notice is attached as Exhibit 2a. The comment period expired on April 28, 2014. FINRA received

51 comments in response to the Notice.[20] A list of the commenters in response to the Notice is attached as Exhibit 2b, and copies of the comment letters received in response to the Notice are attached as Exhibit 2c.[21] A summary of the comments and FINRA's response is provided below.

As discussed below, most of the comments opposed the Notice proposal on the ground that it did not go far enough to relieve LCFBs of their current regulatory burdens. This concern, combined with the limitations in activities that the proposal's rules would impose, would lead most firms commenting on the proposal not to change their status to an LCFB.[22]

Application of LCFB Rules to Municipal Securities

LCFB Rule 015 would have stated that the LCFB rules do not apply to transactions in, and business activities relating to, municipal securities as defined in Section 3(a)(29) of the Exchange Act. One commenter noted that some FINRA member firms provide financial advisory services only to municipalities or municipal agencies, including recommending the timing and type of offering and to assist in the selection of an underwriter. The commenter stated that if this type of firm does not engage in the sale

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20 Twenty-one of the comments were short emails or letters endorsing the comments of 3PM.

21 See Exhibit 2b for a list of abbreviations assigned to commenters.

22 As noted above, the proposal would have referred to firms subject to the proposed rule set as "limited corporate financing brokers" ("LCFBs") rather than "capital acquisition brokers" ("CABs"). Similarly, this discussion refers to the rules proposed in the Notice as the "LCFB rules" rather than the "CAB rules." The CAB rules which are submitted as part of this proposed rule change have been revised from the prior LCFB rules, but maintain the same rule numbers as the LCFB rules.

of municipal securities and would otherwise qualify, it should be eligible to be an LCFB.[23]

LCFB Rule 015 would not prevent an LCFB from engaging in municipal securities activities. Rather, as revised, it simply would clarify that FINRA Rule 0150(b) applies to the CAB rules. FINRA Rule 0150(b) currently provides that the FINRA rules do not apply to transactions in, and business activities relating to, municipal securities as defined in the Exchange Act.

Definition of "Customer"

LCFB Rule 016(d) would have defined the term "customer" as "any natural person and any entity receiving corporate financing services from an LCFB." It also would have specified that the term "customer" does not include a broker or dealer.

One commenter stated that this definition is unclear and should be replaced with other terms, such as "issuer," "investor," "qualified investor," and "intermediary," since these terms better describe the counterparties involved in an LCFB's business.[24] Two other commenters recommended that FINRA use the term "client" rather than "customer."[25] Another commenter suggested that FINRA be clearer as to what types of corporate financing services a customer may receive from an LCFB.[26]

FINRA does not believe it would be appropriate to replace the term "customer" with other terms such as issuer, investor, or intermediary. The meaning of the term

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23 See Sutter.

24 See 3PM.

25 See Achates and Q Advisors.

26 See CFSC.

"customer" depends on the context in which it is used, such as the requirements to know your customer or to recommend a suitable investment to a customer. Terms such as "issuer" or "investor" would not be appropriate in these contexts. However, FINRA does believe that the term customer should be interpreted in a manner consistent with the way it is interpreted under the FINRA rules. Accordingly, FINRA has revised this term to have the same definition as it has under the FINRA rules.[27]

Institutional Investor Definition

LCFB Rule 016(h) would have allowed an LCFB to solicit only institutional investors. LCFB Rule 016(g) would have defined the term "institutional investor" to include banks, savings and loan associations, insurance companies, registered investment companies, governmental entities and their subdivisions, employee benefit plans and qualified plans with at least 100 participants (but not including the participants themselves), any other person with at least $50 million in assets, and persons acting on an institutional investor's behalf.

Seven commenters recommended that the LCFB rules allow LCFBs to offer interests in privately placed companies to accredited investors, as that term is defined in SEC Regulation D.[28] One commenter noted that requiring an LCFB to pre-qualify potential investors to meet the LCFB rules' definition of institutional investor, rather than the Regulation D accredited investor definition, would be difficult, since an LCFB may not know the financial status of a potential buyer, and could potentially harm an LCFB

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27 See FINRA Rule 0160(b)(4) ("The term 'customer' shall not include a broker or dealer").

28 See Achates, LIATI, SFA, Dole, RWI, HighBank, and EYCA. See also 17 CFR 230.501(a).

client seller by diminishing the pool of prospective investors.[29] Three other commenters recommended that the term "institutional investor" be replaced with a new term, "qualified investor," which would include "qualified investors" as that term is defined under the 1940 Act.[30] One commenter questioned whether an LCFB would be permitted to accept an unsolicited offer from a non-institutional investor.[31] Another commenter inquired as to the documents that FINRA would require an LCFB to retain to confirm an investor's institutional status.[32]

As discussed in the Notice, FINRA purposely did not propose to define "institutional investor" based on a more inclusive standard, such as the definition of "accredited investor" in Regulation D under the Securities Act of 1933. FINRA's regulatory programs have uncovered serious concerns with the manner in which firms market and sell private placements to accredited investors. Application of the CAB rules to firms that market and sell private placements to accredited investors would require FINRA to expand the applicable conduct rules and other provisions. Therefore, lowering the threshold of "institutional investor" to the accredited investor standard would frustrate the purposes of a streamlined rule set.

Nevertheless, FINRA agrees that the definition of "institutional investor" should include persons that meet the definition of "qualified purchaser" under the 1940 Act.[33]

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[29] See SFA.

[30] See 3PM, Q Advisors, and M&A Brokers Letter Attorneys.

[31] See SFA.

[32] See EYCF.

[33] See 15 U.S.C. 80a-2(a)(51).

Persons that meet the definition of "qualified purchaser" in most cases must own not less than $5 million in investments, far greater than the minimum assets required by the accredited investor standard. FINRA believes that it is much less likely that a CAB would commit the types of sales practice problems that FINRA has observed in connection with the sale of Regulation D private placements to accredited investors if an investor is required to meet the qualified purchaser standard, since a qualified purchaser likely would have the resources necessary to protect itself from potential sales practice problems. In addition, by defining "institutional investor" to include qualified purchasers, CABs would be able to offer interests in private issuers, such as hedge funds or private equity funds, that are excepted from the definition of "investment company" pursuant to Section 3(c)(7) of the 1940 Act.

Moreover, as discussed below, FINRA has proposed to expand the permissible activities of CABs to include effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company in accordance with the terms and conditions of an SEC rule, release, interpretation or no-action letter.[34] By expanding CABs' proposed activities to include these kinds of M&A transactions, CABs would not be limited to selling ownership or control of a privately-held company only to institutional investors as defined by the CAB rules, since the SEC's M&A Brokers no-action letter[35] does not contain this limitation. FINRA believes this expansion should address many of the commenters' concerns with the institutional investor definition.

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[34] See proposed CAB Rule 016(c)(1)(G).

[35] See M&A Brokers, 2014 SEC No-Act. LEXIS 92 (January 31, 2014).

Limited Corporate Financing Broker Definition

The proposed definition of LCFB would have allowed firms meeting this definition to engage in:

- advising an issuer, including a private fund concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions; and
- qualifying, identifying, or soliciting potential institutional investors.

The proposed definition of LCFB would have excluded any broker or dealer that carries or maintains customer accounts, holds or handles customers' funds or securities, accepts orders from customers to purchase or sell securities either as principal or agent for the customer, possesses investment discretion on behalf of any customer, or engages in proprietary trading of securities or market making activities.

Although one commenter felt that the definition of LCFB was appropriate,[36] others recommended that the definition of LCFB be amended specifically to permit an

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[36] See 3PM.

LCFB to provide valuation services,[37] expert testimony and litigation support.[38] Other commenters recommended that the definition be clarified to permit LCFBs to engage in negotiation of transactions,[39] and to act as a placement agent for a buyer or seller.[40] Another commenter urged FINRA to revise the definition so that it spells out in more detail the types of advice that an LCFB may provide to a client (e.g., preparing a business for sale, financial modeling, financial alternatives, evaluating competing offers, structuring transactions, due diligence and transition issues) and that it should allow an LCFB to act as a finder (introducing parties to a transaction).[41] Others recommended that LCFBs be permitted to provide research and engage in public company transactions in connection with their advisory work.[42]

Commenters also suggested that FINRA allow LCFBs to advise controlling or minority shareholders in a private business in connection with the sale of stock,[43] and that FINRA look to the SEC's M&A Brokers letter for a description of appropriate LCFB activities.[44] The latter commenter also recommended that LCFBs be allowed to solicit non-institutional investors if both the seller and buyer are or will be actively involved in running the business (which also is consistent with the M&A Brokers letter).

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[37] See CFSC.

[38] See Sutter and RWI.

[39] See Q Advisors.

[40] See Q Advisors and M&A Brokers Letter Attorneys.

[41] See RWI.

[42] See Fells and EYCF.

[43] See Harris.

[44] See ABA.

FINRA intended to allow CABs to provide valuation, expert testimony, litigation support, negotiation and structuring services, and to act as a placement agent for, or finder of, institutional investors. Accordingly, FINRA has revised the definition of CAB to make this clearer. FINRA does not agree, however, that CABs should be allowed to produce research for the investing public. If a CAB produced research reports, FINRA would need to consider whether to add FINRA Rule 2241 and potentially other rules to the list of CAB rules, which currently do not include these rules.

FINRA agrees that CABs should be permitted to engage in M&A transactions to the same extent as an unregistered broker pursuant to the M&A Brokers no-action letter. Accordingly, FINRA has revised the definition of CAB to allow such firms to effect securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company in accordance with the terms and conditions of an SEC rule, release, interpretation or no-action letter that permits a person to engage in such activities without registering as a broker under Section 15(b) of the Exchange Act.[45]

One commenter argued that the term "limited corporate financing broker" itself is problematic because it may confuse clients into thinking that a firm has reduced its servicing offerings when in fact they remain unchanged.[46] In response to this concern,

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[45] FINRA also revised the list of activities that a CAB may not engage in to clarify that a CAB may not carry or act as an introducing broker with respect to customer accounts or participate in or maintain an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933. See proposed CAB Rule 016(c)(2).

[46] See McCracken.

FINRA has changed the name of this defined term, and the name of the rule set, from "limited corporate financing broker" to "capital acquisition broker."

New Member and Change of Business Applications

LCFB Rule 112 would have subjected LCFBs to NASD Rule 1013, which governs new FINRA membership applications. LCFB Rule 112 also would have required applicants for FINRA membership that seek to qualify as LCFBs to state in their applications that they intend to operate as an LCFB.

LCFB Rule 116 would have subjected LCFBs to NASD Rule 1017, which governs applications for approval of change in ownership, control, or business operations. Rule 116 also would have allowed an existing FINRA member firm that seeks to change its status to an LCFB, and that is already approved to engage in the activities of an LCFB, but which does not intend to change its existing ownership, control, or business operations, to file a request to amend its membership agreement or obtain a membership agreement (if none exists), to provide that: (i) the member firm's activities will be limited to those permitted for LCFBs under LCFB Rule 016(h); and (ii) the member firm agrees to comply with the LCFB rules. Rule 116 further specified that an LCFB that seeks to terminate its status as such and continue as a FINRA member firm would have to file an application for approval of a material change in business operations pursuant to NASD Rule 1017 (a "CMA"), and would have to amend its membership agreement to provide that it agrees to comply with all FINRA rules.

One commenter also recommended that FINRA streamline the new member and change in membership process for LCFBs, reduce the time period for decisions, and lower the application fees.[47] Other commenters stated that any request to change a firm's membership agreement to elect LCFB status should be without a fee, and that firms should be allowed to revert back to their original non-LCFB status without having to file a change in membership application during the firm's first year of operation as an LCFB.[48] Commenters also noted that the proposed requirement to pay a $5000 fee as part of the CMA in order to buy back a firm's full broker status is a substantial disincentive to become an LCFB.[49]

FINRA does not agree that it should create a different new member process for applicants that are not already registered broker-dealers and that seek to become CABs. Although CABs would be subject to fewer FINRA requirements than other broker-dealers, FINRA still believes that it is important for investor protection and industry confidence reasons that FINRA have an opportunity to vet new CAB firms in the same manner that FINRA vets other new firm applicants. Similarly, if a firm wishes to change its ownership, control or business operations, FINRA believes that it is important that these changes receive the same review as any other registered firm. FINRA has modified CAB Rule 112, however, to clarify that a CAB applicant must state in its application that it intends to operate solely as a CAB.[50]

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47 See M&A Brokers Letter Attorneys.

48 See 3PM and RWI.

49 See Achates and RWI.

50 FINRA also has modified CAB Rules 111, 112, 113, 114, and 115 to clarify that they apply to persons applying for membership in FINRA as a CAB as well as to the CABs themselves.

CAB Rule 116 already permits an existing FINRA member firm to elect CAB status by requesting a change in its membership agreement, and without filing a CMA or paying a filing fee. However, FINRA agrees that Rule 116 should provide some more flexibility to a CAB that seeks to revert to its full broker status within the first year after electing CAB status. Accordingly, FINRA has amended Rule 116 to provide that, if during the first year following an existing FINRA member firm's amendment to its membership agreement to elect CAB status, the firm seeks to terminate its CAB status and continue as a FINRA member firm, the firm may notify the Membership Application Program group of this change without having to file a CMA. The member firm seeking this change would have to file a request to amend its membership agreement to provide that the firm agrees to comply with all FINRA rules, and execute an amended membership agreement that imposes the same limitations on the firm's activities that existed prior to the firm's change to CAB status.

Registration Categories

Proposed LCFB Rule 123 would have allowed persons registered with LCFBs to hold only a limited set of registrations that relate to an LCFB's business.[51] The proposal also would have subjected LCFBs to the Operations Professional (Series 99) registration requirement.

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51 Registered principals of LCFBs would have been permitted to hold the General Securities Principal (Series 24), Limited Principal – Financial and Operations (Series 27), Limited Principal – Introducing Broker/Dealer Financial and Operations (Series 28), and Limited Principal – General Securities Sales Supervisor (Series 9 and 10) registrations. Registered representatives of LCFBs would have been permitted to hold the General Securities Representative (Series 7), Limited Representative – Direct Participation Programs (Series 22), Limited Representative – Private Securities Offerings (Series 82), and Limited Representative – Investment Banking (Series 79) registrations.

Commenters objected to limiting the types of registrations that an associated person of an LCFB may retain.[52] Commenters noted that registered persons may be required to hold other registrations under state law.[53] In addition, commenters argued that this restriction would penalize individuals who may want to change jobs later and return to a full service broker-dealer, where other registrations would be required. They favored allowing registered persons to retain their registrations while employed with an LCFB. Commenters also opposed requiring LCFBs to employ an Operations Professional.[54] Two commenters encouraged FINRA, as part of this process, to re-examine the permissible scope of activities of various registration categories, such as Series 22, 62, 79 and 82 registrations.[55]

However, one commenter supported the restrictions. It recommended that LCFB representatives be required to obtain the Series 79 registration, and that LCFB representatives not be permitted to obtain other registration categories or retain other existing registrations during the time they are associated with an LCFB.[56] Another commenter suggested that LCFB principals and representatives not be permitted to hold other registrations unless a firm can adequately supervise the activities covered by those registrations.[57]

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52 See 3PM, Achates, Signal Hill, Sutter, LIATA, RWI, HighBank, M&A Brokers Letter Attorneys, and EYCA.

53 See 3PM, Achates, Sutter, and Q Advisors.

54 See 3PM and M&A Brokers Letter Attorneys.

55 See ABA and LeGaye.

56 See CFSC.

57 See Harris.

FINRA is persuaded that not allowing registered principals and representatives to obtain and hold the full range of registration categories could potentially penalize individuals who have already obtained those registration categories, and that the limitations of proposed LCFB Rule 123 also could potentially conflict with state law requirements. Accordingly, FINRA is amending CAB Rule 123 to eliminate the prior restrictions on the types of registrations persons associated with CABs may hold. Associated persons still would only be permitted to retain registrations that are appropriate to their functions under the registration rules.

FINRA continues to believe that CABs should be subject to FINRA Rule 1230(b)(6) regarding Operations Professional (Series 99) registration. FINRA believes the Operations Professional registration category enhances the regulatory structure surrounding the specified (or "covered" functions), including contributing to the process of preparing and filing financial regulatory reports, and has noted that for some firms the Operations Professional often may be the firm's Financial and Operations Principal.[58] FINRA also is not re-examining the range of permissible activities for principals and representatives in various registration categories, as those issues are beyond the scope of this proposed rule change.

Continuing Education Requirements

Proposed LCFB Rule 125 would have required any person registered with an LCFB who has direct contact with customers in the conduct of the broker's corporate financing activities, and the immediate supervisors of such persons, to be subject to many of the same requirements contained in the Firm Element provisions of FINRA Rule 1250.

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[58] See Regulatory Notice 11-33 (July 2011).

Proposed LCFB Rule 125 would not have subjected persons registered with an LCFB to the Regulatory Element provisions of FINRA Rule 1250, however.

One commenter stated that it was not opposed to requiring registered persons to undergo additional training and continuing education testing to keep an associated person's registration active, but proposed that these requirements be imposed only once every two years.[59] Another commenter questioned exempting LCFB personnel from the Regulatory Element requirements of FINRA Rule 1250, and noted that investment bankers need to keep up with current rules and regulations as much as other types of brokers.[60]

Given that FINRA has revised the proposed registration rules to allow persons registered with a CAB to hold and retain any principal and representative registrations that are appropriate to their functions under the registration rules, FINRA believes it is appropriate to subject associated persons to all of the continuing education requirements of FINRA Rule 1250, including the Regulatory Element provisions. FINRA has amended CAB Rule 125 accordingly.

Expungement of Customer Dispute Information

Proposed LCFB Rule 208 (Obtaining an Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD) System) would have subjected LCFBs to FINRA Rule 2080, which sets forth requirements for members or associated persons seeking to expunge information from the CRD system arising from disputes with customers. FINRA did not receive any comments on this proposed rule.

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59 See 3PM.

60 See Washington U.

Since the Notice was published, FINRA Rule 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information) became effective.[61] FINRA Rule 2081 prohibits members and associated persons from conditioning or seeking to condition settlement of a customer dispute on, or otherwise compensating the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer information from the CRD system. The rule directly addresses any concerns about parties to a settlement "bargaining for" expungement relief as a condition to settlement and should apply equally to any CAB or its associated persons seeking to expunge information from the CRD system. Accordingly, FINRA has amended LCFB Rule 208 also to subject CABs and their associated persons to FINRA Rule 2081.

Know Your Customer and Suitability

Proposed LCFB Rules 209 (Know Your Customer) and 211 (Suitability) would have included slightly modified versions of the know your customer ("KYC") and suitability requirements of FINRA Rules 2090 and 2111. Proposed LCFB Rule 211(b) specified that an LCFB or its associated person fulfills the customer-specific suitability obligations for an institutional account, as defined by FINRA Rule 4512(c), if (1) the broker or associated person has a reasonable basis to believe that the institutional customer is capable of evaluating investment risks independently, both in general and with regard to particular transactions and investment strategies involving a security or securities and (2) the institutional customer affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's

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[61] See Regulatory Notice 14-31 (July 2014).

recommendations. Where an institutional customer has delegated decision-making authority to an agent, such as an investment adviser or bank trust department, the rule would have applied these factors to the agent.

One commenter recommended that proposed LCFB Rule 209 be redrafted to remove any reference to "customer," instead suggesting that LCFBs should be required to perform due diligence of issuers, as well as reviews of investors and intermediaries considering whether to invest in an issuer to ensure qualified status.[62] Another commenter argued that the rule as written is too vague, and that an examiner would be unable to know if a firm had met its obligations to effectively service a customer.[63]

Commenters also were largely critical of proposed LCFB Rule 211. One commenter stated that it was inappropriate to require a suitability analysis before any recommendation, and that the rule was written as if an LCFB services retail customers. This commenter suggested that any suitability analysis should only be required before a subscription or purchase agreement is signed, and only where an investor is not represented by a qualified intermediary.[64] Another commenter encouraged FINRA to more clearly define a "recommendation" in this context and reconsider the definition of "customer" under the proposed rules.[65]

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62 See 3PM.

63 See Sutter.

64 See 3PM.

65 See ABA.

On the other hand, one commenter stated that LCFBs advise issuers, and that the KYC and suitability requirements should apply to these types of firms.[66] Two other commenters agreed that LCFBs advise both sell-side and buy-side M&A clients, but do not make recommendations to customers in the traditional sense.[67]

FINRA believes that the KYC and suitability rules should apply to CABs. The KYC rule requires CABs to use reasonable diligence to know and retain the essential facts concerning every customer and concerning the authority of each person acting on behalf of such customer. Facts essential to knowing a firm's customer are those required to (a) effectively service the customer, (b) understand the authority of each person acting on behalf of the customer, and (c) comply with applicable laws, regulations and rules.

The rule is flexible in that it recognizes that the determination of what is required to service a particular client will always be based on the facts and circumstances of a firm's relationship with its client. Likewise, the fact that a firm's client is a party to an M&A or other private equity transaction does not alter the need to understand the authority of each person acting on behalf of the customer, or facts necessary to comply with applicable laws, regulations and rules. Again, these facts will depend on each transaction's facts and circumstances, and the rule recognizes this flexibility.

Likewise, FINRA also believes that CABs should be subject to suitability requirements. If a CAB does not recommend a securities transaction, as some commenters assert, then the suitability requirements would not apply. Likewise, the proposed rule specifies that a CAB or associated person fulfills the customer specific

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66 See RWI.

67 See HighBank and CSP.

suitability requirements for institutional investors if (1) the broker or associated persons has a reasonable basis to believe that the institutional investor is capable of evaluating investment risks independently and (2) the institutional investor affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's recommendations. If the institutional investor has delegated decision-making authority to an agent, these factors apply to the agent. FINRA believes that this provision largely addresses concerns expressed by commenters that the proposed rule applies retail investor requirements to transactions involving institutional investors. It also recognizes that a CAB or its associated person may look to an institutional investor's agent if the investor is represented by an agent.

FINRA has added supplementary material to proposed Rule 211 to clarify that a CAB still must have a reasonable basis to believe, based on reasonable diligence, that a recommendation is suitable for at least some investors. FINRA also has added supplemental material providing guidance with regard to the institutional investor exemption from the customer specific suitability requirements. The text of both of these supplementary materials is taken from similar supplementary materials that follow FINRA Rule 2111. FINRA believes that these additions will help clarify the scope of a CAB's suitability responsibilities under proposed Rule 211.

FINRA also has revised the definition of "customer" to reflect the definition of this term under FINRA Rule 0160(b)(4). As revised, customer is defined as not including a broker or dealer. FINRA is making this change to make clear that the definition of customer under the CAB rules has the same meaning as under the FINRA rules.

Communications with the Public

Proposed LCFB Rule 221 would have required LCFB communications to meet the general principles-based content standards of FINRA Rule 2210, although it also would have prohibited LCFB communications from projecting or predicting performance. Proposed LCFB Rule 221 would not have required LCFBs to approve communications prior to use, nor would it have imposed any filing requirements for LCFB communications.

One commenter recommended that the proposed rule's content standards include a "realistic approach" to setting fair and balanced content standards to meet the realities of representing issuers of securities.[68] Another commenter argued that the proposed rule does not sufficiently protect investors, and that it should require new firms to file communications with FINRA and require registered principals to approve firm communications prior to use.[69] Another commenter argued that the cost of archiving emails for three years and reviewing emails periodically is burdensome.[70]

FINRA believes that proposed CAB Rule 221 is already sufficiently general to take into account the institutional nature of CABs' business models. However, FINRA recognizes that firms may need to include projections of an issuer's performance in communications that are sent to prospective investors, such as pro forma financial statements related to a business acquisition or combination. For this reason, FINRA has removed the prohibition on predictions or projections of performance. The proposed rule

68 See 3PM.

69 See CFSC.

70 See Colonnade.

would continue to prohibit communications from implying that past performance will recur or making any exaggerated or unwarranted claim, opinion or forecast.

FINRA does not believe it is necessary to include either principal pre-use approval or filing requirements for CABs given the institutional nature of their business. CABs will be required to supervise communications, but FINRA intends to allow CABs the flexibility to determine the best means of such supervision given each firm's business model. LCFBs will be subject to the SEC's record-keeping requirements for emails under Exchange Act Rules 17a-3 and 17a-4, which FINRA has no authority to alter.

Engaging in Impermissible Activities

Proposed LCFB Rule 240 provided that, upon finding that an LCFB or associated person of an LCFB has engaged in activities that require the firm to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on LCFBs under LCFB Rule 016(h), FINRA may examine for and enforce all FINRA rules against such a broker or associated person, including any rule that applies to a FINRA member broker-dealer that is not an LCFB or to an associated person who is not a person associated with an LCFB. One commenter argued that an LCFB that engages in impermissible activities should be given a defined remedial period and process for any unintentional activities of an LCFB until the rules have been in place for a while, given the potential for rule ambiguity.

FINRA does not believe it is necessary to include within the rule a specific remedial period for engaging in impermissible activities. FINRA believes that unintentional violations during a transition period are best handled through the examination and enforcement process on a case-by-case basis. Accordingly, FINRA is not proposing to amend the rule.

Outside Business Activities of Registered Persons

Proposed LCFB Rule 327 would have required LCFBs to be subject to FINRA Rule 3270 (Outside Business Activities). One commenter urged FINRA to clarify an LCFB's supervisory responsibilities when an associated person engages in private securities transactions away from the firm under NASD Rule 3040, and an LCFB's supervisory obligations when an associated person either is also registered with an affiliated or unaffiliated full-service broker-dealer or refers a customer to a full-service firm in return for a referral fee.[71]

An associated person of a CAB would not be permitted to engage in private securities transactions away from the firm, since such activities would be beyond the scope of permissible activities for a CAB under proposed CAB Rule 016(c).[72] However, in order to make this restriction more clear, FINRA has added CAB Rule 328, which would expressly prohibit associated persons of CABs from engaging in private securities transactions as defined in FINRA Rule 3280(e).

For the same reasons, an associated person of a CAB also would not be allowed to register with an affiliated or unaffiliated full-service broker-dealer. An associated person could receive a fee for referring business to another broker-dealer, provided that the proposed transaction would be permissible for the CAB to conduct itself.

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71 See CFSC.

72 See CAB Rule 014 ("Persons associated with a capital acquisition broker shall have the same duties and obligations as a capital acquisition broker under the Capital Acquisition Broker rules").

Anti-Money Laundering Compliance Program

Proposed LCFB Rule 331 would require an LCFB to develop and implement a written AML program reasonably designed to achieve and monitor its compliance with the requirements of the Bank Secrecy Act and the Department of Treasury regulations thereunder. The AML program would have to meet many of the same standards that full-service broker-dealers must meet under FINRA Rule 3310, except that the program would provide for independent testing for compliance no less frequently than every two years, rather than every year.

Five commenters stated that AML audits should not be required for LCFBs, since such firms receive no customer deposits and have no customer accounts.[73] Another commenter argued that LCFBs should only have to implement a customer identification program ("CIP") for issuers and intermediaries with which the LCFB does business, and for investors where there is no intermediary.[74] However, another commenter stated that there is no reason to exempt an LCFB from the one-year AML testing requirement.[75]

Because the Bank Secrecy Act imposes AML obligations on all broker-dealers, FINRA does not believe it has the authority to exempt CABs from the requirement to adopt and implement an AML program. However, due to the limited nature of CABs' securities transactions, FINRA believes it is appropriate to allow CABs to conduct independent compliance testing of their AML programs every two years rather than every year.

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73 See Growth Venture, Signal Hill, Q Advisors, CSP, and LeGaye.

74 See 3PM.

75 See CFSC.

Capital Compliance

Proposed LCFB Rule 411 would impose on LCFBs certain requirements imposed on full-service broker-dealers under FINRA Rule 4110 (Capital Compliance). Unless otherwise permitted by FINRA, an LCFB would have to suspend all business operations during any period in which it is not in compliance with the applicable net capital requirements set forth in Exchange Act Rule 15c3-1. The proposed rule also would authorize FINRA to issue a notice pursuant to FINRA Rule 9557 directing a non-compliant LCFB to suspend all or a portion of its business. The proposed rule would impose requirements related to withdrawal of equity capital, subordinated loans, and notes collateralized by securities and capital borrowings similar to provisions in FINRA Rule 4110.

Numerous commenters recommended that FINRA either eliminate or substantially reduce net capital requirements for LCFBs,[76] and that FINRA overhaul the net capital and FOCUS reporting requirements to better apply these requirements to LCFBs' business model.[77]

The SEC, however, sets these standards under its net capital rules and FINRA believes that the SEC would have to adjust its net capital requirements before FINRA could alter the net capital requirements that it imposes under its rules. In this regard, FINRA has clarified the CAB rules to note that CABs would be required to file supplemental FOCUS reports pursuant to FINRA Rule 4524 as FINRA may deem necessary or appropriate for the protection of investors or in the public interest.

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[76] See Growth Venture and LIATI.

[77] See 3PM, Colonnade, Bridge 1, CMC, McCracken, RWI, M&A Brokers Letter Attorneys, IMS, and Stonehaven.

Audit

Numerous commenters urged FINRA to work with the SEC and the Public Company Accounting Oversight Board ("PCAOB") to carve out LCFBs from the requirement to produce audited financial statements.[78] Two commenters recommended that, as an alternative to an audit, LCFBs' financials could be subject to an AICPA "review."[79] Another commenter recommended that audits not be required unless a firm has 20 or more employees or $10 million in net revenues.[80]

FINRA believes that it does not have the authority to reduce or eliminate the requirement to obtain audited financial statements.

Fidelity Bonds

The proposal would subject LCFBs to FINRA Rule 4360, which requires each member firm required to join the Securities Investor Protection Corporation ("SIPC") to maintain blanket fidelity bond coverage that provides against loss and have insuring agreements covering at least six enumerated areas. The minimum required fidelity bond amount varies depending on a firm's net capital requirements, but in any case it must be at least $100,000.

Some commenters argued this requirement should not apply to LCFBs, since fidelity bonds protect against theft of a customer's funds. Because LCFBs may not accept or hold customer funds, these commenters argue that the bond requirement makes

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78 See 3PM, Achates, Colonnade, Growth Venture, Signal Hill, Sutter, LIATA, Bridge 1, Q Advisors, Dole, McCracken, HighBank, CSP, M&A Brokers Letter Attorneys, LeGaye, and IMS.

79 See Achates and RWI.

80 See Anderson.

no sense.[81] One commenter noted that an LCFB that issues a fairness opinion should be required to carry a larger fidelity bond than $100,000.[82]

In response to these comments, FINRA has determined not to subject CABs to FINRA Rule 4360 because of CABs' unique business model. CABs' clients would be limited to issuers of unregistered securities, institutional investors, and parties to a transaction involving the change of control of a privately held company. CABs would act as agent only in transactions in which funds flow directly from a purchaser of securities to the issuer or shareholder of such securities, and would not carry or act as an introducing broker in connection with customer accounts. In addition, CABs would belong to a separate FINRA membership category that would make them unique among all other FINRA member firms. For these reasons, FINRA believes it would be appropriate not to require CABs to maintain a fidelity bond under Rule 4360.

SIPC Dues

Thirteen commenters argued that an LCFB should not have to pay dues to SIPC on the ground that an LCFB would not carry or act as an introducing broker with respect to customer accounts or hold or handle customer funds.[83]

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[81] See 3PM, Colonnade, Growth Venture, LIATI, Bridge 1, Q Advisors, Dole, McCracken, RWI, HighBank, CSP, LeGaye, IMS, and Stonehaven.

[82] See Sutter.

[83] See 3PM, Anderson, LIATI, Bridge 1, Q Advisors, Dole, McCracken, RWI, HighBank, CSP, LeGaye, IMS, and Stonehaven.

Almost all persons registered as brokers or dealers under Section 15(b) of the Exchange Act must be members of SIPC.[84] Because these requirements are imposed by statute, FINRA has no authority to exempt any CAB from SIPC membership.

Other Comments

Commenters had a number of other observations and recommendations regarding the proposed rule set, which FINRA addresses below.

One commenter recommended that FINRA relieve LCFBs from the requirement to review and file hard copies of employees' stock trading records.[85] Another commenter recommended that FINRA impose the requirements of NASD Rule 3050 on LCFBs.[86] NASD Rule 3050 imposes certain obligations on a member firm that knowingly executes a transaction for the purchase or sale of a security for the account of a person associated with another member firm, or any account over which such associated person has discretionary authority, and on an associated person who opens an account with another member firm. Among other things, upon written request by the employer member firm, the associated person must request that the executing member firm transmit duplicate account confirmations, statements or other information.

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84 See Section 3(a)(2)(A) of the Securities Investor Protection Act, 15 U.S.C. 78ccc(a)(2)(A). The only exceptions to this requirement are for: (i) firms whose principal business is conducted outside the United States, as determined by SIPC; (ii) firms whose business as a broker or dealer consists exclusively of (I) the distribution of open-end investment companies or unit investment trusts; (II) the sale of variable annuities; (III) the business of insurance; or (IV) advising investment companies or insurance company separate accounts; and (iii) firms that are registered as brokers or dealers solely for the purpose of trading security futures on an exchange.

85 See Colonnade.

86 See CFSC.

The CAB rules would not apply NASD Rule 3050 to CABs. FINRA believes that, due to the limited institutional activities of CABs and their associated persons, it is not necessary to impose this rule's obligations on CABs.

Three commenters urged FINRA to eliminate or reduce its assessments on LCFBs due to the limited level of FINRA oversight of these firms.[87] FINRA derives its revenues from a number of sources, many of which are user fees, such as fees imposed on firms that file communications with FINRA's Advertising Regulation Department, or public offerings with FINRA's Corporate Financing Department. CABs would not be subject to many of these user fees since they would not be subject to these filing requirements. However, CABs would be subject to fees and assessments that apply to all FINRA member firms, such as the gross income assessment or the new member filing fees. FINRA believes that it is appropriate to impose these more generalized assessments on CABs to cover the costs of regulating and examining CAB activities.

One commenter expressed concern that the proposed rule set will lead to differing interpretations of rules, and will create an uneven playing field with full-service broker-dealers. This commenter believes that the proposed rule set is contrary to FINRA's mission of market integrity and investor protection, and that FINRA and the industry would be better served by expanding existing rules rather than creating a new rule set.[88]

FINRA staff strives to interpret all of its rules in a consistent manner, and it will make similar efforts to interpret rules consistently if the proposal is approved. To the extent a CAB rule requires compliance with an existing FINRA rule that applies to full-

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[87] See Anderson, RWI, and LeGaye.

[88] See CFSC.

service broker-dealers, the staff anticipates that it will interpret the CAB rule in the same manner as the corresponding FINRA rule. If the CAB rule differs from its FINRA rule counterpart, the staff intends to interpret the rule consistently with respect to all CABs. FINRA does not agree that the proposed rule set would be contrary to FINRA's mission of market integrity and investor protection. FINRA has carefully crafted the rule set to include rules that should apply to all broker-dealers, or to broker-dealers that engage in M&A and other private equity activities with institutional investors, while excluding from the proposal rules that have no applicability to CABs' business model, or that would impose unnecessary burdens given the kinds of activities in which CABs engage.

One commenter suggested that the Federal Trade Commission Red Flag Rules should apply to LCFBs. This commenter noted that LCFBs may be in possession of confidential and sensitive information concerning their customers, and that these customers could be exposed to risks resulting from identity theft.[89] The proposal would not impact whether a CAB is subject to the Red Flag Rules adopted pursuant to the Fair Credit Reporting Act of 1970, as amended.[90] The application of the Red Flag Rules depends on whether a broker or dealer falls within the requirements of the SEC's Regulation S-ID.[91]

One commenter noted that the proposed rule set omits FINRA Rule 5150 (Fairness Opinions) and a reference to information barriers, such as the guidance provided in NASD Notice to Members 91-45 (July 1991). The commenter also

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89 See RWI.

90 Pub. L 91-508, 84 Stat. 1114 (1970), codified at 15 U.S.C. 1681-1681x.

91 17 CFR 248 Subpart C. See also Securities Exchange Act Release No. 69359 (April 10, 2013), 78 FR 23637 (April 19, 2013).

recommended that FINRA clarify that the proposed rule set would apply only to broker-dealers whose enterprise-wide activities fit within the definition of LCFB, and not to affiliates of large financial conglomerates, even if the LCFB itself only engages in activities permissible for an LCFB.[92]

FINRA agrees that FINRA Rule 5150 should apply to a CAB that provides a fairness opinion that is subject to that rule. Although this rule generally applies to fairness opinions that are provided or described to public shareholders, it is possible that a CAB could serve as an advisor in connection with a public offering of securities and provide a fairness opinion in connection with the offering. In such a case, it would make sense to require the same disclosures regarding potential conflicts of interest in connection with the fairness opinion. Accordingly, FINRA is adding new CAB Rule 515 (Fairness Opinions), which would subject CABs to FINRA Rule 5150.

NASD Notice to Members 91-45 was a joint memorandum prepared by the National Association of Securities Dealers, Inc., the New York Stock Exchange, and a committee of the Securities Industry Association that explained the minimum elements of adequate information barrier policies and procedures pursuant to the requirements of the Insider Trading and Securities Fraud Enforcement Act of 1988. To the extent a CAB deals with information that would trigger application of this statute or any other insider trading law, the CAB would be required to have in place adequate information barriers necessary to meet these requirements.

FINRA disagrees that a CAB may not be affiliated with a broker-dealer that engages in activities that are not permitted for CABs. As discussed previously, the CAB

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92 See Washington U.

rules would prohibit both a CAB firm and its associated persons from engaging in activities that are not permitted under the definition of CAB. However, FINRA does not believe that it would be inconsistent for an affiliate of a CAB to engage in a wider array of activities; in those cases, the affiliate would be subject to all FINRA rules, and not the CAB rules.

One commenter urged FINRA to collaborate with the North American Securities Administrators Association ("NASAA") to further reduce regulatory burdens on LCFBs.[93] FINRA cooperates with NASAA representatives on securities regulatory issues, and expects that its staff will continue to discuss matters of mutual interest regarding CABs with NASAA representatives in the future.

Another commenter requested that FINRA confirm that LCFBs may serve as "chaperones" for non-U.S. broker-dealers under Exchange Act Rule 15a-6 by performing activities that are described in Rule 15a-6(a)(3) and related no-action letters. The same commenter recommended that FINRA confirm with the states that an LCFB would be eligible for an exemption from state business broker licensing laws, to the extent that they exempt other registered broker-dealers.[94]

FINRA is not prepared at this time to confirm that all activities listed in Rule 15a-6(a)(3) and related no-action letters would be permissible for a CAB. For example, these activities include effecting securities transactions and issuing all required confirmations and statements, which appear to be activities beyond what would be permitted under the

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93 See M&A Brokers Letter Attorneys.

94 See EYCF.

CAB definition. Likewise, the question of whether a CAB would be subject to a particular state's business broker licensing laws would be better directed to that state.

Another commenter recommended that FINRA work with the SEC, NASAA, the Commodity Futures Trading Commission, the National Futures Association, and the industry to develop a unified simple regulatory approach to regulating broker-dealer activities on the basis of risk rather than on transaction-based compensation.[95] The commenter's suggestion is beyond the scope of this proposed rulemaking and would likely require changes to the federal securities laws.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

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[95] See IMS.

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2015-054 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Robert W. Errett, Deputy Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2015-054. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2015-054 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[96]

Robert W. Errett
Deputy Secretary

96 17 CFR 200.30-3(a)(12).

Exhibit 2a

Regulatory Notice 14-09

February 2014

Notice Type

- Request for Comment

Suggested Routing

- Compliance
- Legal
- Senior Management

Key Topics

- Corporate Restructuring
- Limited Corporate Financing Brokers
- Mergers & Acquisitions
- Private Equity Funds

Referenced Rules & Notices

- FINRA Rule 1000 Series
- FINRA Rule 2000 Series
- FINRA Rule 3000 Series
- FINRA Rule 4000 Series
- FINRA Rule 5122
- FINRA Rule 8000 Series
- FINRA Rule 9000 Series
- FINRA Rule 10000 Series
- FINRA Rule 12000 Series
- FINRA Rule 13000 Series
- FINRA Rule 14000 Series
- NASD Rule 1000 Series
- NASD Rule 2000 Series
- NASD Rule 3170

Limited Corporate Financing Brokers

FINRA Requests Comment on a Proposed Rule Set for Limited Corporate Financing Brokers

Comment Period Expires: April 28, 2014

Executive Summary

FINRA is soliciting public comment on a proposed rule set for firms that meet the definition of "limited corporate financing broker" (LCFB). An LCFB is a firm that engages in a limited range of activities, essentially advising companies and private equity funds on capital raising and corporate restructuring. The rule set would not apply to firms that carry or maintain customer accounts, handle customers' funds or securities, accept customers' trading orders, or engage in proprietary trading or market-making.

The proposed rules are available as Attachment A at ____________

Notice should be directed to Joseph P. Savage, Vice President and Counsel, Regulatory Policy, at (240) 386-4534.

Action Requested

FINRA encourages all interested parties to comment on the proposed rule set. Comments must be received by April 28, 2014.

Comments must be submitted through one of the following methods:

- Emailing comments to ____________
- Mailing comments in hard copy to:

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

Financial Industry Regulatory Authority

To help FINRA process comments more efficiently, persons should use only one method to comment on the proposed rule set.

Important Notes: All comments received in response to this *Notice* will be made available to the public on the FINRA website. In general, comments will be posted as they are received.[1]

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the FINRA Board of Governors, and then must be filed with the SEC pursuant to Section 19(b) of the Securities Exchange Act of 1934 (SEA or Exchange Act).[2]

Background & Discussion

Some FINRA-regulated firms are solely corporate financing firms that advise companies on mergers and acquisitions, advise issuers on raising debt and equity capital in private placements with institutional investors, or provide advisory services on a consulting basis to companies that need assistance analyzing their strategic and financial alternatives. These firms often are registered as broker-dealers because they may receive transaction-based compensation as part of their services.

Nevertheless, these firms do not engage in many of the types of activities typically associated with traditional broker-dealers. For example, these firms do not maintain customer accounts, handle customer funds or securities, accept orders to purchase or sell securities either as principal or agent for the customer, exercise investment discretion on behalf of any customer, or engage in proprietary trading of securities or market-making activities.

FINRA is proposing to establish a separate rule set that would apply exclusively to firms that meet the definition of limited corporate financing broker. An LCFB would be subject to the FINRA By-Laws, as well as core FINRA rules that FINRA believes should apply to all firms. The rule set would include other FINRA rules that are tailored to address an LCFB's business activities.

General Standards (LCFB Rule 010 Series)

Proposed LCFB Rule 014 provides that an LCFB and persons associated with an LCFB will be subject to the FINRA By-Laws (including the schedules thereto), unless the context requires otherwise, and the Limited Corporate Financing Broker Rules. Proposed LCFB Rule 015 provides that the LCFB Rules do not apply to transactions in, and business activities relating to, municipal securities as that term is defined in the Exchange Act.

LCFB Rule 016 sets forth basic definitions modified as appropriate to apply to an LCFB. The proposed definitions of "limited corporate financing broker" is particularly important to the application of the rule set.

The term "limited corporate financing broker" would include any broker that solely engages in one or more of the following activities:

- advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions; and
- qualifying, identifying or soliciting potential institutional investors.[3]

A firm would be permitted to register as, or change its status to, an LCFB only if the firm solely engages in one or more of these activities.

The term limited corporate financing broker would not include any broker or dealer that:

- carries or maintains customer accounts;
- holds or handles customers' funds or securities;
- accepts orders from customers to purchase or sell securities either as principal or as agent for the customer;
- possesses investment discretion on behalf of any customer; or
- engages in proprietary trading of securities or market-making activities.[4]

Member Application and Associated Person Registration (LCFB Rule 100 Series)

The proposed LCFB Rule 100 series sets forth the requirements for firms that wish to register as an LCFB. The proposed LCFB Rule 100 series generally incorporates by reference FINRA Rules 1010 (Electronic Filing Requirements for Uniform Forms), 1122 (Filing of Misleading Information as to Membership or Registration), and 1230(b)(6) (Operations Professional), and NASD Rules 1011 (Definitions), 1012 (General Provisions), 1013 (New Member Application and Review), 1014 (Department Decision), 1015 (Review by National Adjudicatory Council), 1016 (Discretionary Review by FINRA Board), 1017 (Application for Approval of Change in Ownership, Control, or Business Operations), 1019 (Application to Commission for Review), 1090 (Foreign Members), 1100 (Foreign Associates) and IM-1011-1 (Safe Harbor for Business Expansions). Accordingly, an LCFB applicant would follow the same procedures for membership as any other FINRA applicant, with four modifications.

- First, an applicant for membership that seeks to qualify as an LCFB would have to state in its application that it intends to operate as such.

- Second, in reviewing an application for membership as an LCFB, the FINRA Member Regulation Department would consider, in addition to the standards for admission set forth in NASD Rule 1014, whether the applicant's proposed activities are consistent with the limitations imposed on an LCFB under LCFB Rule 016(g).
- Third, proposed LCFB Rule 116(b) sets forth the procedures for an existing FINRA firm to change its status to an LCFB. If an existing firm is already approved to engage in the activities of an LCFB, and the firm does not intend to change its existing ownership, control or business operations, it would not be required to file either a New Member Application (NMA) or a Change in Membership Application (CMA). Instead, such a firm would be required to file a request to amend its membership agreement or obtain a membership agreement (if none exists currently) to provide that: (i) the firm's activities will be limited to those permitted for an LCFB under LCFB Rule 016(g), and (ii) the firm agrees to comply with the LCFB Rules.[5]

  Fourth, proposed LCFB Rule 116(c) sets forth the procedures for an existing LCFB to terminate its status as such and continue as a FINRA firm. Such a firm would be required to file a CMA with the FINRA Member Regulation Department, and to amend its membership agreement to provide that the firm agrees to comply with all FINRA Rules.[6]

The proposed LCFB Rule 100 series also would govern the registration and qualification examinations of principals and representatives that are associated with an LCFB. These rules incorporate by reference NASD Rules 1021 (Registration Requirements – Principals), 1031 (Registration Requirements – Representatives), 1060 (Persons Exempt from Registration), 1070 (Qualification Examinations and Waiver of Requirements), and 1080 (Confidentiality of Examinations), and FINRA Rule 1230(b)(6) (Operations Professional). Accordingly, LCFB firm principals and representatives would be subject to the same registration and qualification examination requirements as principals and representatives of other FINRA firms.

However, LCFB firm principals and representatives would be eligible for fewer registration categories.[7] LCFB principals would be eligible to register as a general securities principal (Series 24), limited principal – financial and operations (Series 27), limited principal – introducing broker/dealer financial and operations (Series 28), and limited principal – general securities sales supervisor (Series 9 and 10). LCFB associated persons would be eligible to register as a general securities representative (Series 7), limited representative – corporate securities (Series 62), limited representative – private securities offerings (Series 82), limited representative – investment banking (Series 79) and operations professional (Series 99).

Proposed LCFB Rule 125 would subject an LCFB to continuing education requirements that are more streamlined than those imposed on other firms under FINRA Rule 1250. Proposed LCFB Rule 125 would not impose any Regulatory Element continuing education requirements on an LCFB, but would impose Firm Element requirements. The Firm Element requirements would apply to any person registered with an LCFB who has direct contact with customers in the conduct of the firm's corporate financing activities, and to their immediate supervisors.

The proposed rule would require an LCFB to establish and implement Firm Element programs that are appropriate for the LCFB's business, to administer the program in accordance with its annual evaluation and written plan, and to maintain records documenting the program's content and completion by covered persons. The rule would require covered persons to take all appropriate and reasonable steps to participate in continuing education programs required by their firms. The rule also would authorize FINRA to require an LCFB to provide special training to its covered persons in such areas as FINRA deems appropriate.

Duties and Conflicts (LCFB Rule 200 Series)

The proposed LCFB Rule 200 series would establish a streamlined set of conduct rules. An LCFB would be subject to FINRA Rules 2010 (Standards of Commercial Honor and Principles of Trade), 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices), 2070 (Transactions Involving FINRA Employees), 2080 (Obtaining an Order of Expungement of Customer Dispute Information from the CRD System), 2263 (Arbitration Disclosure to Associated Persons Signing or Acknowledging Form U4), and 2268 (Requirements When Using Predispute Arbitration Agreements for Customer Accounts), and NASD Rule 2420 (Dealing with Non-Members) and IM-2420-1 (Transactions Between Members and Non-Members).

LCFB Rules 209 and 211 would impose more streamlined know-your-customer and suitability obligations than are imposed under FINRA Rules 2090 and 2111.

Proposed LCFB Rule 221 is an abbreviated version of FINRA Rule 2210 (Communications with the Public), essentially prohibiting false and misleading statements.

Under proposed LCFB Rule 240, if an LCFB or associated person of an LCFB had engaged in activities that would require the LCFB to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on an LCFB under LCFB Rule 016(g), FINRA could examine for and enforce all FINRA rules against the broker or associated person, including any rule that applies to a FINRA broker-dealer that is not an LCFB or to an associated person who is not associated with an LCFB.

Supervision and Responsibilities Related to Associated Persons (LCFB Rule 300 Series)

The proposed LCFB Rule 300 series would establish a limited set of supervisory rules for an LCFB. An LCFB would be subject to FINRA Rules 3220 (Influencing or Rewarding Employees of Others), 324 (Borrowing from or Lending to Customers), and 327 (Outside Business Activities of Registered Persons).

Proposed LCFB Rule 311 would subject an LCFB to some, but not all, of the requirements of FINRA Rule 3110 (Supervision) and, consistent with Rule 3110, is designed to permit an LCFB flexibility to tailor its supervisory systems to its business models. An LCFB would be subject to many of the provisions of Rule 3110 concerning the supervision of offices, personnel, customer complaints, correspondence and internal communications. However, an LCFB would not be subject to the provisions of Rule 3110 that require annual compliance meetings (paragraph (a)(7)), review and investigation of transactions (paragraphs (b)(2) and (d)), specific documentation and supervision procedures for supervisory personnel (paragraph (b)(6)), and internal inspections (paragraph (c)).

Proposed LCFB Rule 313 would require an LCFB to designate and identify one or more principals to serve as a firm's chief compliance officer.

Proposed LCFB Rule 331 would require each LCFB to implement a written anti-money laundering (AML) program. This is consistent with the SEC's requirements and Chapter X of Title 31 of the Code of Federal Regulations. Accordingly, the proposed rule is similar to FINRA Rule 3310 (Anti-Money Laundering Compliance Programs); however, the proposed rule contemplates that an LCFB would be eligible to conduct the required independent testing for compliance every two years.

Financial and Operational Rules (LCFB Rule 400 Series)

The proposed LCFB Rule 400 series would establish a streamlined set of rules concerning firms' financial and operational obligations. An LCFB would be subject to FINRA Rules 4140 (Audit), 4150 (Guarantees by, or Flow through Benefits for, Members), 4160 (Verification of Assets), 4360 (Fidelity Bonds), 4511 (Books and Records – General Requirements), 4513 (Records of Written Customer Complaints), 4530 (Reporting Requirements), and 4570 (Custodian of Books and Records), and NASD Rules 1150 (Executive Representative), 1160 (Contact Information Requirements) and 3170 (Mandatory Electronic Filing Requirements).

Proposed LCFB Rule 411 includes some, but not all, of the capital compliance requirements of FINRA Rule 4110. An LCFB would be required to suspend business operations during any period a firm is not in compliance with the applicable net capital requirements set forth in SEA Rule 15c3-1, and the rule also would authorize FINRA to direct an LCFB to suspend its operation under those circumstances. Proposed LCFB Rule 411 also sets forth requirements concerning withdrawal of capital, subordinated loans, notes collateralized by securities and capital borrowings.

Because an LCFB would not carry or maintain customer accounts, it would have more limited customer information requirements than is imposed under FINRA Rule 4512.[8] Each LCFB would have to maintain each customer's name and residence, whether the customer is of legal age (if applicable), and the names of any persons authorized to transact business of the customer. An LCFB would still have to maintain all records required under SEA Rules 17a-3 and 17a-4.

Proposed LCFB Rule 452 establishes a limited set of requirements for the supervision and review of a firm's general ledger accounts.

Investigations and Sanctions, Code of Procedure, and Arbitration and Mediation (LCFB Rules 800, 900 and 1000)

Each LCFB would be subject to the FINRA Rule 8000 series governing investigations and sanctions of firms, other than FINRA Rules 8110 (Availability of Manual to Customers), 8211 (Automated Submission of Trading Data Requested by FINRA), and 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA).

An LCFB would be subject to the FINRA Rule 9000 series governing disciplinary and other proceedings involving firms, other than the FINRA Rule 9700 series (Procedures on Grievances Concerning the Automated Systems). Proposed LCFB Rule 900(c) would provide that any LCFB may be subject to a fine under FINRA Rule 9216(b) with respect to an enumerated list of FINRA By-Laws, LCFB Rules and SEC Rules under the Exchange Act. Proposed LCFB Rule 900(d) would authorize FINRA staff to require an LCFB to file communications with the FINRA Advertising Regulation Department at least ten days prior to use if the staff determined that the LCFB had departed from LCFB Rule 221's standards.

An LCFB would be subject to the FINRA Rule 10000 series (Code of Arbitration Procedure), 12000 series (Code of Arbitration Procedure for Customer Disputes), 13000 (Code of Arbitration Procedure for Industry Disputes) and 14000 series (Code of Mediation Procedure).

Request for Comment

FINRA requests comment on all aspects of the proposed rules, including any impact on institutional customers and issuers, potential costs and burdens that the proposal could impose on an LCFB, and any cost savings and reduced burdens that the proposal would create for an LCFB. FINRA also requests comment on whether an LCFB should be subject to any FINRA Rules that are not included in the proposed rule set.

FINRA particularly requests comment concerning the following issues:

- Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?
- Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?
- Is the definition of "limited corporate financing broker" appropriate? Are there any activities in which broker-dealers with limited corporate financing functions typically engage that are not included in the definition? Are there activities that should be added to the list of activities in which an LCFB may not engage?
- Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?
- What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?
- FINRA welcomes estimates of the number of firms that would be eligible for the proposed rule set.
- Proposed LCFB Rule 123 would limit the principal and representative registration categories that would be available for persons associated with an LCFB. Are there any registration categories that should be added to the rule? Are there any registration categories that are currently included in the proposed rule but that are unnecessary for persons associated with an LCFB?
- Should principals and representatives that hold registration categories not included within LCFB Rule 123 be permitted to retain these registrations?
- Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?
- Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014,[9] impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?

Endnotes

1. FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. *See Notice to Members 03-73* (November 2003) (NASD Announces Online Availability of Comments) for more information.

2. *See* SEA Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the Federal Register. Certain limited types of proposed rule changes, however, take effect upon filing with the SEC. *See* SEA Section 19(b)(3) and SEA Rule 19b-4.

3. *See* proposed LCFB Rule 016(g)(1). An LCFB would not be permitted to qualify, identify or solicit potential purchasers of securities unless the purchaser meets the definition of "institutional investor." However, an LCFB would be allowed to serve clients (such as individuals or entities seeking advice on securities offerings or sales of businesses) who do not meet the "institutional investor" definition.

   The term "institutional investor" would have the same meaning as that term has under FINRA Rule 2210 (Communications with the Public). The term would include any:

   - bank, savings and loan association, insurance company or registered investment company;
   - governmental entity or subdivision thereof;
   - employee benefit plan, or multiple employee benefit plans offered to employees of the same employer, that meet the requirements of Section 403(b) or Section 457 of the Internal Revenue Code and in the aggregate have at least 100 participants, but does not include any participant of such plans;
   - qualified plan, as defined in Section 3(a)(12)(C) of the Exchange Act, or multiple qualified plans offered to employees of the same employer, that in the aggregate have at least 100 participants, but does not include any participant of such plans;
   - other person (whether a natural person, corporation, partnership, trust, family office or otherwise) with total assets of at least $50 million; and
   - any person acting solely on behalf of any such institutional investor.

   See proposed LCFB Rule 016(f).

   FINRA purposely does not propose to define "institutional investor" based on a more inclusive standard, such as the definition of "accredited investor" in Regulation D under the Securities Act of 1933. *See* 17 C.F.R. § 230.501(a). The LCFB Rules are intended to govern the activities of firms that engage in a limited range of activities, such as advising companies and private equity funds on capital raising and corporate restructuring. As part of these activities, an LCFB would be permitted to qualify, identify and solicit potential institutional investors, as defined by the LCFB Rules.

   FINRA's regulatory programs have uncovered serious concerns with the manner in which firms market and sell private placements to accredited investors. Application of the LCFB Rules to firms that market and sell private placements to accredited investors would require FINRA to expand the applicable conduct rules and other provisions. Therefore, lowering the threshold of "institutional investor" would eviscerate the benefits of a streamlined rule set.

4. *See* proposed LCFB Rule 016(g)(2).
5. There would not be an application fee associated with this request.
6. Absent a waiver, such a firm would have to pay an application fee associated with the CMA. *See* FINRA By-Laws, Schedule A, Section 4(i).
7. *See* proposed LCFB Rule 123.
8. *See* proposed LCFB Rule 451(b).
9. *See Faith Colish, Esq., Carter Ledyard & Milburn LLP, et al.*, SEC no-action letter (Jan. 31, 2014).

EXHIBIT 2b

Alphabetical List of Written Comments
Regulatory Notice 14-09

1. John Ahern, Compass Securities Corporation (April 28, 2014) *
2. Rick Alvarez, CPA, Capital Markets Compliance ("CMC") (April 25, 2014)
3. James W. Carter, Ernst & Young Capital Advisors, LLC ("EYCA") (April 28, 2014)
4. Faith Colish, Esq., Martin A. Hewitt, Esq., Eden L. Rohrer, Esq., Linda Lerner, Esq., Ethan L. Silver, Esq., and Stacy E. Nathanson, Esq., ("M&A Brokers Letter Attorneys") (April 28, 2014)
5. Donna DiMaria, Tessera Capital Partners (April 28, 2014) *
6. Donna DiMaria, Third Party Marketers Association ("3PM") (April 28, 2014)
7. Catherine T. Dixon, Committee on Federal Regulation of Securities, Business Law Section of the American Bar Association ("ABA") (May 21, 2014)
8. Richard B. Dole, ASA, CFA, Dole Capital, LLC ("Dole") (April 25, 2014)
9. Leanne Erickson, Eaton Partners, LLC (April 28, 2014) *
10. Brian X. Fitzgibbon, Fitzgibbon Toigo Associates, LLC (April 28, 2014) *
11. Weldon G. Fleming, Jr., LIATI Capital, LLC ("LIATI") (April 18, 2014)
12. Saverio Flemma, SF Advisors, LLC ("SFA") (April 23, 2014)
13. Eli Gabay, Growth Venture Partners ("Growth Venture") (March 12, 2014)
14. Stephen A. Gaines and Dennis W. O'Neill, HighBank Securities, LLC ("HighBank") (April 28, 2014)
15. Stacy Havener, Havener Capital Partners LLC (April 28, 2014) *
16. Chester Hebert, Colorado Financial Service Corporation ("CFSC") (March 21, 2014)
17. Tony Ianni, Ernst & Young Corporate Finance (Canada) Inc. ("EYCF") (April 25, 2014)
18. Steven Jafarzadeh, CAIA, CRCP, Stonehaven, LLC ("Stonehaven") (April 28, 2014)
19. Antoine C. Kemper, Jr., Butler Capital Partners (April 28, 2014) *

20. Tom Korzenecki, Grand Avenue Capital Partners LLC ("GAPC") (March 6, 2014)
21. Tiffany Lauterbach, CSP Securities, LP ("CSP") (April 28, 2014)
22. Daniel E. LeGaye, The LeGaye Law Firm, P.C. ("LeGaye") (April 28, 2014)
23. Gregory M. LeNeave, Anderson LeNeave & Co. ("Anderson") (March 12, 2014)
24. Joseph M. Lydon, Goal Consulting LLC (April 28, 2014) *
25. Keith McCracken, McCracken Advisory Partners ("McCracken") (April 28, 2014)
26. Robert G. McGroarty, Bridge 1 Advisors ("Bridge 1") (April 23, 2014)
27. Roger W. Mehle, Achates Capital Advisors LLC ("Archates") (March 5, 2014)
28. John Stuart Miller, Colonnade Securities LLC ("Colonnade") (March 6, 2014)
29. Frank P. L. Minard, XT Capital Partners, LLC (April 28, 2014) *
30. Robert A. Muh, Sutter Securities Incorporated ("Sutter") (April 1, 2014)
31. Richard A. Murphy, North Bridge Capital LLC (April 28, 2014) *
32. Ron Oldenkamp, Genesis Marketing Group (April 28, 2014) *
33. Robert E. Patterson, Signal Hill Capital Group LLC ("Signal Hill") (March 20, 2014)
34. Peter Pavlina, Hamersley Partners (April 28, 2014) *
35. Gilman C. Perkins, Perkins Fund Marketing (April 28, 2014) *
36. Andrew Phillips, Hamersley Partners (April 28, 2014) *
37. Paige W. Pierce, RW Smith & Associates, Inc. (April 28, 2014) *
38. Paul Poggi and Andrew D. Tino, Harris Williams & Co. ("Harris") (April 28, 2014)
39. Sandra Powers, ARK Global LLC (April 28, 2014) *
40. David N. Pringle, Fells Point Research LLC ("Fells") (April 28, 2014)
41. Steven Rubenstein, Arrow Investments, Inc. (April 28, 2014) *
42. Michael S. Quinn, Q Advisors ("Q Advisors") (April 25, 2014)

43. Lisa Roth, Monahan & Roth, LLC (April 28, 2014) *
44. Howard Spindel and Cassondra E. Joseph, Integrated Management Solutions USA LLC ("IMS") (April 28, 2014)
45. Lou Stough, CFE, AIW, LLC ("AIW") (April 2, 2014)
46. Kenneth Sweet, Reliance Worldwide Investments, LLC ("RWI") (April 25, 2014)
47. James L. Tovey, JLT Capital Partners LLC (April 28, 2014) *
48. Andrew F. Tuch, Washington University School of Law ("Washington U.") (April 28, 2014)
49. George Vick, Frontier Solutions, LLC (April 28, 2014) *
50. Bruce A. Williamson, CFA, Fortress Group, Inc. (April 28, 2014) *
51. Michael Wren, Hamersley Partners (April 28, 2014) *

* These commenters wrote a short email or letter supporting 3PM's comments.

Dear Ms. Asquith,

My firm is a FINRA member specializing in raising capital for private investments (we do not engage in investment banking) that are both traditional and alternative in nature. Our focus is marketing to institutional investors. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCFB) —see attached. I urge FINRA's board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Given that more work needs to be done, I especially support the need for flexibility in introducing the LCFB program as it relates to cost, time and the registration process/re-registration process. I also feel that the understanding/definition of the term "customer" is critical going forward when it comes to a firm like ours, which has no accounts or customers as regulators refer to such.

I appreciate all the attention that you give to this matter—thank you.

John Ahern
President
Compass Securities Corporation
50 Braintree Hill Office Park, Ste. 105
Braintree, MA 02184
Email: john@compasssecurities.com

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April 25, 2014

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

Re: Comment on LCFB rule set regarding Net Capital Compliance

Ms. Asquith,

Regarding net capital compliance for Limited Corporate Financing Broker (LCFB), we request for FINRA to consider a modification to the Aggregate Indebtedness (AI) Standard ratio requirement. Currently, the AI ratio requirement increases a member firm's minimum net capital requirement (MNCR) as a result of a member firm's aggregate current liabilities (liabilities due within 12 months). Most member firms who will qualify as a LCFB will have a $5,000 MNCR which will increase from time-to-time as a result of the LCFB's aggregate liabilities.

The most common current liability that causes a member firm's MNCR to increase above $5,000 is commissions or concession payable to sales representatives as a result of a receivable from an investment banking transaction that closes, but the receivable has not been collected. In most cases this receivable is collected between 2 to 5 days from the day of closing and the payable to the representative is paid shortly after it has been received. Most member firms that will qualify as a LCFB actually don't have an obligation to pay the commissions or concession payable until the revenue is received because they have written agreements with the sale representatives that waives the sales representative's right to receive payment of the commission or the concession until the member firm has received payment. However, according to GAAP, the commission or concession payable is required to be booked at the same time the commission or concession receivable is booked regardless of the agreement in place. Because of the manner in which the Aggregate Indebtedness Standard (AI) ratio requirement is currently written and applied, this liability increases the member firm's MNCR. Below is an example of how the AI standard affects a member firm's MNCR:

A member firm has executed agreements with all sales representatives that waive their right to receive any payment from the member firm until such time that the member firm receives the payment due from the issuer in cleared funds. The same member firm closes an investment banking transaction on December 31, 2013, which yields a

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commission or concession receivable of $1,000,000 and has an agreement to pay a commission or concession payable to the sales representatives of $900,000.

According to GAAP, the member firm must book the commissions or concession payable to the registered representative at the same time it books the receivable even though the member firm does not have an obligation to pay it until the free and clear funds are received by the member firm. As a result, the AI standard ratio requirement causes the member firm's MNCR to increase to almost $60,000 and its early warning net capital requirement to approx $72,000. This increase is temporary until it receives the cash and pays the commission; however, the member firm must maintain the $72,000+ in order to comply with the moment-to-moment net capital requirement.

Since the proposed LCFB will not be carrying or maintaining customer funds, then the AI standard should be modified to exclude from AI short term commission or concession payable liabilities that obligate the member firm to have a higher MNCR.

Sincerely,

Rick Alvarez, CPA
CFO & Controller

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April 28, 2014

BY E-MAIL (pubcom@finra.org)

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

Re: Proposed Rule Set for Limited Corporate Financing Brokers

Dear Ms. Asquith:

We appreciate this opportunity to comment on the proposed rule set for limited corporate finance brokers ("LCFBs") described in Financial Industry Regulatory Authority ("FINRA") Regulatory Notice 14-09 (the "LCFB Rules"). Ernst & Young Capital Advisors, LLC ("EYCA") is a broker-dealer registered with the U.S. Securities and Exchange Commission ("SEC") and has been a member of FINRA since 2010. EYCA is also registered in fifty-three U.S. states and territories. EYCA's primary business activities consist of (1) advising public and private institutional clients regarding mergers and acquisitions, corporate restructuring, and capital raising activities, including securities offerings and debt refinancing, and (2) identifying and soliciting investors in private placements.

We commend FINRA for proposing that broker-dealers like EYCA be subject to a limited rule set in lieu of the full panoply of FINRA rules to which they currently are subject. The LCFB Rules, for instance, include streamlined requirements regarding communications with the public, supervision, and continuing education that are appropriate for broker-dealers that do not handle customer funds or securities or communicate with or execute trades for retail customers. For such broker-dealers, the LCFB Rules provide welcome relief from requirements that are unnecessary and costly. Although EYCA has not yet determined whether it would opt for registration as an LCFB if the LCFB Rules were adopted, we submit this letter to highlight two modifications to, or clarifications of, the LCFB Rules that, if adopted, would enhance the potential utility of the LCFB registration category for EYCA and similarly situated member firms. In particular, we believe FINRA should (1) permit LCFBs to solicit institutional accredited investors when participating in the private placement of securities, and (2) permit LCFBs to maintain licenses that are not referenced in LCFB Rule 123 for representatives and principals.

I. Soliciting Institutional Accredited Investors

Under LCFB Rule 016(h)(1), only broker-dealers that qualify, identify, or solicit "institutional investors" as defined in LCFB Rule 016(g) would be eligible to register as LCFBs. As FINRA acknowledged in Regulatory Notice 14-09, the definition of "institutional investor" in LCFB Rule 016(g) is more restrictive than the definition of "accredited investor" in Regulation D under the

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Securities Act of 1933. For instance, and most significantly from EYCA's perspective, whereas broker-dealers that participate in private placements pursuant to Rule 506 of Regulation D are currently permitted to solicit institutions with total assets in excess of $5,000,000, LCFBs generally would be prohibited under LCFB Rules from soliciting institutions with total assets of less than $50,000,000 (unless they fell into one of only a few categories of entities enumerated in the LCFB Rules, such as banks or registered investment companies). Thus, broker-dealers that otherwise would be eligible to register as LCFBs would be prohibited from doing so if they solicited institutions with total assets of between $5,000,000 and $50,000,000. We urge FINRA to permit broker-dealers that solicit such institutions to register as LCFBs.

FINRA justifies this gap in LCFB eligibility by noting that "[a]pplication of the LCFB Rules to firms that market and sell private placements to accredited investors would require FINRA to expand the applicable conduct rules and other provisions."[1] It is not clear which requirements FINRA has in mind, particularly if the accredited investors in question are institutions.[2] Moreover, the overriding differences between potential LCFBs and broker-dealers ineligible for registration as LCFBs is – and so the key consideration when determining whether existing FINRA rules should [illegible]

[illegible]

[1] FINRA Regulatory Notice 14-09, note 3.

[2] For instance, if, as a consequence of permitting LCFBs to solicit accredited investors, FINRA elected to incorporate into the LCFB Rules FINRA Rule 5123 (Private Placements of Securities), which imposes a filing requirement on broker-dealers that sell securities in private placements, doing so would have no effect on LCFBs that solicit *institutional* accredited investors because broker-dealers that solicit such investors are exempt from the requirements of the rule. FINRA Rule 5123(b)(1)(J) exempts offerings sold to accredited investors described in Securities Act Rule 501(a)(1), (2), (3), or (7) – *i.e.*, institutional accredited investors.

[3] SEC Securities Act Release No. 6683 (Jan. 16, 1987) (proposing, among other things, to include corporations and partnerships with total assets in excess of $5,000,000 within the scope of the definition of "accredited investors" for purposes of Regulation D).

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II. Maintaining Registration Licenses Not Referenced in Rule Set

LCFB representatives and principals should be permitted to retain licenses that are not referenced in LCFB Rule 123. As discussed below, the potentially transient nature of the LCFB registration category may cause representatives and principals of an LCFB to become associated with a non-LCFB broker-dealer within a short period of time. Consequently, representatives and principals may hesitate to associate with an LCFB unless they are permitted to retain licenses that are not referenced in LCFB Rule 123.

Several aspects of the LCFB registration category could dissuade representatives and principals from associating with an LCFB unless they are permitted to retain non-required registrations. First, under LCFB Rule 240, FINRA may require an LCFB to register as a non-LCFB broker-dealer if FINRA determines that the LCFB "has engaged in activities that require the firm to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on limited corporate financing brokers under Limited Corporate Financing Rule 016(h)." Second, under LCFB Rule 116(c), an LCFB may become a non-LCFB broker-dealer by filing an application for approval of a material change in business operations and amending its FINRA membership agreement. In each of the above scenarios, an LCFB representative or principal who relinquished a registration in order to associate with the LCFB may find that he or she needs that registration in order to associate with a non-LCFB broker-dealer.

We urge FINRA to permit principals and representatives associated with LCFBs to retain licenses that are not referenced in LCFB Rule 123. Specifically, LCFB Rule [illegible] should permit LCFBs to maintain a registration for a representative or principal so long as the representative or principal is active in the broker-dealer's "investment banking or securities business" as a representative or principal, respectively. For instance, an LCFB should be permitted to maintain a Series 22 license (Limited Representative—Direct Participation Programs) for a representative who actively sells corporate securities on behalf of the LCFB pursuant to the representative's Series 62 license (Limited Representative—Corporate Securities).[4]

We appreciate this opportunity to comment on the proposed LCFB Rules. Please do not hesitate to contact me at [illegible] if you would like to discuss any of the topics addressed in this letter or any other aspect of the proposal.

Sincerely,

James W. Carter
Chief Executive Officer

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[4] We note in this regard that FINRA's proposed Rule 1210 would permit FINRA members to maintain a non-required registration for a representative or principal "provided that such person is engaged in a bona fide business purpose of the member." FINRA Regulatory Notice 09-70.

Faith Colish, Carter Ledyard & Milburn LLP
Martin A. Hewitt, Attorney at Law
Eden L. Rohrer, Crowell & Moring LLP
Linda Lerner, Crowell & Moring LLP
Ethan L. Silver, Carter Ledyard & Milburn LLP
Stacy E. Nathanson, Attorney at Law

April 28, 2014

Via email to: pubcom@finra.org

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

Re: FINRA's Regulatory Notice 14-09 Request for Comment
Proposed Limited Corporate Financing Broker Rules

Dear Ms. Asquith:

This comment letter is submitted on behalf of the six lawyers who authored the recent request to the SEC with respect to M&A Brokers, which relief was granted by the staff in a No-Action Letter made publicly available on January 31, 2014 and amended February 4, 2014 (the "M&A Brokers Letter"). We submit this comment letter with respect to FINRA's proposed rule set for firms that meet the definition of "limited corporate financing broker" ("LCFB") (the "LCFB Rule Proposal").[1]

As proposed by FINRA, an LCFB is a firm that engages in a limited range of activities, essentially advising companies and private equity funds on capital raising and corporate restructuring, and "soliciting" investments from "institutional investors." We applaud FINRA in recognizing the rationale proposed by the ABA Task Force for Private Placement Brokers (the "Task Force") and enunciated in its 2005 report (the "2005 Task Force Report") calling for a broker-dealer limited category of registration. However, we do not believe that the language in the LCFB Rule Proposal is clear enough, nor as proposed, goes far enough to limit the costs and other additional burdens to which these types of limited broker-dealers are currently subject.

FINRA has specifically sought comment as to whether the M&A Brokers Letter impacts the analysis of whether a firm would become an LCFB and whether it is likely that some limited corporate financing firms (a) will not register as a broker consistent with the fact pattern set forth in the M&A Brokers Letter, or (b) will become FINRA members and qualify as an LCFB. There is no reason under the M&A Brokers Letter for persons acting within its parameters to be regulated as an LCFB or register as any other type of broker. The SEC has effectively carved

[1] See Limited Corporate Financing Brokers at FINRA Regulatory Notice 14-09 (February 2014), available at http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p449586.pdf

out this category of brokers from all registration requirements, provided they abide by the parameters set forth in the M&A Brokers Letter. Because M&A brokers are not required to register with the SEC, they are ineligible for membership with FINRA and cannot be required to be regulated as LCFBs. Only M&A brokers who wish to conduct activities outside the four corners of the M&A Brokers Letter (i.e., participating in capital raising activities) will be eligible for membership as an LCFB or some other broker category.

We have not addressed each of your requests for comments, but rather wish to point out our key concerns.

First, FINRA's explanation of what an LCFB can and cannot do is ambiguous and needs to be stated more clearly. As described in the proposal and more thoroughly below, an LCFB can solicit institutional investors.[2] Nevertheless, proposed Rule 016(h)(2) states that the term LCFB does not include a broker-dealer that "accepts orders from customers to purchase or sell securities…as agent for the customer…." If by permitting solicitation but not the acceptance of orders FINRA means that an LCFB may engage in effecting transactions but that final acceptance of orders is within the sole control of the issuer, and that the LCFB cannot bind the issuer to a sale, that point should be more clearly stated. In other words, FINRA needs to make explicit that an LCFB can engage in capital raising in private placements, so long as the customer is at least an institutional investor (or as we propose below, qualified purchaser), and that the prohibition against an LCFB from accepting customer orders to purchase or sell securities, even as agent, was not intended by FINRA to limit an LCFB from engaging in capital raising.

We also believe that FINRA should lower the economic threshold of the types of customers an LCFB may **solicit** in order to **effect** these private placements without compromising the goal of investor protection. The "qualified purchaser" standard of the Investment Company Act of 1940[3] is, we believe, a much more appropriate standard. While, an LCFB would be allowed to serve clients such as individuals or entities seeking advice on securities offerings or sales of businesses who do not meet the "institutional investor" definition, an LCFB is more restricted in the category of investors that it can qualify, identify and solicit to invest in a transaction.

The term "institutional investor" would have the same meaning as that term has under FINRA Rule 2210 (Communications with the Public). The term generally includes banks, savings and loan associations, insurance companies, registered investment companies, governmental entities, employee benefit plans, qualified plans, or other persons (including natural persons, corporations, partnerships, trusts, family offices or otherwise) with total assets of at least $50 million or any person acting solely on behalf of any such institutional investor.

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[2] *See* Rule 016(h)(1)(F).

[3] 15 U.S.C. 80a-2(a)(51). A qualified purchaser must meet one of the following criteria: a) Individuals who own $5 million in investments; b) Institutional investors who own $25 million in investments; c) A family-owned company that owns $5 million in investments; d) For trusts with less than $25 million, a trust where the trustee and each person who contributes assets to the trust is a Qualified Purchaser; e) A "Qualified Institutional Buyer" under Rule 144A of the 33 Act, except that "dealers" under Rule 144 must meet the $25 million standard of the 1940 Act, rather than the $10 million standard of Rule 144A;
f) A company owned beneficially only by Qualified Purchasers; however, a company will not be deemed to be a qualified purchaser if it was formed for the specific purposes of acquiring the securities offered by a 3(c)(7) fund.

[illegible]

[illegible]

We also propose that FINRA collaborate with the North American Securities Administrators Association ("NASAA") and the SEC to further reduce certain administrative burdens for LCFBs while still providing meaningful investor protections. We are mindful of the vital role played by state securities regulators in monitoring activities of securities intermediaries. We urge FINRA to continue to work closely with representatives of NASAA in a joint effort to devise a more appropriate framework for limited business brokers. We also recommend that FINRA work with the SEC to devise a better investor protection mechanism than a $5,000 minimum net capital requirement. This may require a fidelity bond or perhaps a fund, to which LCFBs must contribute and that could be drawn upon in cases of fraud or other loss by an LCFB. It is important to note that individual states may have certain fidelity bond requirements and thus it is critical that they be consulted as well in order to make the final rule set more efficient and cost effective. Additionally, we believe that FINRA should eliminate the requirement for an annual audit by PCAOB accountants. These requirements seem entirely unnecessary and unduly burdensome from a financial point of view given the limited business of LCFBs, the fact that they do not execute securities transactions, maintain customer accounts or hold funds or securities. Should regulators wish to assure themselves that an LCFB or its principal has not received customer funds, the regulator could accomplish that goal far more effectively by reviewing the relevant bank account activity.

For similar reasons, the requirement to file FOCUS Reports on a quarterly basis, and the obligation to have a Financial and Operations Principal (FINOP) who has passed either the Series 27 or the Series 28 exam could be eliminated. It may be more effective to concentrate scarce regulatory resources on escrow requirements, general solicitation issues, offering documentation (in order to be able to affirmatively establish the availability of the exemption), to name a few. Regulators could require a designated principal to complete simplified training that would cover the very limited accounting skills and knowledge required for this type of broker-dealer rather than requiring a FINOP. Without lessening the financial burden of operating a firm, there is little incentive for a firm to become an LCFB rather than a broker-dealer. Likewise, FINRA could institute very focused examination and continuing educational requirements for LCFB principals and agents with respect to applicable regulatory requirements.

Additionally, FINRA should make it clear that it will permit, pursuant to NASD Rule 2420 or an amended rule, all member firms (including LCFBs) to share compensation with M&A Brokers based on a representation that the M&A Broker satisfies the conditions of the M&A Brokers Letter and the member firm has no reason to believe otherwise. This type of activity would be explicitly included in the language of the successor to Rule 2420, FINRA Rule 2040, that was proposed in 2009 but still has not been adopted.

We also urge FINRA to adopt a more streamlined Membership Process (NMA, CMA) for these basic LCFB applications. The application review period should be no more than 90 days from the time of filing and the fee should be reduced to a maximum of $1,500 (CMA) or $3,750 (NMA). The typical expense and 180-day review period from the time an application is filed, are unnecessary barriers to entry for these types of limited brokers.

Registered representatives of an LCFB should also have the opportunity to maintain registrations that go beyond those required to perform activities for the LCFB so long as they satisfy Continuing Education requirements in the related areas, similar to what has been proposed and discussed for Retained Associates.

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We support FINRA's objective to provide a broker-dealer limited category of registration. However, for the reasons cited above, we believe that the rule proposal falls short of providing an efficient and cost effective limited registration for LCFBs. The six lawyers appreciate the opportunity to comment upon FINRA's rule proposal.

Sincerely,

Faith Colish, Esq., Carter Ledyard & Milburn LLP

Martin A. Hewitt, Esq., Attorney at Law

Eden L. Rohrer, Esq., Crowell & Moring LLP

Linda Lerner, Esq., Crowell & Moring LLP

Ethan L. Silver, Esq., Carter Ledyard & Milburn LLP

Stacy E. Nathanson, Esq., Attorney at Law

TESSERA
Capital Partners

Member FINRA / SIPC, MA Registered with the SEC and MSRB

April 28, 2014

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

Re: Regulatory Notice 14-09

Dear Ms. A[illegible]

[illegible] member specializing in third party marketing services. Tessera offers traditional long-only investment management services as well as alternative investments to institutional investors and financial intermediaries. I am also a member and a part of the Board of Directors for Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Respectfully yours,

Donna DiMaria

Donna DiMaria
CEO & CCO

3PM
THIRD PARTY MARKETERS ASSOCIATION

[illegible]

[illegible]

[illegible]

[illegible]

[illegible] financial advisors that advise companies on mergers and acquisitions, advise issuers on raising debt and equity capital in private placements with institutional investors, or provide advisory services on a consulting basis to companies that need assistance analyzing their strategic and financial alternatives (Limited Corporate Financing Broker or "LCFB").

While we applaud the steps that FINRA has taken to move this initiative forward by establishing a working group of industry participants and undertaking a revised rule set, we believe that the proposed rule set requires amendments and changes in order to effectively address the nuances related to the constituency of LCFBs, in order to provide a clear roadmap for regulators, including regulatory examiners in their oversight efforts, and to afford appropriate investor protections.

To that end, this letter we will set forth our comments, suggestions and proposed amendments as applicable in the hope that we can participate in the forward-moving momentum of this initiative.

Rule 016. Definitions

Because the LCFB does not engage individual consumers in the same manner as full service BDs, the term "customer" does not fit in the vernacular of an LCFB. For regulators, regulatory field examiners and industry participants seeking to draft internal working procedures that both conform to regulations and address their business and operating needs, use of the term presents a fundamental obstacle.

In discussion with FINRA staff members we have ascertained that point (f) in the definition of a "LCFB" is intended to bring the institutional investors we work with into the definition of "customers". We feel, however that the way in which point (f) is written is unclear and leaves room for interpretation. Point (f) states that a LCFB is any broker that engages in any one or more of the following activities - qualifying, identifying or soliciting potential Institutional Investors. FINRA asserts that this clause should be read to mean that an "Institutional Investor" is receiving corporate financing services from a LCFB and is thus a "customer". The definition, however, could be interpreted to mean that qualifying, identifying or soliciting potential institutional investors is a service that benefits the manager, fund sponsor or Issuer not the "Institutional investor". Rather than force the definition into existing terms, we believe a more sound approach involves clear new definitions tailored to the business of an LCFB.

We propose that the term "customer" be eliminated from the LCFB rules. In its place, we recommend the following terms:

- **"Issuer"** – A Manger, Fund Sponsor, GP, Offerer or other similar person or organization that engages the services of a LCFB.

- **"Investor"** – any person, whether a natural person, corporation, partnership trust, family office or otherwise, that commits or is solicited to commit money or capital to the Issuer.

- **"Qualified Investor"** – We propose substituting the term "Qualified Investor" for "Institutional Investor" and utilizing the current definition of "Institutional Investor" as defined in FINRA Rule 2210 with some modifications. One such modification should include allowing Qualified Purchasers, as defined in section 2(a)(51)(A) of the Investment Company Act of 1940 [15 U.S.C. 80a-2 (a)(51)(A)], to be included in the definition of "Qualified Investors". While we recognize FINRA's concerns with lowering the threshold of "Institutional Investor" to "accredit investors", we see Qualified Purchasers as a prudent and reasonable standard for the following reasons:

    - It would provide a standard consistent with the highest requirements of alternative investment funds themselves mandated by the SEC - (3(c)(7) funds versus 3(c)(1) funds – and by extension other private placements and alternative investments; and

    - It would reduce ambiguity and inconsistency with SEC rules both where third party marketers and placement agents conduct business directly with investors and indirectly through consultants, wealth managers and other investment advisors who serve as intermediaries for the actual legal and beneficial investors.

- **Intermediary** – a Federally regulated entity that is compensated by an Investor to act on its behalf by engaging in any one of the following activities:

    - Advise the investor regarding its investment policy
    - Determine a target asset allocation

- Provide education on new investment opportunities
- Qualify, identify and select investment managers to handle mandates consistent with the Investors target allocations and risk tolerance

We believe these definitions clearly describe the counterparties involved in LCFB and provide a meaningful foundation and common vernacular for industry participants, regulators, regulatory examiners and investors alike. We believe these definitions effectively remove ambiguity and ensure the consistent application of rules as they are intended. Furthermore, by using terminology that more accurately reflects the business of a LCFB, we would eliminate any inconsistencies or uncertainty that currently exists in the proposed definitions.

Rule 116. Application for Approval of Change in Ownership, Control, or Business Operations

While FINRA has eliminated the need for members changing their status to a LCFB to file a CMA /NMA, firms would still be required to file a request to amend to their membership agreement. We believe that any firm opting into the LCFB category should be permitted to do so without a fee. We further believe that firms should have the ability to change their status back to that of a full broker dealer without the expense of transition or the need to file a CMA for at least the first year of the category's availability. We believe by making the transition period less complex and costly, FINRA will help to facilitate a broader adoption of the new rule set while allowing LCFB's to put these resources towards the revision of their compliance program.

Rule 123. Categories of Registration

3PM proposes that FINRA waive the S99 examination requirement for small firms who have a registered principal assigned to the covered functions outlined in the rule. We believe that the requirements of Rule 1230 should only apply to unregistered individuals handling any of the covered functions outlined.

Rule 125. Continuing Education Requirements

FINRA is waiving the RE requirement for LCFB, but is reserving the right to require firms to take educational courses if mandated. We would not be opposed to the requirement for additional training so long as the training is applicable to the LCFB's business and relevant from an industry perspective. In general, we support the requirement for CE testing to keep licensure active, but propose a two-year frequency which we believe to be more reasonable.

[illegible]

[illegible]

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- **[illegible]**

- *"Knowing your Investor or Intermediary"* " standard should require the LCFB to conduct thorough risk-based, due diligence review of the investor or intermediary that is reviewing the offering, again consistent with the reasonable basis review. This would include ensuring that the intermediary meets all applicable licensing standards, business and experience standards, among other reviews.

Rule 211. Suitability

We believe that Rule 211 is essential to providing meaningful, defining requirements for LCFBs. Because of the unique nature in which LCFBs conduct their business, we believe that Rule 211 must be properly crafted so that regulators, including regulatory examiners, and industry personnel alike will find a common ground, and a far more effective regulatory regime. We believe that the Rule as currently drafted does not adequately capture aspects of the suitability process that are inherent to LCFBs, and, importantly, that it does not adequately provide for investor protections.

We believe the rule as proposed fails in two primary regards:

1) by requiring the suitability analyses to be performed before any recommendation, and
2) by defining suitability in terms applicable to retail investors.

To remedy these issues, we propose that the Rule be redrafted as generally described below:

Regarding the timing of the suitability analysis, we encourage FINRA to recognize that the process of diligence related to offerings ranging from private placements offered to Investors and Qualified Investors, to placements, mergers and acquisitions of businesses of all sizes is ongoing and often does not, and should not, conclude until the deal is closed. We believe incorporation of this process is essential to investor protections and to the success of the rulemaking regime for LCFBs. We encourage FINRA to redraft Rule 2111 to require that the suitability analysis be complete by the time the subscription agreement or relevant contract is signed in recognition of the actual ongoing work performed by a LCFB and, most importantly, to protect investors in the non-institutional circumstances. With regard to the suitability requirements themselves, we again revert to our proposed definitions suggesting as follows:

- The LCFB should be required to perform reasonable basis suitability analysis regarding each "**Issuer**" by which it is engaged.

- The LCFB should be required to perform a reasonable basis suitability analysis regarding each "**Intermediary**" with which it does business. The LCFB will perform no look-through to the underlying investor so long as the suitability review of the Intermediary demonstrates that the Intermediary is qualified to recommend suitable securities to their clients and represents that their clients are Qualified Purchasers and thus "**Qualified Investors**".

- The LCFB should be required to perform Investor-Specific suitability analysis as per FINRA Rule 2111 for every "**Investor**" with which it directly conducts business (not through an Intermediary").

- The LCFB should be required to perform a suitability analysis similar to that required by the institutional investor exemption as per Rule 2111 for every "**Qualified Investor**" for which it directly conducts business (not through an intermediary). The requirement for a "**Qualified Investor**" to provide an affirmative indication of independent judgment should be waived.

Rule 2210 Communications with the Public

While the LCFB proposal did remove two of the three communication categories covered by Rule 2210, Retail Communications and Correspondence, these are categories that by definition would not apply to a LCFB who can only work with institutional investors. Accordingly, the changes to the Rule did make the rule more relevant to the members who may decide to register as a LCFB than it was before. LCFBs are still subject to the same provisions of Rule 2210 covering institutional communications as we were before which we believe do not accurately reflect how LCFB firms operate in a real life setting.

[illegible] proposes that FINRA revise Rule 2210 and specifically the general content standards to meet the realities of representing issuers. Proposed modifications should include a realistic approach to setting fair and balanced content standards for communications and marketing materials as well as an expansion of the exemptive provisions for our new definition of "**Qualified Investor**" especially those that are professional advisors or use the services of investment consultants.

Rule 240. Engaging in Impermissible Activities

As proposed, FINRA may impose severe penalties on a LCFB if the firm engages in any activities that require the firm to be registered as a broker or dealer under the Exchange Act. To ensure an evenhanded approach, modification would include explicit language outlining a defined remedial period and process for any unintentional activities of an LCFB until the practical application has played out which will likely illuminate these areas of the Rule framework which warrant additional precision. Egregious and intentional disregard of an LCFB would still fall into the enforceable realm of FINRA authority.

Rule 331. Anti-Money Laundering Compliance Program

3PM recognizes that all financial institutions play an important role in the detection and prevention of money laundering. While we believe that extending the independent test requirement from annually to bi-annually is appropriate for LCFBs, we also suggest that FINRA consider amending the Customer ID Program (CIP) requirements to conform to the business of a LCFB. Specifically, 3PM recommends that LCFB's should be required to implement a CIP as follows:

- For all Issuers and Intermediaries with which the LCFB does business
- For all Investors when there is no Intermediary involved.

Rule 411. Capital Compliance

3PM believes that proposed Rule 411 should remove the minimum net capital requirement of $5,000 currently applied to the LCFB members. Furthermore, FINRA should assist the LCFB community in working with the SEC to correct the calculation of net capital for LCFBs so that the nature of our business does not cause us have to improperly report our financial condition to the FINRA. Additionally, we suggest that FINRA overhaul the current Supplemental Statement of Income ("SSOI") content by convening a working committee of LCFBs to help write appropriate questions that accurately reflect our business model. Further details regarding specific components of the proposal are described below.

- **Net Capital Requirement** – The current net capital requirement thresholds of $250,000, $100,000, and $50,000 respectively for carrying members and introducing members are rather arbitrary in nature; however, the materiality of these dollar amounts at least substantively supports the spirit of these minimum net capital requirements which is in part to protect the customer should a scenario unfold which causes damage to an investor. In theory, the broker dealer carrying or clearing that customer account would have minimally sufficient reserves to apply to a remedial solution for the customer. When applying this ideology to the $5,000 net capital requirement for LCFBs (non-carrying and non-clearing members), it is clear that $5,000 would universally be determined as an insufficient amount to apply to any hypothetical remedial solution involving a customer. One may then deduce that this specific net capital requirement remains in place to ensure that all member firms remain on the grid and adhere to the general net capital requirement apparatus, and that perhaps the intention was that a well thought out resolution would be implemented down the line. This time has now finally come and we collectively need to implement specific rules which effectively and efficiently regulate the LCFB universe of member firms.

Countless hours and resources have been allocated to this $5,000 minimum net capital requirement by LCFBs and FINRA examiners alike. This is clearly not an effective and efficient use of our collective resources when recognizing that the minimum net capital requirement of $5,000 for LCFBs (non-carrying firm) does not deliver any type of investor protection.

- ***FOCUS Reports and Calculation of Net Capital*** **-** 3PM believes that the calculation of net capital and FOCUS reporting requirements for LCFB members need to be overhauled as the current set of calculations and data points are not directly applicable to the business conducted by LCFBs. We believe that this approach is simply another attempt by both FINRA and the SEC to standardize reporting regardless of fit rather than make the appropriate changes required for LCFBs to properly assess their financial viability and ability to protect investors.

  A specific issue that illustrates this disconnect is demonstrated through the revenue generation framework relative to private placement activity. When payment is due, a LCFB will book a receivable for the incentive fee owed to the firm. Often a corresponding payable will be established that would pass-through a portion of that fee to the registered representative who gets paid a commission on that fee. Both of these entries are in compliance with the SEC and GAP standards. A disconnect, however occurs in the firm's calculation of net capital. Under SEC rules, the current net capital calculation does not allow the accrued receivable to be offset by the payable that is directly related to it. Instead, the entire net commission payable is required to be recorded as aggregate indebtedness (AI), in effect requiring the LCFB to double count the payable. This methodology does not adhere to GAP standards which would allow for the corresponding offset to the receivable. Furthermore a significant number of PCAOB registered accountants believe that this is the improper way to record revenue or calculate AI. By following the SEC's mandated approach, the LCFB is not accurately reflecting its true capital condition.

- ***Supplemental Statement of Income ("SSOI")*** – In an attempt to gather new information and intelligence, FINRA implemented the SSOI. The SSOI incorporated new questions and data requests regarding the financial condition of member Firms. While the goal of this exercise was worthwhile, we believe that the results FINRA receives from these forms are inaccurate due to

[illegible]

[illegible]

Rule 414. Audit

3PM believes that the cost of Audits, which are extremely prohibitive to small firms, need to be addressed. Given the new requirement that PCAOB Auditors must now be audited by the Board, the costs of such audits, which will be absorbed by the broker dealer community, is growing exponentially. The rule requiring PCAOB audits was initially intended to cover firms working with public entities, not small, broker dealers like those that are covered by the LCFB rule set. Furthermore, the PCAOB interim inspection program findings simply are not relevant to LCFBs, and would therefore would not be found in the audits of our firms.

We believe that FINRA should work with other Authorities and Government Agencies, in this case the PCAOB, to help carve out small broker dealers, specifically LCFBs from this new oversight requirement. Please see the Appendix for a report entitled PCAOB Audit Oversight and Small, Non-Public Non-Custodial Broker-Dealers; Attributes-Based Analysis of the Broker-Dealer Risk Profile which supports 3PM's perspective.

Rule 436. Fidelity Bonds

3PM feels that Rule 4360 is not applicable to LCFBs and should be omitted from the rule set. Continuing to subject LCFBs to this Rule does not make sense and offers no protection to the LCFB or investors.

The LCFB proposal did not make any changes to Rule 4360 and as such LCFBs are still required to obtain a fidelity bond. A fidelity bond insures a firm against intentional fraudulent and dishonest acts committed by employees and registered representatives under certain specified circumstances. In cases of theft of customer funds, a fidelity bond generally will indemnify a firm for covered losses sustained in the handling of customers' accounts. Since, by definition, an LCFB is not permitted to hold or handle customer funds or securities, this rule is irrelevant to LCFBs. Under the current rules, LCFBs are required to secure costly insurance policies that would protect us and our customers from bankruptcy. While in theory the idea is sound, in practice if an LCFB was ever sued for wrongdoing, the fidelity bond policy would not cover our firms or provide the bankruptcy protection the Rule was designed to provide. Since this rule does offer any type of protection, LCFBs are wasting capital on premiums that could alternatively be used to support business operations.

Additional Rules Not Covered in the LCFB Rule Set

3PM believes that LCFBs should be exempt from membership in SIPC. Furthermore, while we understand that FINRA was not the authority that mandated compliance with SIPA, we do believe that FINRA is in a position to assist the LCFB community in its mission to seek relief from this irrelevant requirement.

Rule 2266. SIPC Information

The proposed rule set did not make mention about Rule 2266 and whether or not this Rule applied to LCFBs. 3PM would however like to make clear our thoughts on the relevancy of this Rule to LCFB firms.

SIPC was created under the Securities Investor Protection Act as a non-profit membership corporation. SIPC oversees the liquidation of member broker-dealers that close when the broker-dealer is bankrupt or in financial trouble, and customer assets are missing. In a liquidation under the Securities Investor Protection Act, SIPC and the court-appointed Trustee work to return customers' securities and cash as quickly as possible. Within limits, SIPC expedites the return of missing customer property by protecting each customer up to $500,000 for securities and cash (including a $250,000 limit for cash only).

SIPC is an important part of the overall system of investor protection in the United States. While a number of federal and state securities agencies and self-regulatory organizations deal with cases of investment fraud, SIPC's focus is both different and narrow: restoring customer cash and securities left in the hands of bankrupt or otherwise financially troubled brokerage firms.

In SIPC's own words, their mission directly relates to protecting customer assets. LCFB firms by definition ***"do not include any broker or dealer that carries or maintains customer accounts, holds or handles customers' funds or securities, accepts orders from customers to purchase or sell securities as a principal or as an agent for the customer"***. As such, LCFB are continually paying assessments on their revenues in to the SIPC fund to protect investors that will never require coverage from such an event from a LCFB. This rule is not properly aligned with the business of LCFB and creates significant expenses to LCFBs without providing any tangible benefit. In reality LCFBs are paying into a fund that reimburses investors for somebody else's wrongdoing which is an unfair practice.

Questions posed by FINRA

FINRA particularly requested comment concerning the following issues:

- **Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?**

  We believe it is FINRA's intent and consistent with investor protections in general, to offer the greatest level of protection to the individual or entity making the capital commitment or investment. In our language, as proposed above, this is the investor. We believe that by changing the definitions that apply to LCFBs as we have proposed, FINRA would address the fundamental confusion and inconsistencies that exist in the current rulebook and close any loopholes that are open to interpretation as to who is actually a LCFB's "customer". Further we believe that the suitability rules must be amended to better reflect the business those firms offering private placements actually engage in. This would ensure that reasonable basis and investor level suitability are considered ongoing requirements timed to the purchase of an investment rather than to the recommendation.

- **Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?**

  We do not believe that the current rule set as written is relevant to the LCFB business model for the reasons articulated above is our discussion on the proposed rule set for LCFBs.

- **Is the definition of "limited corporate financing broker" appropriate? Are there any activities in which broker-dealers with limited corporate financing functions typically engage that are not included in the definition? Are there activities that should be added to the list of activities in which an LCFB may not engage?**

  We believe that definition of LCFB is appropriate.

- **Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?**

  We believe that firms may forego the new registration category until details regarding the NMA/CMA process are better defined. In particular, the cost of switching registration types and potential enforcement may outweigh the benefits gained by changing categories. For this reason, we request that consideration be given to preliminarily offering the LCFB registration as a category (in lieu of "Other") subjecting the relevant portion of a firm's business to the new rules, as opposed to requiring an all-or-none decision. This would facilitate an orderly transition for firms, lessen the learning curve for examiners, and generally reduce the margin for unintended consequences.

- **What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?**

  3PM does not believe that this rule will have a meaningful economic impact on the LCFBs that are eligible to operate under this proposed rule set. We are not convinced that firms will adopt the rules unless and until LCFB registration eliminates costly and, we would argue irrelevant, financial audits and reporting, AML Independent Testing, and SIFMA registration.

- **FINRA welcomes estimates of the number of firms that would be eligible for the proposed rule set.**

  The below information was excerpted from a report presented to PCAOB in early 2013. While the data may not be as current as we would like, we believe numbers reflect a viable estimate of the firms that would be eligible to register as a LCFB.

  FINRA, defines a small firm is any firm with 150 or fewer licensees, or registered representatives. FINRA is comprised of approximately 4400 firms of which 85% are categorized as small firms. A significant percentage of small broker-dealers that have only 2 or fewer business lines, have less than $1mm in annual revenue, and/or engage in business lines such as private placements, mergers and acquisitions, and other such business lines which would fall under the category of LCFB.

  These types of small broker-dealers are readily identifiable using BrokerCheck, FINRA's public resource for broker-dealer background reviews, or through its central data depository (CRD) with the following acronyms:

    - Other
    - PLA – Private Placement
    - PLA and Other

  Of the 4400 FINRA broker-dealers registered, the statistics reveal the following:

- 191 broker-dealers report that private placement activity is their only business line;
- 174 broker-dealers do not fall into any of the customary FINRA business lines and disclose "Other" as their only line of business. Most of these describe their business as mergers and

acquisitions;

- 541 broker dealers disclose that they engage solely in private placement agent and "other" activities, again describing the other activity as mergers, acquisitions and placement agent or third party marketing services.

Cumulatively, these 906 firms represent a class of broker-dealer that does not open securities or investment accounts, does not carry or introduce assets or securities, and does not have customers in the retail sense. The business activities of these firms are governed by contract and are not "transactional." As such, we would conclude that they would fall under the definition of a LCFB.

It is important to note that the majority of these firms are also very small firms, and many have revenue of less than $1mm/year. Of the 457 firms reporting only one line of business (private placements or "other") all but 13 are small firms (fewer than 50 employees). Of those reporting two business lines private placements and "other", 98% have fewer than 50 employees.

Attributes	# Firms	# with Fewer than 50 RRs	As %
PLA	191	188	98%
Other	174	164	94%
PLA and Other	541	528	98%
Total or Average	**906**	**880**	**97%**

- **Proposed LCFB Rule 123 would limit the principal and representative registration categories that would be available for persons associated with an LCFB. Are there any registration categories that should be added to the rule? Are there any registration categories that are currently included in the proposed rule but that are unnecessary for persons associated with an LCFB?**

3PM does not believe that the Rule 123 should limit the principal and registration categories that would be available for persons associated with a LCFB. We believe that there are other registration categories that could apply to a LCFB that are not included in the proposed rule set. For example,

- LCFB Firms that are registered as a broker dealer with the ability to engage in investment advisory services would also need to hold the Series 65 or 66 registrations
- Some LCFBs may be required under state requirements to hold the Series 63 registration
- LCFB Firms that are distributing mutual funds may have associated persons holding the Series 6 and 26 registrations

- LCFB firms may be acting as a solicitor for direct participation programs and may have associated persons holding the Series 22 and 39 registrations
- LCFB firms offering private placements whereby the Issuer is a CTA may be required to have associated person who hold the Series 3, 30, 31 or 32 registrations
- LCFB firms offering private placements whereby the Issuer's strategy involves options may hold the Series 4 and 42
- LCFB firms may have associated persons holding the Series 14 examination

As such we believe that FINRA should not restrict the principal and representative registration categories for persons associated with a LCFB.

- **Should principals and representatives that hold registration categories not included within LCFB Rule 123 be permitted to retain these registrations?**

IPM believes that principals and representatives should be able to continue to retain their registrations so long as they continue to stay current with their CE requirements. We believe that prohibiting a principal or representative from maintaining a registration because it was not within LCFB 123 would be penalizing a professional for choosing to engage in a regulatory scheme that was more relevant to their current business operations. The financial industry has long been categorized by inventive and driven people who often change firms or focus several times throughout their careers. We believe allowing a LCFB to maintain additional registrations would be no different than someone who changed roles in a firm and continued to maintain registrations used in a previous role.

- **Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?**

We believe that there are firms that would otherwise qualify as a LCFB that make recommendations to customers. We believe that our recommendations regarding the fundamental definitions of counterparties and their respective roles in suitability address concerns that may exist or arise from recommendations of this type.

- **Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014,9 impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?**

In general, 3PM members conduct a business that is very different than the business conducted by Faith Colish et al. As such we do not believe that this would be a reason for any of our constituents to choose not to register as a LCFB.

3PM does not believe that many FINRA members meeting the definition of this rule will convert their registration to this category. Our reasoning is that there are just not enough meaningful changes to the rule which would make it more conducive to the business of LCFBs. LCFBs are currently spending a great deal of time and resources following rules that are not appropriate or applicable to our businesses. These are resources that can alternatively be applied to making meaningful enhancements to our business and compliance operations.

While we are pleased that FINRA took on this initiative and convened a working industry group to address the issue, the feedback solicited from this group was only related to the definition of an LCFB not the underlying rule set. We believe that FINRA should have taken the initiative at least one step further and worked together with the industry to write a meaningful and relevant rule set rather than the one presented which did little more than remove the sections of rules that already did not apply to us. We only hope that all of the industry feedback received will not dissuade FINRA from revisiting this proposal and this time listening to what the industry has to say. 3PM stands ready to participate in any further initiatives regarding this proposal and looks forward to a day when LCFBs have a rule set that appropriately addresses our business model.

If you have any questions or comments regarding any of the information contained in this letter or would like to discuss any of these comments in further detail, please feel free to contact me directly by phone at (212) 209-3822 or by email at donna.dimaria@tesseracapital.com.

Thank you in advance for your consideration.

Regards,

Donna DiMaria
Chairman of the Board of Directors
3PM Association

Appendix

3PM is an association of independent outsourced sales and marketing firms that support the investment management industry worldwide.

3PM Members are properly registered and licensed organizations consisting of experienced sales and marketing professionals who come together to establish and encourage best practices, share knowledge and resources, enhance professional standards, build industry awareness and generally support the growth and development of professional outsourced investment management marketing.

Members of 3PM benefit from:

- Regulatory Advocacy
- Best Practices and Compliance
- Industry Recognition and Awareness
- Manager Introductions
- Educational Programs
- Online Presence
- Conferences and Networking
- Service Provider Discounts

3PM began in 1998 with seven member-firms. Today, the Association has more than 35 member organizations, as well as significant number of prominent firms that support 3PMs and participate in the Association as 3PPs, Industry Associates, Member Benefit Providers, Media Partners and Association Partners.

A typical 3PM member-firm consists of two to five highly experienced investment management marketing executives with, on average, more than 10 years' experience selling financial products in the institutional and/or retail distribution channels. The Association's members run the gamut in products they represent. Members work with traditional separate account managers covering strategies such as domestic and international equity, as well as fixed income. In the alternative arena, members represent fund products such as mutual funds, hedge funds, private equity, fund of funds and real estate. Some firms' business is comprised of both types of product offerings. The majority of 3PM's members are currently registered with FINRA or affiliated with a broker-dealer that is a member of FINRA.

For more information on 3PM or its members, please visit www.3pm.org

PCAOB Audit Oversight and Small, Non-Public Non-Custodial Broker-Dealers

Attributes-Based Analysis of the Broker-Dealer Risk Profile

January 2013

Report Objectives

Since its inception, the PCAOB has exerted diligent efforts to carry out its mission of investor protection. When Dodd Frank expanded the scope of PCAOB authority to include oversight of the audits and auditors of broker-dealers, the broker-dealer community responded with recommendations for exclusions of certain types of broker-dealers. While forging ahead with an interim audit program, Board members have continued to express their interest in identifying and understanding trends related to broker-dealer attributes, facilitating a meaningful dialogue regarding risk, and possibly leading to exclusions.

This brief report will present data and information to support exemption of certain classes of small and limited purpose broker-dealers from the PCAOB audit requirement. It presents an update to data previously shared in March 2011, and asserts that broker-dealers of limited size and/or with limited business purposes present little or no risk relative to the scope of PCAOB responsibilities to protect investors. To best ensure that risk is adequately considered, the report includes an analysis of SIPC distributions through 2012 based on dollar amount and broker-dealer attributes.

Data presented in this report may lead to other useful trend analyses, including the consideration of excluding other types of firms, such as introducing firms, firms with minimum net capital of $5,000, or firms with less than $1mm in annual revenue.

Background

To FINRA, a small firm is any firm with 150 or fewer licensees, or registered representatives. FINRA is comprised of approximately 4400 firms of which approximately 85% are categorized as small firms. But 'small' is relative. To a research analyst, a small cap company is one with $300 million to $2 billion in market capitalization. The JOBS Act, designed to lower the regulatory burdens for small companies intending to go public applies to companies with less than $1billion in revenues. By stark contrast, many of the smallest broker-dealers are scattered along a broad spectrum of characteristics and attributes much smaller than any of these standards.

Low Risk Broker-Dealers Based on FINRA Data

Significant percentages of small broker-dealers have only 2 or fewer business lines, have less than $1mm in annual revenue, and/or engage in business lines that do not inherently indicate high percentages of risk, such as 'application way' mutual funds, variable annuities, private placements, mergers and acquisitions, and other such business lines. Many of these firms operate under a minimum net capital requirement of $5,000.

Small broker-dealers characterized by business lines are readily identifiable using BrokerCheck, FINRA's public resource for broker-dealer background reviews, or through its central data depository (CRD) with the following acronyms:

- MFR – Mutual Funds Retailer
- MFR and VLA
- Other
- PLA – Private Placement
- PLA and Other
- VLA – Variable life insurance or annuities

Of the 4400 FINRA registered broker-dealers, the statistics reveal the following:

- **191** broker-dealers report that private placement activity is their only business line;
- **174** broker-dealers do not fall into any of the customary FINRA business lines and disclose "Other" as their only line of business. Most of these describe their business as mergers and acquisitions;
- **541** broker-dealers disclose that they engage solely in private placement agent and "other" activity, again describing the other activity as mergers, acquisitions and placement agent or third party marketing services.

Cumulatively, these **806** firms represent a class of broker-dealer that does not open securities or investment accounts, does not carry or introduce assets or securities, and which does not have customers in the retail sense. The business activities of these firms are governed by contract, and are not 'transactional.'

Consider also the following approximate number of firms that only engage in retail sales to customers by application:

- **39** broker-dealers report that their only business line is retail sales of mutual funds. Out of these 39 firms, **all but 3 have fewer than 25 employees;**
- **21** broker-dealers offer only variable annuities. **16 of the 21 report having fewer than 50 employees;**
- **87** broker-dealer firms disclose having only two business lines, mutual funds and variable annuities. **82% of these companies have fewer than 10 employees**.

The **147** broker dealers described above engage solely in 'application-way' business, which means that their business is limited to purchases and sales of funds and/or annuities accomplished through direct paper-based application to the mutual fund or annuity companies. These companies do not have custody of customer funds or securities, and also do not have clearing arrangements (they are not 'introducing'). Rather they operate through selling agreements with mutual fund and annuity companies, which are themselves regulated by the SEC.

It is important to note that the majority of these firms are also very small firms, and many have revenue of less than $1mm/year. (see the chart below). Of the 457 firms reporting only one line of business (private placements, "other", mutual funds, or variable annuities) all but 20 are small firms (fewer than 50 employees). Of those reporting two business lines (Private placements and "other"), 98% have fewer than 50 employees.

Attributes	# Firms	No. with Fewer than 50 RRs	As %
PLA	[illegible]	158	95%
Other	174	164	94%
PLA and Other	541	[illegible]	[illegible]
MFR	59	57	95%
VLA	21	16	76%
MFR and VLA	87	82*	94%
Total or Average	1,052	1,015	96%

* Nearly 50% of 87 BD firms with combination of only two attributes MFR and VLA have fewer than 10 employees.

Low Risk Broker-Dealers Based on SIPC Data

SIPC weighed in against a statutory exemption for broker-dealers during Congressional deliberations regarding the PCAOB's scope of authority over broker-dealer audits. Later, in response to the request by broker-dealer trade associations and others encouraging PCAOB to carve out introducing broker-dealers from its audit scope, SIPC again wrote to PCAOB in favor of an all-inclusive audit program, citing statistics regarding its payouts related to introducing broker-dealer liquidations in particular.

While SIPC payouts may be used as a measure of risk, even SIPC has never undergone consideration of liquidation coverage for the types of small broker-dealers discussed in this report.

In this context, a review of SIPC distributions for the past 5 years demonstrates that companies with only 1 or 2 business types or attributes in the following combinations present little or no risk of insolvency for investors. In fact, no broker-dealer with 2 or fewer business lines, including those listed below has every been represented on SIPC bankrolls:

- MFR – Mutual Funds Retailer
- MFR and VLA
- Other
- PLA – Private Placement
- PLA and Other
- VLA – Variable life insurance or annuities

Low Risk Broker-Dealers Based on PCAOB Data

PCAOB's interim audit program preliminary results, reported August 2012, reveal certain material weaknesses in BD audit programs. While the findings appear proportionately significant, the results are less worrisome in the context of small broker-dealers as summarized in the table below:

Finding	Description	Application to Small and Limited Purpose Broker-Dealers
Supplemental Report on Material Inadequacies	21 of 23 did not adequately test for controls related to safeguarding securities	Not applicable to non-custodial broker-dealers
Exemption from Provisions of Customer protection Rule	All 14 audits of BDs claiming exemptions to 15c3-3 did not fully comply with conditions of the exemption	Not applicable to non-custodial broker-dealers
Customer Protection Rule	2 of the 9 audits of BDs required to maintain a customer reserve failed to properly verify and disclosure the appropriate restrictive provisions	Not applicable to non-custodial broker-dealers
Net Capital Rule	7 of 23 audits failed to sufficiently test the minimum net capital computation	Not materially significant to broker-dealers with $5,000 minimum net capital
Consideration of Risks of Material Misstatements Due to Fraud	13 of 23 audits did not incorporate adequate assessments of risks of material misstatement	Subject to FINRA reviews, requirements
Related Party Transactions	10 of 23 audits did not adequately test existence and/or sufficiency of procedures related to material third party transactions	Subject to FINRA reviews, requirements
Revenue Recognition	15 of 23 audits did not adequately test occurrence, accuracy and completeness of revenue	Not materially applicable to firms with <$1mm annual revenue
Establishing a Basis for Reliance on Records and Reports	12 of 23 audits did not evidence adequate procedures for reliance on third parties used in the audit process	Not applicable to the accounting firms most likely to perform the audits of small broker-dealers
Fair Value	6 of 9 audits involving valuations did not adequately test valuation	Not applicable to non-custodial

Finding	Description	Application to Small and Limited Purpose Broker-Dealers
measurements	practices	broker-dealers
Evaluation of Control Deficiencies	4 of 23 audits did not evidence sufficient evaluation of identified errors for determination of control weakness	Subject to FINRA reviews, requirements
Financial Statement Disclosures	7 of 23 audits did not evidence adequate tests of accuracy and completeness of financial statement disclosures	Subject to FINRA reviews, requirements
Auditor Independence	2 audits revealed inadequate procedures to test auditor independence	Subject to discussion

This summary data can be interpreted to mean that many of the PCAOB interim inspection program findings simply are not relevant, and therefore would not be found, in the audits of small broker dealers. Of those with a degree of relevance, most would be apparent as a result of the regulatory initiatives carried out by FINRA, which incorporate considerable depth in routine inspections of broker-dealer financial data. FINRA reviews include ongoing assessments of FOCUS filings carried out at both the district and national levels, and FINRA performs routine onsite inspections according to a risk-based cycle. These inspections include reviews of financial data, and cover all registered broker-dealers.

Summary

[illegible]

- [illegible]
- [illegible]
- [illegible]
- [illegible]

Each of these considerations is consistent with the recommendation of this paper that broker-dealers in any of the following categories should be excluded:

- Non-custodial, non-public BDs with 2 or fewer business lines including but not limited to the following:
  - MFR
  - VLA
  - PLA
  - Other

Important to the practical implementation of this recommendation, each of the attributes listed above is based on data and information routinely reported to FINRA and/or the SEC. As such, this data is readily available from a reliable regulatory source.

By excluding BDs based on these attributes, the PCAOB will have trimmed its auditor oversight by a measurable degree (approximately 1,400 firms) without compromising its mission.

AMERICAN BAR ASSOCIATION
Business Law Section

ABA BUSINESS LAW SECTION

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May 21, 2014

Via email to: pubcom@finra.org

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

Re: FINRA Regulatory Notice 14-09
Request for Comment on Proposed Rules for Limited Corporate Financing Brokers

This comment letter is submitted on behalf of the Committee on Federal Regulation of Securities (the "*Committee*" or "*we*") of the Business Law Section (the "*Section*") of the American Bar Association (the "*ABA*"), in response to the request for comment by the Financial Industry Regulatory Authority, Inc. ("*FINRA*"), in Regulatory Notice 14-09 ("*RN 14-09*" or the "*Proposal*") with respect to a proposed new rule set for "Limited Corporate Financing Brokers" ("*LCFBs*" and "*LCFB Rules*"). As described in the Proposal, an LCFB would fall within a new FINRA member firm category and engage only in a limited range of activities, essentially advising companies and private equity funds on capital raising and corporate restructuring. The LCFB Rules would not apply to member firms that carry or maintain customer accounts, handle customers' funds or securities, accept customers' trading orders, or engage in proprietary trading or market-making.

This letter was prepared by members of the Committee's Subcommittee on Trading and Markets. While this letter represents the views of those who have prepared and reviewed it, this letter has not been approved by the ABA's House of Delegates or Board of Governors and, accordingly, does not represent the official position of either the ABA or the Section.

We commend FINRA for developing a customized rule set pertinent to the limited activities of members engaged in the subset of activities described in the Proposal. We strongly encourage FINRA to move forward with refining and advancing the Proposal to the formal rulemaking stage after taking into consideration the various comments and recommendations you receive during this initial public comment process. As set forth in detail below, we have responded to FINRA's request for comments on RN 14-09 and also provide our views about the strong public policy rationale underlying the Proposal and other rulemaking in conjunction with FINRA's retrospective rule review.[1]

[1] *See, e.g.*, FINRA Regulatory Notice 14-14, *FINRA Requests Comment on the Effectiveness and Efficiency of its Communications With the Public Rules*; FINRA Regulatory Notice 14-15, *FINRA Requests Comment on the Effectiveness and Efficiency of its Gifts and Gratuities and Non-Cash Compensation Rules*.

General Comments

FINRA requested comment on all aspects of the LCFB Rules, including any impact on institutional customers and issuers, potential costs and burdens that the Proposal would impose on LCFBs, and any cost savings and reduced burdens that the proposal would create for LCFBs. FINRA also requested comment on whether LCFBs should be subject to other requirements in the transitional and consolidated FINRA rulebook (together, the "FINRA Rules"). Set forth below are our general comments regarding the Proposal as well as other observations regarding FINRA's rulemaking process, followed by our more specific comments with respect to the proposed LCFB Rules.

As a general matter, we believe FINRA should give careful consideration to the impact of the LCFB Rules, as well as existing rules, on smaller, limited, and non-traditional firms including "finders", merger and acquisition intermediaries, advisers, and business brokers (collectively, "M&A brokers"), and private fund placement agents. These types of members would, in our view, be the most likely to benefit from and utilize the relief created by the Proposal. Accordingly, our comments are primarily focused on the LCFB Rules as relevant to these members. We also believe FINRA should take into consideration the potential impact of the Proposal—and, as importantly, the failure to move forward with it—upon the availability of capital-raising and business brokerage services to smaller privately held companies and private funds. These types of customers are most often served by smaller, limited, and non-traditional members.

Particularly in the context of the LCFB Rules and ideally in all of the FINRA Rules, we believe FINRA should more clearly differentiate between capital-raising and M&A brokerage services, which are two very different types of securities-related activities and are accompanied by correspondingly different "investor protection" considerations. We also believe the FINRA Rules need to better accommodate limited brokerage service business models, such as members that place private fund securities with "institutional investors", as we suggest that term be redefined. There are important contextual distinctions between private and public companies, private and public offerings, active versus passive investors, and sophisticated institutional investors staffed by professional managers, yet the FINRA Rules largely combine these securities-related activities together making it challenging for member firms to parse these rules for those requirements applicable to their particular activities.

With these considerations in mind, we believe several of the proposed LCFB simplifications do not go far enough to be meaningful to either smaller FINRA member firms or the smaller business issuers and owners intended to be served by the Proposal. We also believe FINRA should give greater consideration to the overall complexity and largely retail brokerage orientation of the FINRA Rules in general. As reported in its 2012 Year in Review and Annual Financial Report, FINRA has embarked upon a more structured analysis of the costs and benefits of new and existing rules. We commend those efforts, particularly since the economic impact of the FINRA Rules on smaller member firms and the smaller privately owned companies they commonly serve have not, in the view of many industry participants, been given adequate con-

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[illegible] owned businesses for their livelihoods. Similarly, venture capital and private equity funds, business development companies, and similar privately-raised pools of capital are critically important financial resources for privately held companies at various stages of their development. These types of professionally-staffed institutional investors are well-equipped to do their own due diligence, economic and financial analysis, and evaluation of privately owned businesses and thereby to more effectively provide corporate financing or acquire a controlling interest in a portfolio company. Participation in these transactions by well-managed pooled investment vehicles reduce some of the risks associated with small business enterprises for the benefit of their own investors through diversification of their portfolios of corporate financings and acquisitions, and so as a matter of public policy should be strongly encouraged.

FINRA's regulation of securities-related services has a direct and substantial impact on each of these stakeholders whose interests are often not well articulated in the context of broker-dealer regulation or rulemaking. Addressing several areas of particular concern will require FINRA's coordination with the SEC and a joint evaluation of how their respective rules impact the securities-related services available to smaller private business issuers and owners. These stakeholders depend on and benefit from the professional services provided by intermediaries that are, or by law should be, registered and regulated as broker-dealers under Section 15 of the Securities Exchange Act of 1934, as amended ("Exchange Act"), and related rules. The statutory definition of "broker" and related interpretations and guidance issued by the SEC and its staff[3] encompass a broad range of securities-related activities subsumed within the traditional

[2] See Section 15(b)(8) under the Securities Exchange Act of 1934, as amended, which provides: "It shall be unlawful for any registered broker or dealer to effect any transaction in, or induce or attempt to induce the purchase or sale of, any security (other than commercial paper, bankers' acceptances, or commercial bills), unless such broker or dealer is a member of a securities association registered pursuant to section 15A of this title or effects transactions in securities solely on a national securities exchange of which it is a member." FINRA is the only registered securities association at present.

[3] See Exchange Act Section 3(a)(4). *See also* SEC Staff *Guide to Broker-Dealer Registration*, available at: http://www.sec.gov/divisions/marketreg/bdguide.htm; SEC staff no-action letters cited in the American Bar As-

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[illegible]

For example, smaller privately held companies may seek capital from a small number of investors and only seek initial introductions to those prospects. Similarly, some larger privately held companies may seek institutional corporate financing through a negotiated transaction that involves its issuance of custom-tailored securities to a single professional investor, such as a private fund or insurance company. Commonly in these instances, the broker does not handle, even momentarily, the issuer's securities or the investor's cash and so no custody-related investor protection, SIPC, or anti-money laundering considerations appear to be implicated. Typically, in these transactions the broker has not undertaken any financial obligation to the issuer or investor and yet a panoply of net capital and operational rules still apply, including those requiring GAAP accounting, quarterly financial reporting, audited financial statements, employment of a financial and operations principal, and anti-money laundering procedures. Each of these requirements imposes a substantial on-going compliance cost, but without any apparent investor protection benefit given this limited service context.

Similarly, the owners of smaller private companies eventually need assistance in preparing for sale, finding buyers, and transitioning ownership. Small business sales are commonly structured as cash-for-assets transactions and do not involve securities or related regulation; however, for various reasons, in some transactions the parties may choose to convey ownership through the transfer of the company's securities—a stock sale or exchange through a merger or other business combination. The same economic objective of the parties—conveying ownership of the business—can have vastly different regulatory consequences to the M&A broker de-

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sociation, Business Law Section, *Report and Recommendations of the Private Placement Broker-Dealer Task Force* (2005), available on the SEC's web site at http://sec.gov/info/smallbus/2009gbforum/abareport062005.pdf ("*ABA PPB Report*").

4 FINRA By-Laws, Article I, paragraph (u) defines the phrase "investment banking or securities business" as "the business, carried on by a broker, dealer, or municipal securities dealer (other than a bank or department or division of a bank), or government securities broker or dealer, of *underwriting or distributing issues of securities, or of purchasing securities and offering the same for sale as a dealer, or of purchasing and selling securities upon the order and for the account of others*" (emphasis added).

[illegible]

[illegible] apply FINRA's By-Laws and virtually all of the FINRA Rules to their "investment banking or securities business".

Analyzing how the FINRA Rules do and do not apply in a limited, non-traditional context is sometimes difficult, even for experienced securities counsel. Existing rules, perhaps for historical reasons that are no longer applicable, do not appear to distinguish between capital-raising where protecting passive investors is a paramount consideration, and M&A transactions where sellers and buyers of privately owned companies control and actively run those businesses and where buyers perform substantial self-directed pre-purchase due diligence because they will control and run the business after closing. FINRA's "know your customer" and "suitability" rules as applied to "customers" who are passive investors make little sense when applied to business sales and M&A transactions.[8] How does a member demonstrate the customer-specific suitability of an M&A transaction to a prospective business seller or buyer?[9] Many small business

5 This assumes that the intermediary is, in fact, SEC-registered and not relying on SEC staff no-action letters to avoid broker-dealer registration. The limitations and impact of these no-action letters is discussed later in this letter.

6 The term "investment banking services" is defined in FINRA Rule 2711, *Research Analysts and Research Reports*, but only for purposes of that specific rule. FINRA Rule 2711(a)(3) provides "[i]nvestment banking services" include, without limitation, acting as an underwriter or participating in a selling group in an offering for the issuer; acting as a financial adviser in a merger or acquisition; providing venture capital, equity lines of credit, private investment, public equity transactions (PIPEs) or similar investments; or serving as placement agent for the issuer."

7 *See, e.g.*, NASD Rule 1032(i)(defining the registration and qualifications category of "Limited Representative—Investment Banking"); FINRA Rule 2711, *Research Analysts and Research Reports*, and FINRA Rule 5110, *Corporate Financing Rule—Underwriting Terms and Arrangements*.

8 *See* FINRA Rule 2090, *Know Your Customer*, and FINRA Rule 2111, *Suitability*; *see also* subsection (b)(4) of FINRA Rule 0160, *Definitions* and SEC Rule 15c1-1, *Definitions*.

9 *See, e.g.*, Regulatory Notice 10-22, *Obligation of Broker-Dealers to Conduct Reasonable Investigations in Regulation D Offerings*.

buyers do not meet FINRA's definition of an "institutional account."[12] Does that terminology and definition truly make sense in an M&A context? Does a member really have an "account" relationship with a business seller, buyer, or prospect? Is a business seller or buyer's investment objectives or the same relevant in an M&A transaction? Customary contractual obligations owed by a broker-dealer to its client in an M&A engagement may be inconsistent with the regulatory notion that the counterparty to the transaction is also a "customer" of the broker-dealer.[13] Why is a member to deliver a "confirmation" to a business buyer prior to the closing of an M&A transaction?[14] The FINRA Rules, including the proposed LCFB Rules, should be reviewed and reconsidered in light of current day realities, technological advances and expansion of securities-related markets and participants in order to more clearly state their particular scope and application to not-so-routine types of securities transactions and activities.

The regulatory and compliance costs associated with obtaining and maintaining registered status for limited purpose members are prohibitive for small firms with limited purpose business models. Increasing regulatory complexity and higher compliance-related costs are among the reasons frequently cited by members in closing their doors. The tangible impact of this trend is evidenced by the dramatic decrease in FINRA's membership over the last decade, further increasing the proportionate share of regulatory infrastructure costs borne by the remaining member firms, and likely contributing to FINRA's annual operating deficits.[15] As a result, the adverse economic impact on small members and the smaller companies and business owners they serve has grown progressively worse over the years.

For example, the burdens and costs of initial broker-dealer registration and on-going compliance with current SEC and FINRA requirements are quite substantial. In our experience, initial legal, accounting, and compliance-related costs for even the most basic broker-dealers often exceed $150,000 and on-going compliance-related costs can easily be in the range of $75,000 to $100,000 per year. Applying for and obtaining FINRA membership takes a minimum of six months (without taking into consideration the time necessary to ready the initial application for submission) and is frequently longer for non-traditional applicants despite the limited or narrow focus of their proposed activities. The application process is confusing to applicants where the proposed activities do not fit the traditional "investment banking or securities business" paradigm. Commonly during the application process, FINRA requires new applicants to have written supervisory procedures to address a variety of securities-related activities they do not intend to perform under their submitted business plan. Form BD nowhere identifies "investment banking", M&A, business brokerage, or similar concepts as a type of regulated "stand-

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[12] Subsection (c) of FINRA Rule 4512, *Customer Account Information*.

[13] Consider, for example, that many state real estate licensing laws do not contemplate a dual agency relationship and may, in fact, prohibit a real estate broker from representing both the seller and the buyer in a contemplated sale of property. Commonly both securities and real estate licensing apply to the broker in an M&A transaction.

[14] *See* SEC Rule 10b-10 and FINRA Rule 2232, *Customer Confirmations*.

[15] See FINRA's "year in review and annual financial reports", available at: http://www.finra.org/AboutFINRA/AnnualReports.

[illegible] activity in the industry [illegible]. Accrual-based GAAP accounting, quarterly financial reporting, annual audits, a financial and operations principal, anti-money laundering programs, "periodic independent third-party AML testing and SIPC-related compliance and fee assessments are required for all members—even those who never have custody or possession of "customer funds or securities" and thus no apparent investor protection objective is served. We recognize that these particular requirements are largely driven by SEC rules and we strongly encourage FINRA to cooperatively work with the SEC to refine these requirements in the context of this Proposal and other rulemaking efforts that may follow.

Because of these requirements, smaller member firms cannot profitably or cost-effectively provide a limited subset of securities-related services to smaller privately held companies. Their resources are necessarily economically structured to serve larger companies in larger transactions. Smaller companies and their owners cannot afford these professional services, particularly in view of the relatively small size of their desired capital-raise, business sale or M&A transaction. The net result is that the aforementioned stakeholders are unable to obtain limited, more affordable securities related services. Without access to cost-effective services, smaller privately owned businesses are unable to start, grow, and thereby preserve or create jobs that are critical to our national economy.

Helpfully, the LCFB Rules would allow for some simplification and customization of the requirements, but there are still a number of areas in which the proposed rules could be further streamlined and relaxed in order to enhance the regime's utility without sacrificing important investor protections. Accordingly, we strongly encourage FINRA to re-examine the proposed LCFB Rules and all of its existing rules with these considerations in mind.

We also encourage FINRA to work closely with the SEC to review and streamline the financial and operational rules applicable to limited-service broker-dealers, such as LCFBs, and with the North American Securities Administrators Association and state securities regulators, to discuss the rationale underlying the LCFB Rules and to coordinate regulatory reform efforts, so as to reduce regulatory inconsistencies and enhance uniformity at the federal and state levels.

Specific Comments

FINRA requested comment concerning certain specific issues. For convenience of reference, each of those issues is repeated below followed by our comments.

[14] Title 31, Part 1023, *Rules for Brokers or Dealers in Securities*, under the Bank Secrecy Act, defines the operative terms "customer" and "account" for purposes of the Customer Identification Program required under Section 1023.220. Section 1023.100(d) provides, in relevant part, that a "customer" is "a person that opens a new account". Subparagraph (a)(1) provides that an "account" is "a formal relationship with a broker-dealer established to effect transactions in securities, including, but not limited to, the purchase or sale of securities and securities loaned and borrowed activity, and to hold securities or other assets for safekeeping or as collateral." Many, if not most, LCFBs would not have an "account" relationship with customers as so defined.

- Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?

We believe the LCFB Rules provide sufficient protections to customers of LCFBs because the rules are tailored to the business model, risks and circumstances of these firms, as well as to the nature of the relationship and interaction between the LCFB and such customers (or, perhaps more precisely, "counterparties"). Reduced regulatory requirements in the LCFB context are mitigated by the sophistication and active involvement of the parties in these types of transactions, who are assisted by their own internal and external financial advisers and legal counsel throughout the process.

Institutional corporate financing and M&A transactions, to the best of our knowledge, have not historically been the subject of frauds or abuses. Based on the notable absence of reported disciplinary actions, we believe FINRA has not observed significant regulatory concerns with members operating in these limited contexts. Commonly, participants in these types of transactions are represented by counsel and rely on their negotiated contractual remedies if post-closing disputes arise.

We have not identified material gaps to investor protection that would be created by the Proposal. Public and investor (including sellers and buyers of businesses) understanding could be modestly enhanced by requiring delivery of a simple form of disclosure describing the limited scope of securities-related services permitted under the LCFB classification.

With respect to the LCFB Rule 200 Series, *Duties and Conflicts*, we support the more streamlined approach that keys the duties to the actual conflicts and risks of LCFBs. With respect to the LCFB Rule 300 Series, *Supervision and Responsibilities Related to Associated Persons*, we support giving member firms flexibility to tailor their supervisory systems to their business models. This is consistent with the FINRA Rules, as well as the Exchange Act.

With respect to the LCFB Rule 400 Series, *Financial and Operational Rules*, we believe FINRA should work closely with the SEC to modify these existing rules. For example, LCFBs are not permitted to have custody or possession of the parties' funds or securities. The parties typically close these transactions themselves and the purchase price is typically wired between the parties' commercial banks, which are already subject to AML rules and requirements. Typically, LCFBs do not have material financial obligations to their issuer/seller or investor/buyer clients. Accordingly, we see little or no investor protection benefit to require accrual-based accounting under GAAP, periodic financial reporting, audited financial statements, a financial and operations principal qualified under the Series 27 or 28 exams, anti-money laundering programs with periodic third-party testing, or SIPC requirements. These are inherently expensive on-going compliance requirements for which no apparent investor protection benefit is obtained in this context.

With respect to LCFB Rules 1001, et seq. (Arbitration and Mediation), we simply observe that it is unusual for members to include mandatory binding arbitration agreements in their M&A engagements.

With respect to M&A transactions, we note that the SEC staff's issuance of the "M&A Brokers" no-action letter dated January 31, 2014 (the "M&A Broker Letter")[15] implicitly acknowledges that, all things considered, the imposition of SEC broker-dealer registration, FINRA membership, and the associated regulation are unwarranted in the context of qualifying M&A transactions involving privately held companies. However, as discussed below, members may choose not to rely on the M&A Broker Letter for various reasons, so the FINRA Rules as applied in this context could be further relaxed, thereby leveling the playing field and associated regulatory costs among members and their unregistered competitors.

- *Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?*

As explained in our general comments, we believe the FINRA Rules, and particularly the proposed LCFB Rules, should take into greater consideration the comparatively heavier burdens and adverse competitive impacts on smaller member firms handling transactions for smaller privately held companies and owners, as well as other limited non-traditional firms such as those assisting private funds with fund-specific capital-raising activities. These are materially different contexts than SEC-registered offerings involving public companies with retail investors. The elimination or modified application of certain investor protection-based requirements in institutional corporate financing and M&A transactions is typically balanced by, among other things, the sophistication of the parties and their active participation in the negotiation of specific terms, conditions, and contractual remedies; direct access to the issuer's management team and corporate information; and competent internal staffing and third-party advisors to perform their own thorough self-directed due diligence on the issuer/seller.

Moreover, we strongly believe that, to be useful to capital-raising by smaller privately held businesses, placement agents to private funds and others, an investor threshold lower than FINRA's "institutional account" definition must be used. In view of the typical capital needs of smaller private issuers, and private funds relying on the "3(c)(7)" exemption from registration under the Investment Company Act of 1940, as amended (the "*1940 Act*"), we recommend using a "qualified purchaser" standard as defined in Section 2(a)(51)(A) of the 1940 Act,[16]

[15] 2014 SEC No-Act. LEXIS 92 (2014).

[16] As defined in Section 2(a)(51)(A), a "qualified purchaser" means "(i) any natural person (including any person who holds a joint, community property, or other similar shared ownership interest in an issuer that is excepted under section 3(c)(7) with that person's qualified purchaser spouse) who owns not less than $5,000,000 in investments, as defined by the Commission; (ii) any company that owns not less than $5,000,000 in investments and that is owned directly or indirectly by or for 2 or more natural persons who are related as siblings or spouse (including former spouses), or direct lineal descendants by birth or adoption, spouses of such persons, the estates of such persons, or foundations, charitable organizations, or trusts established by or for the benefit of such per-

together with the other categories of investors listed in Rule 5123(b)(1) for purposes of the exemption from the filing requirements imposed under that rule. We believe these types of investors are generally capable of evaluating the relevant risks associated with the types of transactions covered by the LCFB Rules, and so we see no reason why FINRA should adopt a stricter standard for purposes of the LCFB regime than was deemed sufficient by [illegible] to achieve the investor protection goals of FINRA Rule 5123 (which was adopted following SEC approval in 2012).

We encourage FINRA to develop examination modules, document requests, and checklists [illegible] geared to the LCFB Rules (assuming the proposed regime's eventual adoption). By using a more customized approach, we believe the examination process could be more effective and efficient for examiners and members. FINRA has developed excellent instructional materials for members and investors that contain [illegible] through a variety of convenient methods. New instructional materials related to the LCFB audience should be developed.

- *Is the definition of "limited corporate financing broker" appropriate? Are there any activities in which broker-dealers with limited corporate financing functions typically engage that are not included in the definition? Are there activities that should be added to the list of activities in which an LCFB may not engage?*

We believe the proposed functional definition is too narrow because there are related activities commonly performed that should also be permissible and, without which, the public policy rationale behind the Proposal would not be achieved. Notably, the presently listed permissible activities appear to allow only communications with the issuer or business seller, or at most "offers" but no involvement with negotiations or "sales" of securities to qualifying investors/buyers. As proposed in RN 14-09 (emphasis added):

> The term "limited corporate financing broker" would include any broker that solely engages in one or more of the following activities:
>
> - advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;
>
> - advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
>
> - advising a company regarding its selection of an investment banker;

sons; (iii) any trust that is not covered by clause (ii) and that was not formed for the specific purpose of acquiring the securities offered, as to which the trustee or other person authorized to make decisions with respect to the trust, and each settlor or other person who has contributed assets to the trust, is a person described in clause (i), (ii), or (iv); or (iv) any person, acting for its own account or the accounts of other qualified purchasers, who in the aggregate owns and invests on a discretionary basis, not less than $25,000,000 in investments." *See also* related SEC Rules 2a51-1, 2a51-2, and 2a51-3.

- *assisting* in the preparation of offering materials on behalf of an issuer;
- *providing* fairness opinions; and
- *qualifying, identifying or soliciting* potential institutional investors.

We note that all of the listed activities except the last envision limiting the LCFB's communications to those with the issuer or business seller, with the last apparently being limited to solicitations. In our view, these limitations are unworkable in the context of (i) institutional corporate financing; (ii) M&A transactions; and (iii) limited purpose members such as private fund placement agents.

With respect to both institutional corporate financing and private fund placement agents, the LCFB classification would be virtually useless unless the member is also permitted to communicate with prospective investors in a manner that is not confined to "solicitation" activity. In particular, in the institutional corporate financing context, the framework would have very little utility if LCFBs are unable to be actively involved in the discussions, negotiations, and structuring of the contemplated corporate financing transaction. For private fund placement agents, we believe that the LCFB definition should encompass communications with qualified investors and the full range of related activities, including the secondary placement of private fund interests pursuant to Rule 144A under the Securities Act of 1933, as amended.

Similarly, in the M&A context, we believe that LCFBs must be permitted to communicate with and become involved in all aspects of these transactions.[17] Commonly, M&A transactions involve the resale or exchange of outstanding securities, so LCFBs must also be able to communicate with a company's shareholders. A prospective investor or a business buyer may engage an M&A broker to find, screen, evaluate, and approach prospective companies/issuers/sellers. So-called "buy-side" engagements do not appear to come within the scope of permitted activities, but are quite common in the M&A context.

We encourage FINRA to incorporate into the LCFB definition activity-related concepts used in the definition of "M&A broker" in the M&A Broker Letter. In addition, the definition needs to be refined to state clearly that the "institutional investor" requirement does not apply to M&A-related activities, as explained in endnote 3 to RN 14-09. We concur that there is no need to apply any "institutional investor" qualification to M&A transactions where both the seller and buyer are or will control and be actively involved in running the business. Moreover, to do otherwise would, in effect, preclude smaller business sellers and buyers who are not "institutional investors", as presently defined by FINRA, from obtaining these professional services. For example, in a management buy-out and in the formation of an employee stock ownership plan ("ESOP"), the business buyers are typically not "institutional investors". This approach is also consistent with the M&A Broker Letter, which imposes no such conditions.

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[17] *See, e.g.*, the scope and description of M&A broker activities provided to the SEC staff in the incoming submission that resulted in the issuance of the M&A Broker Letter.

- *Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?*

As presently proposed, we believe the permissible scope of activities is too narrow, and the institutional investor threshold too high, for any member to find the LCFB regime to be a commercially or economically attractive alternative. As noted above, additional reforms in the financial and operational rules (which would require coordination with the SEC staff) could result in substantially greater cost savings without diminishing investor protections in the context covered by the LCFB Rules. Current members have already obtained full membership and created the compliance infrastructure necessary to maintain it, so would have relatively little incentive to substantially narrow the scope of their presently permitted activities in exchange for its limited benefits.

We believe many prospective members will still find the new membership application process to be daunting, frustrating, costly, and time-consuming. As a way to measure and address these concerns now and over time, we encourage FINRA to periodically conduct anonymous surveys of new members who have recently completed the process, including questions identifying the types of approved member activities.

- *What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?*

Unless the additional reforms we have described are adopted, the likely economic impact to an LCFB of the adoption of the Proposal would be negligible. As described elsewhere, there are a number of opportunities for meaningful cost savings that are not presently part of the Proposal. We believe these cost savings are very important. The present impact of FINRA's "one-size-fits-all" approach on competition among broker-dealers disproportionately burdens smaller members far more than the larger firms that have the economic resources, business volume, and average transaction size over which to spread their largely fixed compliance costs. These considerations have not been adequately addressed in FINRA's historical cost/benefit and competitive analyses, which we believe need to be as robust as those required of the SEC in a rulemaking context, because of FINRA's delegated authority and legally mandated membership.

On the other hand, the M&A Broker Letter may have a far greater and immediate competitive impact by allowing unregistered firms and individuals to engage in qualifying M&A activities without any of the substantial costs and burdens of SEC registration and FINRA membership. If the LCFB Rules are adopted with the adjustments we are recommending, we believe smaller privately held businesses and their owners could be greatly benefited by the opportunity to receive these limited but more cost-effective services from members. We believe the adoption of the LCFB Rules (to the extent modified along the lines suggested herein) would help to level the competitive playing field with unregistered service providers.

Similar considerations of competitive equity are relevant to private fund placement agents. Many private fund managers are calling on the SEC staff to expand the relief provided in SEC Rule 3a4-1, *Associated Persons of an Issuer Deemed Not to Be Brokers*, from SEC broker-dealer registration (and FINRA membership). This relief would only apply to issuers, creating a serious competitive disadvantage for those members only acting as private placement agents. Placement agents that are not affiliated with any private fund perform virtually the same functions as a private fund manager's employees, but they will remain subject to the FINRA Rules, even while issuers have less need for placement agent services by instead using rapidly evolving general solicitation techniques. If adopted with the recommended modifications, the LCFB Rules would allow these members to more cost-effectively provide unaffiliated placement services.

- *FINRA welcomes estimates of the number of firms that would be eligible for the proposed rule set.*

While we have no statistical data upon which to base a numerical estimate, in view of the frequency of questions we receive pertaining to broker-dealer registration with respect to these limited subsets of securities-related activities, we believe there is a significant number of presently unregistered intermediaries engaged in limited capital-raising and business brokerage activities who, if presented with a straightforward, economically viable alternative, may register with the SEC and become limited FINRA members in order to have greater regulatory certainty with respect to their activities.

- *Proposed LCFB Rule 123 would limit the principal and representative registration categories that would be available for persons associated with an LCFB. Are there any registration categories that should be added to the rule? Are there any registration categories that are currently included in the proposed rule but that are unnecessary for persons associated with an LCFB?*

We strongly encourage FINRA to re-examine how its limited registration categories are aligned for purposes of both the FINRA Rules and the Proposal. Current classifications artificially distinguish between, and require separate examinations for, the sale of corporate stock (Series 62 and 82) and limited liability companies ("*LLCs*") and general partnerships (Series 22). Securities-related activities covered by the Series 22 classification are expressly excluded from the Series 62 and 82 classifications. This distinction was created in a day when "direct participation programs" ("*DPPs*") were a unique type of securities product because of their tax treatment and how they were marketed to retail investors. Today, LLCs are commonly used in all business contexts and are by no means limited to DPPs. Many businesses choose the LLC business structure because of its flexibility in corporate governance, as well as its optional pass-through tax treatment. The net effect of this artificial alignment of classifications is to require individuals to take and pass more examinations than we believe should be required to engage in essentially the same securities-related activities involving corporations, LLCs, or general partnerships. The Series 22 classification could be redrawn by focusing on other characteristics of a DPP "program" that are, in substance, different than a general business operated as an LLC or general partnership.

FINRA's realignment also should address the Series 82 classification's scope. Read literally, the Series 82 only covers sales "as part of a primary offering of securities", and hence does not appear to cover resales of outstanding securities as would occur in a typical M&A transaction. The Series 82 is cited by FINRA's FAQs[18] as an alternative to the Series 79, but without adjusting the scope of the Series 82 to include LLCs and general partnerships, as well as resales of outstanding securities, that alternative compliance approach would not work.

We also encourage FINRA to reassess the scope and application of its Series 79 classification. When developed and even when announced in Regulatory Notice 09-49, *Investment Banking Representative*, this classification was widely expected to serve as the single FINRA classification and examination necessary to engage in all aspects of investment banking activities. To the surprise of many, FINRA's FAQs limited its scope to advisory-only activities and included no selling-related activities. When coupled with the misalignment of the Series 62/82 and exclusion of the Series 22 classifications, noted above, FINRA's FAQs substantially added to the compliance burden placed on smaller firms and their associated persons with respect to M&A transactions for smaller companies. Parts of the Series 79 are relevant to M&A brokers, but the exam presently includes a significant component of public offering-related content that is not relevant in this context. An alternative approach could consider the adaptation of an LCFB examination from existing outlines and content.

We also believe that the Series 24 classification's exam includes a significant component of content that has little or no relevance to the operation of a limited purpose broker-dealer or the activities that would be covered by the LCFB. Instead, we believe that either of FINRA's existing Series 62 or 82 exams (modified to include LLCs and general partnership engaged in a general business and resales), together with the states' Series 63 exam, are adequate to cover the principal and representative activities contemplated by the LCFB classification in so far as they do not involve public offerings. For many reasons few, if any, smaller members or LCFBs would ever consider becoming engaged in a public offering. In contrast, we believe few, if any, larger members who regularly handle public offerings would ever consider becoming an LCFB. Public offerings generally require the commitment of substantial firm resources and are designed for the broadest universe of prospective investors; in contrast, the LCFB Rules are designed for smaller private offerings involving a limited subset of sophisticated investors and privately owned businesses.

Finally, we believe there is no investor protection purpose served by applying the Series 99, *Operations Professional*, qualification or related examination to LCFBs. While relevant in a retail brokerage context, the limited business models of LCFBs would not have the transaction volume or operational components to justify the use of this examination.

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[18] Posted on FINRA's website at http://www.finra.org/Industry/Compliance/Registration/QualificationsExams/Qualifications/FAQ/P124190.

- *Should principals and representatives that hold registration categories not included within LCFB Rule 123 be permitted to retain these registrations?*

We believe it serves no investor protection principle to prevent securities industry professionals from retaining validly held qualifications permitting broader activities while they remain engaged in a subset of those activities. Associated persons do not lose their past training, knowledge and, as importantly, experience and, if they rejoin a fully-registered member, will resume the continuing education training pertaining to the broader activities.

- *Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?*

The term "recommendation" is not expressly defined by FINRA; instead, general guidance as to what may constitute a recommendation is provided in a number of largely unrelated interpretations, as well as court opinions (usually addressing fraudulent conduct), creating no bright lines and making the legal analysis of the particular facts and circumstances challenging.[19] Often, out of an abundance of caution there is a tendency to treat every discussion regarding a securities transaction with a potential counterparty that is not itself a broker or dealer as a "recommendation" to a "customer". As discussed above, the LCFB classification would have little to no utility if it did not include the ability to communicate with prospective investors/buyers, and for buy-side M&A engagements, to communicate with prospective sellers. Such communications with a prospective investor/buyer/seller specific to a capital-raising offering or M&A transaction could be construed, perhaps over-broadly, as a "recommendation".

For this and the reasons noted in our general comments, we strongly encourage FINRA to more clearly define a "recommendation" and reconsider its definition of "customer" in the LCFB context, as reflected in LCFB Rule 209. Given the limited scope of LCFB activities, there is no traditional customer relationship and no "account" to service and, accordingly, we do not believe that communications by LCFBs with these types of investors and in the context of the limited transactions covered by the LCFB regime should constitute a "recommendation".

With respect to LCFB Rule 211, reference to or the use of a "customer profile" or an "investment strategy" would not be relevant. The prescribed content of such a "customer profile" is incongruent with the predicate for the LCFB Rules, particularly with respect to M&A transactions. Similarly, the prescribed customer information required by LCFB Rule 451(b) should be modified to reflect the types of parties who would be served by LCFBs. We believe the same would be true for other limited purpose, non-traditional members such as private fund placement agents.

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[19] *See* FINRA Rule 2111; *see also* FINRA's "Frequently Asked Questions: FINRA Rule 2111 (Suitability)" and FINRA Regulatory Notices 12-55, 12-25 and 11-25.

Similarly, the "know your customer" and customer suitability obligations are of far less relevance in the context of institutional corporate financing activities and private fund placement activities, and wholly irrelevant to M&A transactions. Potential investors in "3(c)(7)" funds are, by virtue of the exemption's conditions,[20] limited to qualified purchasers. Subscription agreements and purchaser questionnaires typically include, among other things, representations and warranties attesting to the conditions defining a qualified purchaser.

Institutional corporate financing and M&A transactions are commonly heavily negotiated. Unlike a small retail investor, institutional investors and high net worth individuals have sufficient economic bargaining power to exert substantial influence over, if not dictate, the terms and conditions they will either offer to or accept from the issuer. In this context, there is no doubt that the investor/buyer is exercising independent judgment and fully self-evaluating investment risks. Accordingly, in the LCFB context there is little investor protection purpose served by these rules. Further, in the M&A context, the prospective business buyer will do its own self-directed pre-purchase due diligence, will assess whether the target business comes within its strategic, financial, or business objectives, strategies, and plans, will determine the price and terms it is willing to offer, and will control the business after the transaction's closing.

We recommend that LCFB Rule 221 recognize that in the LCFB context an introductory communication, summary in nature, is typically produced, which is initially distributed to prospective institutional investors or business buyers and used to determine if they have any interest in a potential transaction. As written, LCFB Rule 221 says "no" communication may "omit any material fact or qualification". Inherently, by design, these summary documents do not contain all material facts and circumstances that may pertain to the issuer/seller. Prospective institutional investors and business buyers want a condensed summary to determine, as an initial matter, whether they wish to devote any additional time or resources to considering whether a potential transaction is of any interest. Typically, these summary documents are expressly qualified in their entirety by the extensive information and documentation that will be directly accessible, subject to a confidentiality agreement, by each prospective institutional investor/buyer as an integral part of its self-directed pre-purchase due diligence. Direct access is provided to the issuer/seller's management team and commonly electronic access to material documents as identified by the issuer/seller and its counsel.

In the M&A context, it is also common for the seller's written materials to include forward-looking information about such matters as projected sales growth, including opening new markets and developing new products. This type of forward-looking information is self-evaluated by the prospective business buyer as part of its due diligence process. LCFB Rule 221 should not prohibit this type of information from being provided where the prospective institutional investor or business buyer is capable of self-evaluating this type of forward-looking information.

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[20] *See* Sections 2(a)(51)(A) and 3(c)(7) of the 1940 Act, and SEC Rules 2a51-1, 2a51-2, and 2a51-3.

- *Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014, impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?*

We believe it is likely that some, but not all, LCFB-eligible persons will choose not to become SEC-registered broker-dealers and, consequently, FINRA members. The M&A Broker Letter and similar prior SEC staff no-action letters provide the Staff's view as to the circumstances in which broker-dealer registration should not be required.[21] However, these no-action letters have significant limitations, both as a legal and practical matter.[22] Importantly, the M&A Broker Letter does not allow for general capital-raising activities where no change of control occurs. Hence some members are certain to remain registered (and new applicants may apply for FINRA membership) in order to engage in both types of securities-related activities. The FINRA Rules should recognize and give appropriate effect to the reality that members' M&A-related services within the scope of the no-action relief compete with large numbers of unregistered M&A brokers who rely on the SEC staff no-action letters. Adopting the LCFB Rules, with our proposed modifications, would help to balance the competitive circumstances as between registered and unregistered M&A brokers.

We also believe that some members could choose to bifurcate their business model by moving those activities falling within the scope of the M&A Broker Letter into an unregistered affiliate. Most firms will have dually employed associated persons and so NASD Rule 3040, as currently in effect, will likely require the registered member to supervise the private securities transactions conducted through the unregistered affiliate.[23] The unregistered affiliate could pay its affiliated member for the cost associated with its supervision, but the transaction-related revenue is not required to be paid to the member under this rule. Accordingly, members

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[21] See, e.g., M&A Broker Letter; Country Business, Inc., 2006 SEC No-Act LEXIS 665 (2006); [illegible], 1987 SEC No-Act LEXIS 2517 (1987); and International Business Exchange Corp., 1986 SEC No-Act LEXIS 3065 (1986).

[22] The SEC's general rules, specifically Rule 202.1(d), state that a no-action letter only expresses the SEC staff's view on the question presented—in this case the need for an M&A broker to register with the SEC. It is merely an interpretation that can be later modified or withdrawn. See the SEC's description of no-action letters on its website at http://www.sec.gov/answers/noaction.htm. Courts may give the SEC's no-action letters some deference but the staff's position is not legally binding on anyone, not even the Commission. See New York City Employees' Retirement System v. SEC, 45 F.3d 7 (2d Cir. 1995).

[23] As a general matter, and particularly in the context of the LCFB Rules, we strongly encourage FINRA to reconsider and reexamine NASD Rule 3040 to better acknowledge and align the rule with present day realities in which particular employees may be dually employed by individual affiliates within a multi-service organization, many of which affiliates are separately regulated under different regulatory regimes and subject to different regulatory requirements. Requiring a FINRA member to "supervise" the employee's participation in securities-related activities performed in the context of their employment with a separately regulated (or exempt) affiliate as if the activity were performed on behalf of the member, and to "record" resulting securities-related transactions on the FINRA member's books and records, is not practical or appropriate and indeed may be inconsistent with the affiliate's applicable regulatory requirements.

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are likely to find a significant cost-savings from bifurcating their M&A business with respect to privately held company transactions.

We note that an important unresolved question about the M&A Broker Letter is whether a FINRA member could pay a referral fee to an unregistered M&A broker for transactions coming within the scope of that no-action letter. In 2009, FINRA proposed to replace NASD Rule 2420 with a new FINRA Rule 2040 that would, in essence, allow payments or sharing of compensation with unregistered persons when, based on SEC rule or guidance, broker-dealer registration would not be required. The modernization of NASD Rule 2420 is long overdue. NASD Rule 2420 was first written and adopted for entirely different purposes and a literal reading of the rule today barely hints at its current application, creating a compliance trap for the unwary. While the proposed FINRA Rule 2040 could itself be written far more clearly, its reproposal is strongly encouraged.

Conclusion

We greatly appreciate the opportunity to share our thoughts and comments on the Proposal. FINRA has taken an important step forward in modernizing its rules in light of the dramatic shift in the demographics of its members and in recognition of the pending revolution in issuer-direct capital raising activities facilitated by The Jumpstart Our Business Startups Act of 2012 ("JOBS Act"). The 2013 SEC report, *Capital Raising in the U.S.: An Analysis of Unregistered Offerings Using the Regulation D Exemption, 2009-2012*,[24] documents the leading edge of these impending changes. Notably, the report's Summary of Main Findings highlights, among other points, that: "Only 13% of Regulation D offerings since 2009 report using a financial intermediary (broker-dealer or finder)". Neither this statistic nor the JOBS Act's innovations in general solicitation and crowdfunding bode well for the future revenues of FINRA's members, particularly smaller members who are still willing to undertake Regulation D private offerings. We are concerned that these developments may result in the further decline in FINRA small firm membership.

We believe that the Proposal is the first step in the right direction. We hope these comments will be helpful, both in consideration of the Proposal and in FINRA's retrospective rule review process. We are available to meet and discuss these matters with FINRA and to respond to any questions you may have. We greatly appreciate your consideration and look forward to future opportunities to provide further input.

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[24] Available on the SEC's website at http://www.sec.gov/divisions/riskfin/whitepapers/dera-unregistered-offerings-reg-d.pdf

Very truly yours,

/s/ Catherine T. Dixon
Catherine T. Dixon, Chair
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April [illegible], 2014

Ms. Marcia E. Asquith
Senior Vice President and Corporate Secretary
FINRA
pubcom@finra.org

Re: Re: GENERAL COMMENTS ON PROPOSED RULE SET FOR LIMITED CORPORATE FINANCING BROKERS

Dear Ms. Asquith:

I commend FINRA for proposing a separate rule set that would apply exclusively to firms that meet the definition of limited corporate financing broker ("LCFB"). This new rule set potentially could streamline regulation specifically for an LCFB's business activities. However, I think that more consideration and work are needed in order to implement such a rule set. Many of the concerns have already been addressed by others. I will merely highlight a few that are of particular concern.

The proposed rule set seems overly restrictive without much by way of benefits to the LCFB.

I must assume that the scope of advising a company regarding the purchase or sale of a business or assets, corporate restructuring, and/or divestiture or merger, would include a valuation analysis and the analysis of strategic alternatives under the proposed rule set. More typically, such advice is to assist companies in developing strategies for transferring ownership within the family, sale to shareholders/partners, sale to employees, sale of business or merger, liquidation, and recapitalization.

Such advice may also include "show-me" type valuations that would not be for purposes of a transaction. Among these are valuations for estate and gift tax purposes, employee benefit plans, disputes, wealth transfer strategies for the closely-held business owner, and so forth.

A particular area of concern with the proposed rule set for the LCFB falls under the basic definition of an LCFB, which seems to restrict activities to advising an issuer or company and/or its board of directors. Any qualifying, identifying or soliciting of investors would be limited to institutional investors as defined under LCFB Rule 016(g)(1). The $50 million minimum asset requirement for persons (entities) other than institutions is problematic.

I highlight the following Request for Comment: *Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?*

Page 2

The advisor generally does not make specific recommendations to the issuer, company, or board. The advisor instead assists the customer in making his, her, or its own decisions. For instance, a fairness opinion specifically states that "this fairness opinion is not a recommendation to buy or sell."

Accordingly, under the proposed rule set, an LCFB would be able to advise an issuer, a company or its board, but would not be able to qualify prospective investors unless the investors met the institutional investor qualification. This would limit the scope of an LCFB's services and it would be hard to justify a success fee upon the closing of a transaction, unless the prospective investor qualified as an institutional investor.

Before choosing to be treated as an LCFB, I would like to see a better balance between activity restrictions and benefits to the Member. This could be accomplished by either reworking the rule set by loosening the restrictions on an LCFB's business activity or significantly reducing the FINRA imposed costs of doing business – membership fees, SIPC and fidelity insurance requirements, and the need for an annual audit.

I hope my comments on the proposed rule set are helpful.

Richard B. Dole, ASA, CFA
Chief Executive Officer
Dole Capital, LLC

Dear Ms. Asquith,

My firm is a FINRA member specializing in placement agent services dedicated to the singular goal of capital raising for investment managers so they could focus on creating returns and not on the fundraising. We raise institutional capital across highly differentiated funds, including private equity, real estate, real assets and hedge funds.

I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD) which are attached. I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

With kind regards,

Leanne

LEANNE ERICKSON
Chief Compliance Officer

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in placement agent services to institutional investors. I do not carry or maintain customer accounts, hold or handle customer funds or securities. I do not accept orders from customers to purchase or sell securities as a principal or as an agent for any customer. My customers are actually Investment Managers, Fund Sponsors or GP's not retail Investors. I believe that FINRA, MSRB, and the SEC all wish to make their own lives easy be closing their eyes to the relevance of rules for distinct sub-sections of their member universes. A one size fits all mentality at FINRA requires a standardization of actions/reports to please Congress regardless of their relevance, expense to their members or protection to investors.

I was hoping to see regulations that more reflected my business model in your proposed regulation changes for Limited Corporate Finance Brokers. As things stand your proposed changes entirely miss the mark and there is no reason for any placement agent to consider a change in registration.

I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support. (see attached)

Best wishes,
Brian X. Fitzgibbon

Fitzgibbon Toigo Associates, LLC (FINRA/SIPC/MSRB member)
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Ours is a small firm that already limits itself to advisory services for direct private placements and if the LCFB were changed as follows would certainly opt to change the firms status

- Add Accredited Investors as part of the customers the LCFB can serve. The current customer definition is too narrow
- Because the LCFB would not carry customer accounts or deposits, as is the case for our firm today, eliminate the costly PCAOB Annual Audit, the SIPC insurance and Fidelity Bond requirements
- End the Net Capital requirement since the firm is not engaged in any business operation that would require the protection by its capital base.
- And finally, allow LCFB's whose registered representatives and principals are series 7 and 24 respectively when they become LCFB's to return to full broker status, without having to reapply for membership, should their business model require them to do so

Thank you for providing the opportunity to comment on the proposed rules,
Weldon G. Fleming, Jr.
Principal
LWTI Capital, LLC

April 23, 2014

To: Maria E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006

Re: Proposed Rule Set for Limited Corporate Financing Brokers (Regulatory Notice 14-09)

General Observations

I am encouraged by FINRA's proposed activities for Limited Corporate Financing Brokers ("LCFB"). I believe LCFB may meaningfully increase the alternatives for competent representation available to small businesses seeking to sell themselves or raise capital. However, limiting investors and acquirors to "institutional investors" undermines what FINRA's proposed rules are seeking to accomplish for the following reasons:

1) LCFB and their clients cannot reasonably know upfront without potentially negative consequences if certain potential buyers/investors meet the institutional investor qualification before or even after they are solicited. While it is common in the private placement context to pre-qualify accredited investors by asking that such investors complete a questionnaire to certify their "accredited investor" status prior to providing offering materials, a buyer or investor may be unwilling to certify to the much higher institutional investor status prior to receiving any information on the transaction. The buyer of a small company in many cases may be a comparable size company or a competitor. The seller will likely never know the financial position of the buyer in an all cash for stock transaction. The seller is primarily concerned with the buyer's ability to pay the purchase price and the terms of the transaction. If the deal is structured as a cash and stock deal or an all stock deal, the seller would in fact have reasonable access to the buyer's financials and could determine if the buyer has $50 million in assets, however, the timing of determining this could be a month or more after the LCFB has been engaged by its client. Further, the institutional investor status of the investor is only relevant to the LCFB and no other party to the transaction. There is no "investor protection" rationale in the proposed rule for requiring institutional investor status rather than accreditor investor status. Under U.S. securities laws, accredited investors are assumed to be both informed and sophisticated enough not to need the protections afforded to other investors under the federal securities laws.

2) I believe that the proposed rules as currently written would prohibit a LCFB from representing small companies unless the LCFB agreed upfront with the prospective client as to what purchasers/investors would be solicited and that list would be limited to institutional investors. This does not seem practical given that a prospective buyer/investor list is usually not compiled until well into any engagement and often concurrent with or after the LCFB representatives having done a substantial portion of their financial and business due diligence including thoroughly assessing the competitive landscape, which in many cases will undoubtedly identify potential buyers/investors. For a small company seller, limiting the landscape of buyers (for the sole purpose of allowing the LCFB to be engaged and participate in the transaction for compensation) is a disadvantage to the selling client with no offsetting benefit. The smaller the pool, the less likely the company will be sold which could negatively impact job growth, and future investment in the economy.

If I am the prospective client and the LCFB "honestly" explained to me this limitation as to who can be solicited, and the lack of any offsetting benefit, I would not hire the LCFB. The client could always turn to a traditional broker-dealer to seek representation, use a M&A Broker under the recent SEC no-action letter, assume no advisory representation, use legal counsel only, or circumvent or disregard the rules entirely.

Putting aside the larger broker-dealers which generally would have limited interest in representing companies with an enterprise value of less than $25 million, many of the regional broker-dealers currently have minimum fee requirements that are still cost prohibitive to a small company. Even if these broker-dealers accept the assignment, it is possible the company and the engagement will not get the senior level attention that is warranted and the client expects and is paying for.

3) Even assuming that a seller and its advisor can determine that all the potential buyers to be solicited are institutional investors, what happens if and when the company receives an unsolicited offer from a non-institutional investor? What is the LCFB responsibility in this scenario? Would the LCFB still be paid even if the company sells to the unsolicited party? This is problematic.

Summary and Suggestions

While I appreciate the term "accredited" has been diluted somewhat by the overall growth in the economy and inflation, it is the standard long established for registered broker-dealers with respect to selling private placements. Accredited investors are presumed under U.S. securities laws to be sophisticated enough to not need the protections afforded other investors under U.S. securities laws. It is the role of the U.S. Congress and the SEC to determine what the appropriate thresholds should be for the accredited investor standard to balance the goals of investor protection, the public interest and the economy. Section 413(a) of the Dodd-Frank Act, requires the SEC undertake a review of the definition of accredited investor as it applies to individuals every four years and make adjustments as the SEC deems appropriate for protection of investors, in the public interest and in light of the economy. From the proposed rules, FINRA is proposing to dictate what level is appropriate for investor protection, rather than Congress and the SEC. It is hard for me to understand why a sole practitioner like myself with twenty-five years of investment banking experience with three bulge-bracket firms is being asked to submit to a higher standard. Is not a large part of your concern addressed with the registration requirements (Series 24,79, etc.) that LCFB principals and employees must adhere to? Registration and continuing education are the salient factors FINRA uses to determine minimum competency with respect to all registered broker- dealers. I believe that all advisors, whether associated with a bulge-bracket firm or sole practitioner like myself should be held to the same standard, no less or no more, in the pursuit to offer their clients only world-class advice.

While it is not my intent to pursue non-institutional accredited investors, there are many very sophisticated and wealthy investors that I believe should not be excluded in executing an M&A transaction or private placement. You may consider establishing a new definition for "non-institutional accredited investor" with a minimum net worth above accredited but below institutional.

You will be able to weed out many of the "bad actors" through your proposed registration of LCFB. Unfortunately, there will always be those individuals that have no respect for the law.

Furthermore, the SEC no-action letter dated January 31, 2014, is more favorable to brokers than the proposed FINRA rules. I believe, with respect to the sale of a company, many M&A brokers may take comfort in the SEC no-action letter and selectively disregard any new FINRA rules given they are, as written, more restrictive.

Inadvertently, the FINRA rules as proposed may actually discourage companies from hiring a LCFB given the inconsistencies between the two sets of rules for certain of the same activities. It is reasonable to assume that counsel to a seller will advise their client not to hire the LCFB given the inconsistencies. These inconsistencies increase risk, and increased risk has a cost. Does a seller need to be concerned with remedies that may accrue to a buyer if the advisor on the transaction relies on one set of rules and not the other? If you are an owner of a small company that has been in the family for generations and have made the important decision to sell, would you risk hiring a broker that is potentially restricted in his ability to maximize shareholder value and that may be subject to litigation/enforcement from FINRA and the SEC. Is it conceivable the LCFB would advise his client to not solicit a certain party in the best interest of the client because he realizes the party is not an institutional investor? The rules would dictate that the LCFB not act in the best interest of his client. This creates an illogical result.

I hope my comments will encourage FINRA to modify the definition of institutional investor if it is unwilling to establish parity among all providers of financial advice.

I would be happy to discuss my comments and suggestions with you.

Sincerely,

Saverio Flemma
SF Advisors, LLC
sav@sfadvisors.co
(917) 623-9159

To whom it may concern,

As the owner of a small limited BD that would likely qualify as a limited corporate financing broker, I would greatly appreciate if you would consider lowering the financial burden on such entities.

For example, since these entities (like mine) don't carry customer accounts, the fidelity bond should no longer be required, the net capital requirement should be eliminated (or substantially lowered), and the annual financial/AML (anti money laundering) audits should no longer be required (as the firm poses no financial or systemic risk on anyone else nor does it deal with cash deposits/customer accounts). In fact, the biggest regulatory cost for small BDs, such as mine, is the annual financial/AML audit, especially with the new PCAOB regulations that are coming into effect later this year.

I believe that these changes won't prevent companies like mine from still being compliant with FINRA rules, but will certainly help out by eliminating unnecessary cost burdens.

Thanks in advance for your consideration.

Regards,
Eli

Eli Gabay
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April 28, 2014

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

Re: Limited Corporate Financing Brokers RN 14-09

Dear Ms. Asquith,

HighBank Securities, LLC (CRD 153796) welcomes the opportunity to comment about the proposed rule set for Limited Corporate Financing Brokers. Our business consists mainly of investment banking advisory services, namely mergers & acquisition advisory services as well as assisting clients in raising capital, mainly from parties that qualify as institutional investors. It is our view that our firm would fit within the proposed definition of an LCFB.

Through the creation of the Series 79 (Limited Representative – Investment Banking) in 2009 and now this proposed rule, it appears that FINRA is seeking to tailor its regulatory requirements to fit the activities performed by firms like ours. We welcome this movement. That said, we believe that the proposed rules do not go far enough and still result in a level of regulation and oversight that remains onerous and contains specific requirements that are unnecessarily burdensome to our business. Furthermore, the recent SEC Staff no-action letter issued to Faith Colish, et al., threatens to undermine FINRA's efforts to encourage registration by firms that conduct corporate finance business.

While the proposed LCFB rules eliminate a few of the regulatory burdens imposed upon firms like ours, it is our view that the rules do not go far enough. Specifically:

- LCFB's would still be required to participate as members of SIPC, whose specific mission is to protect clients assets held by broker-dealers. LCFB's are not permitted to hold client funds or securities and, accordingly, maintaining the requirement of SIPC participation makes little sense.[1]

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[1] Indeed, it is senseless that the SIPC applies to our firm <u>presently</u> as our firm holds no customer funds or securities and, accordingly, there is no scenario in which customers of our firm – the contingent that SIPC is chartered to protect – would benefit from SIPC's existence. Compulsory membership in SIPC results in a tariff on our firm's revenues that is patently unfair. This unfairness would be continued under the proposed LCFB framework.

- The requirement of an annual audit by an independent accountant and bi-annual AML independent reviews are of negligible value but material cost. Firms like ours expend considerable time, effort and expense to comply with the requirements of these annual reviews. These audits provide the investing public with no identifiable benefit.
- The rules would continue to require LCFB's to maintain a fidelity bond with coverage of at least $100,000, again at significant annual cost to the firm. For the reasons mentioned above – we hold no customer funds – the fidelity bond requirement makes little sense and we would request a reconsideration of its need.

For these reasons and others, the LCFB proposed rules do not represent a meaningful reduction in our regulatory burden and, accordingly, it is doubtful whether we would elect into the LCFB category, especially as the LCFB precludes raising capital from accredited investors. While the vast majority of our targeted investors qualify as institutional investors, we sometimes reach out to a network of high-net worth accredited investors, an action that would be prohibited by the LCFB proposal.

FINRA requested comments on certain specific issues. Our view on the most relevant issues for us is below:

- *Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?*

  Our view is that the proposed rule set continues to provide sufficient protections for customers of an LCFB. In fact, there are many rules and regulations that would unnecessarily apply to an LCFB that provide no meaningful protection to LCFB's customers (SIPC, fidelity bond, annual audit).

- *Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?*

  The proposed rule set allows LCFBs to solicit institutional investors but not investors that meet the definition of accredited investors. This is a distinction that should be reconsidered, as accredited investors are deemed to have a level of sophistication that allows them to sufficiently analyze the risks associated with investing.

- *Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?*

  Yes! One of our great frustrations is that our firm has elected to formally register as a broker-dealer, at significant cost and burden, while other firms with whom we directly compete have not properly registered as broker-dealers (with no negative consequences). It is our opinion that these firms will continue to operate without proper registration despite the LCFB proposed rule set.

- *What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?*

  We don't see any significant economic impact to an LCFB. The costs associated with being an LCFB are marginally lower than the costs of being a broker-dealer today, but, as mentioned, the proposed on-going costs are still significant.

- *Should principals and representatives that hold registration categories not included within LCFB 123 be permitted to retain these registrations?*

  Yes. We believe that representatives of an existing broker dealer that elects LCFB status should be allowed to continue to hold all of the registrations categories that they held prior to the election. This protection seems justified in that future rule changes could occur or the firm could decide the election was not worthwhile and desire to convert back to a full broker-dealer without the "penalty" of having to re-certify.

- *Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?*

  Aside from advice provided to our buy-side and sell-side merger and acquisition clients, our firm does not make recommendations to clients or customers to purchase or sell securities and, in fact, that activity (aside from in the merger and acquisition context) does not in our opinion seem appropriate for an LCFB.

- *Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014, impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?*

  The no action letter represents a shift in regulation that is significantly more meaningful than the incremental changes made in the LCFB proposed rule set. Our firm derives the majority of its revenue from activities consistent with those set forth in the no-action letter. We are currently analyzing the no-action letter in detail, but our preliminary conclusion is that the majority of our business would no longer be subject to FINRA regulation as a result of the no-action letter. Although this would represent welcome financial relief, we believe this is a significant step backward in ensuring the quality of advice and protection provided by existing regulations and as such encourage FINRA and our membership to work hard to have the ruling reversed.

  Some might argue that unlicensed "M&A brokers" cause no harm and therefore they should not be subject to regulation. We disagree and provide two real examples.

First, assume a John owns a business worth $10 million and the vast majority of his net worth and life's earnings are tied up in the business. John, despite his significant net worth, is unsophisticated with all matters financial. John hires an unlicensed M&A broker who due to poor advice and shoddy execution proceeds to sell his business for half of what it is truly worth. John has lost $5mm and is by our way of thinking significantly "harmed."

Second, under the same fact pattern John's consideration for the sale of his business is stock in the acquirer and not cash. The stock is subject to a lock-up and other liquidity limitations that require John to hold the stock for 24 months post-closing. The M&A broker advises John that there is no real risk to holding the stock and is not able to even quote appropriate studies and current market data regarding the liquidity discount John should assume if he decides to take the stock as consideration. During the 24 month period the acquirers stock drops 50%. John is certainly harmed by having hired the unlicensed, unregulated M&A broker.

It is our opinion that the proposed rule set will not encourage firms like ours to register as an LCFB. In fact, the proposed rule set, coupled with the no-action letter, makes it even more likely that many firms will continue to "roll-the-dice" and perform their services illicitly outside voluntary FINRA and SEC oversight, risking the livelihoods of countless, financially unsophisticated business owners.

Thank you for allowing us to provide our comments. Please don't hesitate to contact us if you have questions concerning our response.

Very truly yours,

Stephen R. Gaines
Managing Director/CEO

Dennis W. O'Neill
Managing Director/COO

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

At Havener Capital Partners, my sales colleagues and I are registered reps with FINRA member firm Compass Securities Corporation. Havener provides outsourced sales and marketing services to investment managers targeting institutional investors. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Thank you for your consideration.
Stacy Havener

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Colorado Financial Service Corporation
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March 21, 2014

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

RE: Regulatory Notice 14-09; Limited Corporate Financing Broker

Ms. Asquith:

Thank you for the opportunity to comment on the proposed Rule Set for Limited Corporate Financing Brokers.

Colorado Financial Service Corporation is a full service general securities firm that includes an investment banking division. We have been involved in investment banking transactions since 2008 and conduct approximately 50 transactions per year. We operate on the independent contractor model that has proved to be beneficial to both our Firm and our registered representatives and very attractive to investment banking professionals. For the most part, our clients are private corporations seeking both mergers and acquisitions services as well as capital in the form of both debt and equity.

In reviewing this proposal, we could not help but look back at the rollout of the Series 79 Investment Banking registration[1] and the unintended consequences it placed on firms. FINRA did not provide clear cut definitions that allowed firms to make reasonable interpretations of the rule and reasonably expect to have a FINRA examiner make a similar interpretation. From our own experience, FINRA staff, including the general counsel's office could not provide a definition of the term "facilitate" as used in the rule. I see similar confusion in the proposed rule set that will lead to very differing interpretations of the rule when it comes to application. Though not FINRA's responsibility, the US Securities and Exchange Commission's letter to exempt most mergers and acquisitions brokers from any registration adds to the confusion and creates an atmosphere of "no direction" when viewing the regulatory scheme surrounding securities registration. We see confusion in the proposed rule set that will lead to very

[1] **1032(i) Limited Representative—Investment Banking** (1) Each person associated with a member who is included within the definition of a representative as defined in NASD Rule 1031 shall be required to register with FINRA as a Limited Representative—Investment Banking and pass a qualification examination as specified by the Board of Governors if such person's activities involve: (A) advising on or facilitating debt or equity securities offerings through a private placement or a public offering, including but not limited to origination, underwriting, marketing, structuring, syndication, and pricing of such securities and managing the allocation and stabilization activities of such offerings, or (B) advising on or facilitating mergers and acquisitions, tender offers, financial restructurings, asset sales, divestitures or other corporate reorganizations or business combination transactions, including but not limited to rendering a fairness, solvency or similar opinion.

differing interpretations of the rule when it comes to application. We believe FINRA's mission is being compromised to retain firm and representative registrations.

As an example, the proposed Rule 016(h)(1)(F) and footnote 3 of Regulatory Notice 14-09 indicates that qualifying, identifying or soliciting securities to potential institutional investors by LCFB will be permissible. This creates confusion. Because, it appears that, pursuant to 016(h) (F) and the footnote, LCFB will be allowed to engage in traditional broker-dealer's activities to institutional investors. Allowing solicitation of institutional investors creates confusion and further blurs the line between a normal broker-dealer and an LCFB.

By way of response, I have repeated your specific requests:

1. *Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?*

   a. The term "customer", pursuant to the proposed rule LCFB 016(d), means any natural person and any entity receiving *corporate financing services* from a limited corporate financing broker. "*Corporate Financing services*" is a broadly used term, and typically includes capital raising activities which should be outside the scope of an LCFB.

      However, FINRA did not clearly indicate whether capital raising activities would be allowed by LCFB in the proposed rule. We propose, to make reasonable interpretations of the rule, either: (i) to clarify the term "Customer" by stating "any natural person and any entity receiving or having an engagement with LCFB for the services listed, identified or defined in LCFB Rule 016(h); or (ii) to provide FINRA's view or expectation on capital raising activities by LCFB; a bright-line of demarcation.

   b. According to the proposed rules, registered associated persons of LCFB will be subject to FINRA Rule 3270. However, the proposed rule is silent on the activities which are currently subject to NASD Rule 3040, private securities transactions.

      We request; (i) FINRA's view on securities transactions of which associated persons of LCFB participated in; and (ii) to provide FINRA's interpretation of the following circumstances.

      - Whether such activities will be viewed as the business activity outside the scope of the relationship with the LCFB firm, therefore will be subject to FINRA Rule 3270;
      - When/if an associated person of LCFB is also registered with an affiliated full service broker-dealer for the purpose of conducting traditional brokerage activities;
      - When/if an associated person of LCFB is also registered with an unaffiliated full service broker-dealer for the purpose of conducting traditional brokerage activities; and
      - When/if an associated person of LCFB refers a customer (either institutional or non-institutional customers) to a broker-dealer (either affiliated or unaffiliated) for capital raise of an issuer of which the LCFB firm engaged in one of the activities of 016(h) (1).

   c. The proposed rule 221 appears to disregard the existing rules concerning communications with the public:

      - The one-year filing requirement appears to be waived.
      - There appears to be no required supervision of communications

The rules appear to be vague and contradict their intent. The rule proposal allows capital raise transactions to institutional clients and yet the rules appear to match retail clients. An LCFB should be limited to services only and NO transactions, institutional or otherwise.

There is no reason to exempt an LCFB from the annual requirement for the AML independent examination. The existing exemption applies to Firm's that do not have *any* transactions. FINRA propose to allow transactions, though institutional which we believe are contrary to AML rules.

2. *Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?*

   a. The proposed rules appear to have removed or limited LCFB's and its associated persons' direct contact with general public customers (aka retail customers). However, LCFB's and/or its associated persons' certain conduct may still impact general public customers.

      As an example, LCFB can possess non-public information that may impact, either positively or negatively, an issuer's stock price, when/if the issuer is a publicly traded company. Therefore, LCFB's and its associated persons' securities transactions need to be scrutinized and supervised by a qualified principal.

      Accordingly, we propose to require LCFB's and their associated persons' compliance with NASD Rule 3050(C) and (d). In addition, due to the fact that the investment bankers do often receive stocks or equity shares as compensation from the issuer, we suggest to modify personal securities related rules similar to 204(A)-1 of the Investment Advisers Act of 1940.

   b. There should be a bright-line of distinction between an LCFB and any other broker-dealer firm registration category. I would repeat response to item 1 above. As an example, LCFB Rule 209; LCFB Rule 211; LCFB Rule 451 (b); LCFB Rule 512; LCFB Rule 900 (c); we believe, contradict the spirit and intent of the rule; especially as they may relate to individual customers rather than entities which are the norm in corporate finance.

3. *Is the definition of "limited corporate financing broker" appropriate? Are there any activities in which broker-dealers with limited corporate financing functions typically engage that are not included in the definition? Are there activities that should be added to the list of activities in which an LCFB may not engage?*

   a. NASD Rule [illegible] requires an individual who provides investment banking services to register as a Limited Representative-Investment Banking. The rule also defines what activities are to be provided by such individual. We are asking FINRA to clarify whether registered representatives of LCFB will also be deemed a Limited Representative-Investment Banking or not. If yes, why does FINRA use two different terms Investment Banking and Limited Corporate Financing. The description looks very similar to a Series [illegible] registration. If not, what is the difference?

   b. The proposed LCFB [illegible] currently states that "advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities." Will the marketing of securities of or for an issuer be permitted for LCFB? If yes, we propose to add as such in the proposed LCFB [illegible]. If not, also state as such.

c. **LCFB should be also prohibited from raising capital from any source what-so-ever; debt or equity. To do anything less would compromise the whole intent of the rule set.**

4. *Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?*

Adopting an LCFB format should be strictly for an investment banking firm that limits itself to mergers and acquisitions transactions, no capital raise whatsoever and other usual and normal fee-based investment banking consulting or drop the idea all together.

5. *What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?*

Carving out the LCFB would create an un-level playing field for existing broker-dealers who conduct corporate finance activities in addition to their other lines of business.

6. *FINRA welcomes estimates of the number of firms that would be eligible for the proposed rule set.*

An M & A firm would more than likely use the SEC's exemption and not register.

7. *Proposed LCFB Rule 123 would limit the principal and representative registration categories that would be available for persons associated with an LCFB. Are there any registration categories that should be added to the rule? Are there any registration categories that are currently included in the proposed rule but that are unnecessary for persons associated with an LCFB?*

The IB (Series 79, either completed or grandfathered by waiver on May 3, 2010) should be a required registered representative registration that cannot default to a Series 7, 62, or 82 registration. Allowing the use of the Series 7, 62, or 82 contradicts the intent of the rule and creates additional confusion. An LCFB by being "limited" <u>forfeits</u> it rights to other business lines that are allowed for full service broker-dealers that also conduct investment banking activities.

8. *Should principals and representatives that hold registration categories not included within LCFB Rule 123 be permitted to retain these registrations?*

No. As is the rule now, if a firm is not licensed for a particular line of business, the broker-dealer cannot "park" the license. To repeat, an LCFB by being limited <u>forfeits</u> it rights to other business lines that are allowed for full service broker-dealers that also conduct investment banking activities.

9. *Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?*

   a. **Typically, an LCFB does not engage in recommending any securities (either of the issuers with investment banking engagement or of those with no investment banking engagement or relationship) to any customers. When/if an LCFB firm does engage in such activities, it would be in the form of a capital raise. Accordingly, by removing or prohibiting LCFB from directly or indirectly engaging in capital raise for or on behalf of any issuers will eliminate the suitability obligations. Furthermore, allowing an LCFB firm to make recommendations to customers to purchase or sell securities defeats the purpose of the rule (accepts orders to**

purchase or sell securities). Such a recommendation indicates business other than what is intended under this rule.

b. An LCFB should be subject to LCFB Rule 209, "Know Your Customer."

10. Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014, impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?

The SEC letter issued on January 31, 2014 has opened the floodgates for anybody to hang out a shingle and be an "Investment Banker". Public Protection has been disregarded in this letter in favor of a very small vocal minority of individuals who do not want to be registered. FINRA and the membership should make every effort to have the Colish letter rescinded.

The creation of the LCFB is contrary to FINRA's mission of market integrity and investor protection. The mergers and acquisitions market has been populated by numerous unsavory characters. The prevailing attitude since creation of the Series 79 license in the legal community had become one of "if the banker is not registered, don't use them". The creation of the LCFB and the SEC's no-action letter referenced earlier, I believe, will result in the unsavory characters returning to the market place and taking advantage of, what could be, very vulnerable small business owners and market integrity being compromised. Perhaps, FINRA and the industry would be better served by expanding existing rules rather than creating a whole new category to accommodate business that is already being conducted in an orderly fashion.

Respectfully submitted,

Chester Hebert

Chester Hebert
CEO

EY
Building a better working world

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April 25, 2014

Marcia E. Asquith
Senior Vice President and Corporate Secretary
FINRA
1735 K Street, NW
Washington DC 20006-1500

Re: Regulatory Notice 14-09

Dear Ms. Asquith:

We appreciate the opportunity to comment on Regulatory Notice 14-09, in which the Financial Industry Regulatory Authority ("FINRA") proposes a new set of rules for firms that meet the definition of a limited corporate financing broker ("LCFB"). Ernst & Young Corporate Finance (Canada) Inc. ("EYCF(C)") is a broker-dealer registered with the SEC and is a member of FINRA. Among other things, EYCF(C) primarily provides advisory services to its clients with respect to equity and debt financing, corporate restructuring and divestitures and mergers and acquisitions. All of EYCF(C)'s clients are institutional in nature and EYCF(C) does not carry or maintain customer accounts, handle customers' funds or securities, accept customers' trading orders, or engage in proprietary trading or market-making.

Since much of EYCF(C)'s business appears to be encompassed by FINRA's proposed LCFB registration category, EYCF(C) is interested in fully understanding the proposed parameters of the registration category so that it can determine whether it should change its broker-dealer registration to that of an LCFB, if such registration category is adopted. EYCF(C) is greatly appreciative that FINRA has recognized through its LCFB proposal that firms providing advisory services such as EYCF(C), do not engage in many of the activities typically associated with traditional broker-dealers. Therefore, such firms should not be required to comply with those FINRA rules that are not actually relevant to their business.

While EYCF(C) is excited by the concept of a new limited registration category, EYCF(C) would like to confirm its understanding of certain aspects of the proposal, as well as suggest possible modifications to ensure that EYCF(C) and similarly situated broker-dealers will be able to rely on the LCFB registration category if the proposal is adopted.

1. Non-Registerable Activity.

EYCF(C) seeks to confirm that if a registered representative of an LCFB engages in activities that do not require broker-dealer registration, such activity will not be required to take place under the LCFB. This issue arises in the context of the SEC's recent series of no-action letters involving broker-dealer registration relief for merger and acquisition advisory firms. EYCF(C) is interested in understanding how this no-action relief impacts the LCFB registration category.

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Most recently, on January 31, 2014 the SEC staff issued a no-action letter that provides limited broker-dealer registration relief for firms that engage in merger and acquisition advisory activities (the "January 31 No-Action Letter").[1] Specifically, the January 31 No-Action Letter provides that M&A Brokers,[2] subject to certain conditions, may effect transactions in connection with the transfer of ownership of privately-held companies[3] without being subject to the broker-dealer registration requirements under Section 15(a) of the Exchange Act. The conditions on which the no-action position is based, include, among other things, the M&A Broker not having the ability to bind a party to a transaction or to provide financing for a transaction. The M&A Broker must also not have custody, control or possession of funds or securities in connection with the transaction and the transaction cannot involve a public offering. In addition, the issued securities in the transaction must be "restricted securities" under the Securities Act of 1933 (the "Securities Act").

EYCF(C) assumes that activities that do not require broker-dealer registration, either because such activities fit within the parameters of an SEC staff no-action position, or some other exemptive relief, will not be required to be conducted through an LCFB. However, EYCF(C) seeks confirmation that if a registered representative of an LCFB engages in non-registerable activities, such as those contemplated in the January 31 No-Action Letter, the registered representative will not be required to engage in those activities under the LCFB. Rather, those activities will be treated as "outside business activities" pursuant to proposed Rule 327 and will not need to be recorded on the books and records of the LCFB or be subject to FINRA rules governing the LCFB.

2. Rule 15a-6 under the Exchange Act

In addition, a core part of EYCF(C)'s advisory functions involves EYCF(C) acting as a "chaperone" for non-U.S. brokers dealers from the Ernst & Young network. EYCF(C) typically chaperones the non-U.S. broker-dealers in cross-border merger and acquisition transactions, that in the absence of an exemption, would require the non-U.S. broker-dealers to register with the SEC as broker-dealers under Section 15(a)(1) of the Exchange Act. As this concept is not addressed in FINRA's proposal, EYCF(C) would like to confirm that chaperoning activities pursuant to Rule 15a-6(a)(3) under the Exchange Act (and related no-action letters) would be permissible for LCFBs in cases in which the foreign broker-dealers' activities are limited to those that could be effected by an LCFB, including activities otherwise permitted under the M&A No-Action Letters. Under the Rule 15a-6 chaperoning arrangements, EYCF(C) is responsible for, among other things, participating in communications, obtaining consents to service of process, and maintaining required books and records. EYCF(C) does not know of any reason why an

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[1] *See Faith Colish, Esq., Carter Ledyard & Milburn LLP, et al.*, SEC No-Action Letter (Jan. 31, 2014). *See also Roland Berger Strategy Consultants*, SEC No-Action Letter (May 28, 2013) and *Ernst & Young Corporate Finance (Canada) Inc.*, SEC No-Action Letter (July 12, 2012). Together, these three SEC No-Action Letters, and any subsequent No-Action Letters addressing this subject matter, shall be referred to as the "M&A No-Action Letters."
[2] An "M&A Broker" is defined in the January 31 No-Action Letter as an entity whose business of effecting securities transactions is "solely in connection with the transfer of ownership and control of a privately-held company…to a buyer that will actively operate the company or the business conducted with the assets of the company."
[3] A "privately-held company" is defined as an operating company that is not a reporting company under the Securities Exchange Act of 1934 (the "Exchange Act")

LCFB would not be permitted to chaperone a foreign broker-dealer in the same manner that traditional broker-dealers can, however, EYCF(C) would like confirmation of this. EYCF(C) would also like to confirm with FINRA that there will be no additional restrictions or limitations placed on chaperoning LCFBs that are not currently in place on traditional chaperoning broker-dealers.

3. **Public Company Transactions.**

EYCF(C) notes that there is no restriction on LCFBs engaging in public company transactions in connection with their advisory work. EYCF(C) believes that this is particularly important in light of the limitation on the scope of the January 31 No-Action Letter to private company transactions. EYCF(C) occasionally provides public company M&A advisory services. EYCF(C) wishes to confirm that these services will be able to be conducted by LCFBs. This will encourage firms to utilize this new registration category in lieu of reliance on the M&A No-Action Letters

4. **Required Documentation for Institutional Investor Status.**

As currently proposed, Rule 016(g) defines an "institutional investor" to include among other entities, a person (whether a natural person, corporation, partnership, trust, family office or otherwise) with total assets of at least $50 million. EYCF(C) seeks to understand whether LCFBs will be required to obtain any particular documentation to substantiate the value of an investor's total assets. EYCF(C) believes that LCFBs should be able to make their own determinations as to whether an investor meets the "institutional investor" threshold based on the receipt of documentation that the LCFB considers to be reasonably appropriate. Currently, EYCF(C) will qualify an investor by information provided by the investor, including representations or by publicly available information concerning the investor. The status of the investor is also the subject of representations and warranties in the engagement materials. Personnel of the firm are alert to circumstances arising during their research prior to a mandate arising or learned during the course of their mandate suggesting that the information obtained to date is inaccurate. EYCF(C) believes that its current practices have served as an effective means for determining an investor's status and should be sufficient to determine "institutional investor" status in connection with LCFB requirements as well.

5. **State Registration Issues.**

One of the potential benefits of LCFB registration is that it will afford an exemption from certain state business broker registration requirements that are available for federally registered broker-dealers, as well as state broker-dealer registration requirements in cases in which the institutional buyer exemption is predicated on federal broker-dealer registration. For example, the Illinois Business Brokers Act of 1995 requires that any person domiciled in Illinois, receiving compensation from another person to procure a business or assist in the procurement of a business, must be registered as a business broker with the Illinois Secretary of State Securities Department, unless, among other exemptions, he or she is registered as a dealer in the state of Illinois or he or she is exempt from registration as a dealer in Illinois but registered pursuant to federal securities laws. Those firms that choose to rely on the M&A Letters, rather than registering as a broker-dealer, may be in the position of being required to register as a business broker or broker-dealer with state securities commissions notwithstanding that they are not

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Marcia E. Asquith
April 25, 2014
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required to register with the SEC or become members of FINRA. We urge FINRA to ensure that this new category is fully recognized by the states as a basis for the exemptions noted above notwithstanding the more limited requirements applicable to the LCFB category.

Thank you for providing us with the opportunity to provide comments on FINRA's proposed rules for LCFBs. We would be pleased to discuss any comments herein or provide FINRA with any additional assistance as it proceeds with the proposal. Please do not hesitate to contact me at [illegible] if you have any questions.

Yours truly,

Tony [illegible]
President, Ernst & Young Corporate Finance (Canada) Inc.

STONEHAVEN

April 28, 2014

Attention: Marcia E. Asquith
Office of the Corporate Secretary FINRA
1735 K Street, NW
Washington, D.C. 20006-1506

RE: Regulatory Notice 14-09 Proposed Rule Set for Limited Corporate Finance Brokers

Dear Ms. Asquith:

This comment letter is being submitted to the Financial Industry Regulatory Authority ("FINRA") on behalf of Stonehaven, LLC, a FINRA member firm and its associated persons (collectively "Stonehaven") with respect to Regulatory Notice 14-09 and the Proposed Rule Set for Limited Corporate Finance Brokers ("LCFB"). Stonehaven is also a member of the Third Party Marketers Association ("3PM"), and has had the opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 or LCFBs. Stonehaven urges FINRA's Board to carefully consider 3PM's thoughtful and informed commentary which has earned Stonehaven's strong support.

Although Stonehaven understands the prescribed format which must be followed regarding the informational exchange executed in these comment periods, it should be noted that this particular topic covers a broad range of material and nuances which we believe warrants an oral discussion to truly understand the details and drivers of the proposed reform on this topic in addition to the conventional comment period and responses which shall be in written format. Stonehaven suggests that a round table discussion be held following FINRA's review of the collective response letters from members to achieve this goal.

Stonehaven is a global alternative asset capital raising firm which was founded with the mission of representing "best of breed" investment managers in connection with raising capital for their alternative investment vehicles. Stonehaven has cultivated relationships on a global basis with professional allocators and sophisticated investors since its inception in 2001. Stonehaven's business model, along with other dedicated capital raising firms which are serving the U.S. alternative asset management industry, is materially distinct and different from traditional broker dealers' business models which are carrying and clearing members.

This comment letter has been formatted to directly convey our "Suggestions" and the correlating "Reasons to support this suggestion".

<u>Suggestion #1:</u>

The proposed rule set for LCFB members should remove the net capital requirement applied to the LCFB members which currently has the threshold set at $5,000.

Reasons supporting this suggestion:

The current net capital requirement thresholds of $250,000, $100,000, and $50,000 respectively for carrying members and introducing members are rather arbitrary in nature, however the materiality of these dollar amounts substantively supports the spirit of the net capital requirements which is in part to protect the investor should a scenario unfurl which causes damage to an investor, and in theory the broker dealer carrying or clearing that customer account would have minimally sufficient reserves to apply to a remedial solution. When applying this methodology to the $5,000 net capital requirement for non-carrying and non-clearing members, it is clear that $5,000 would universally be determined as an insufficient amount to apply to any hypothetical remedial solution involving a customer. One may then deduce that this specific net capital requirement is in only place to ensure that all member firms remain on the grid and adhere to the general net capital requirement apparatus, and that perhaps the intention was that a well thought out resolution would be implemented down the line. This time has now finally come, and we collectively need to implement specific rules which effectively and efficiently regulate the LCFB universe of member firms.

Stonehaven submits that the FOCUS reporting requirements for LCFB members would need to be overhauled as the current set of calculations and data points are not directly applicable to LCFB members and more specifically, placement agents. For example, a specific issue that illustrates this disconnect is demonstrated through the revenue generation framework relating private placement activity. The accrual requirements set forth by the PCAOB accounting regime directly conflict with a placement agent firm's ability to accurately reflect its true capital condition because of the Aggregate Indebtedness variable and its function relating to allowable and non-allowable assets. A placement agent may accrue a substantial receivable in the form of an incentive allocation referral fee which has been accrued on its books with a correlating net pass through payable to registered representatives, but the current net capital calculation methodology does not allow the accrued net retained earnings amount to impact the net capital, and therefore can negatively impact the excess capital as well. This makes no sense to member firms in this situation, nor does it make sense to our PCAOB registered accounting firms which are auditing us. The reason is directly related to the net capital rules which were written to apply to trading firms who carry accounts, and not to placement agent firms which do not carry accounts or trade securities. Countless hours and resources have been allocated to this $5,000 minimum net capital requirement by member firms and FINRA examiners alike. This is clearly not an effective and efficient use of our collective resources when recognizing that the de minimis threshold amount does not translate to investor protection, but rather to FINRA maintaining a rule requirement to get every non-carrying and non-clearing member firm to ensure similar forensic accounting scrutiny applied to member firms which carry, custody and clear investor accounts.

More importantly, the compliance exposure which is forcibly imposed onto non-carrying member firms that results from this disconnected framework must be corrected, and this can be achieved by removing the $5,000 minimum net capital requirement and revising the FOCUS reporting requirements so that the data points are streamlined and meaningful for non-carrying member firms.

Suggestion #2:

Remove or overhaul the current Supplemental Statement of Income ("SSOI") content and filing requirement for LCFB.

Reasons supporting this suggestion:

The questions and data requests outlined in the SSOI in theory have been implemented to assist FINRA in intelligence gathering of member firms engaged in private placement activity among other items, but in practice this has not been achieved in a satisfactory manner. This recently implemented layer of recurring and required informational exchange does not provide accurate information to FINRA or the SEC because of the wide array of methods, timelines and fee structures which apply to the private placement framework and the placement agents which operate within this framework. The SSOI is clearly written inferring that a uniform application of method, timeline and fee structures applies to the private placement framework similar to the uniform process which applies to framework for trading public securities. This is simply inaccurate, and when Stonehaven specifically identified this issue to FINRA, we were told that FINRA understands this disconnect, but we should just make best efforts to interpret the questions and attempt to provide punctual and accurate data anyway. This reflects another disconnected channel of required informational exchange where non-carrying and non-clearing member firms are allocating resources to the FOCUS reports, and now SSOI filings as well, which does not promote effective and efficient regulation or accurate informational exchange, and this collectively results in valuable resources being wasted. One obvious example of this would be relating to the questions posed in the SSOI which request information regarding the revenue generated from the sales made in the reference period. Generally, private placements closed in any particular quarter will not generate commissions in the same quarter which would require the member firm filing the SSOI to reflect a "0" in the answer to the aforementioned question. This is just one example of the poorly written questions in the SSOI which confuse regulatory liaisons and examiners alike, precipitate unnecessary scrutiny relating to perceived hotspots by the regulators, and indirectly increases exposure for private placement agents due to the disconnected framework.

Suggestion #3:

Exempt LCFB members from or revise the specific rules that apply to carrying members and clearing members, and cause material expenses in the form of premiums for non-carrying members which arguably have no tangible insurance payoff in the equation. Specifically, Rule 4360 regarding the Fidelity Bond.

Reasons supporting this suggestion:

Rule 4360 and the maintenance of a $100,000 fidelity bond applies to non-carrying member firms. The spirit of this requirement dovetails with the general spirit of the net capital requirements which is to secure a minimum reserve amount of capital that may be applied to remedial solutions involving investors. A fidelity bond insures a firm against intentional fraudulent and dishonest acts committed by employees and registered representatives under certain specified circumstances. In cases of theft of customer funds, a fidelity bond generally will indemnify a firm for covered losses sustained in the handling of customers' accounts. Clearly, this does not apply to non-carrying member firms and therefore LCFB members should be exempted from Rule 4360, or the Rule should be revised accordingly.

Suggestion #4:

Exempt LCFB members from the Securities Investor Protection Corporation required payments relating to the SIPC-6 and SIPC-7 filings which impose assessment payments based on a member firm's gross revenues.

Reasons for supporting this suggestion:

Non-carrying member firms do not carry investor accounts, but must pay these ever increasing amounts which are effectively premium payments funding the SIPC Fund. These rules are not aligned properly and disproportionately create significant expenses for LCFB without providing any tangible benefit to the non-carrying member firm. This is clear through reading the SIPC Mission Statement below (with most relevant language underlined for emphasis):

SIPC was created under the Securities Investor Protection Act as a non-profit membership corporation. SIPC oversees the liquidation of member broker-dealers that close when the broker-dealer is bankrupt or in financial trouble, and customer assets are missing. In a liquidation under the Securities Investor Protection Act, SIPC and the court-appointed Trustee work to return customers' securities and cash as quickly as possible. Within limits, SIPC expedites the return of missing customer property by protecting each customer up to $500,000 for securities and cash (including a $250,000 limit for cash only).

SIPC is an important part of the overall system of investor protection in the United States. While a number of federal and state securities agencies and self-regulatory organizations deal with cases of investment fraud, SIPC's focus is both different and narrow: restoring customer cash and securities left in the hands of bankrupt or otherwise financially troubled brokerage firms.

In SIPC's own words, their mission directly relates to protecting customer assets. It is unfair and unjust to be collecting premium payments from all member firms, when non-carrying member firms do not carry accounts and therefore have nothing for SIPC to protect.

In closing, Stonehaven submits that it is critical to understand the motive of the proposed rule set for LCFB members, which is effectively to draw a line of intelligent distinction regarding the applicable core rules which have been thematic and consistent in application for all member firms since the passage of the 1933 Act and 1934 Act, and to create a subset of the member universe to effectively differentiate a carrying and clearing member firm, such as Morgan Stanley, from a non-carrying and non-clearing member firm, such as Stonehaven. This much is common sense. It is imperative to understand the large universe of the distinct differences and nuances which apply to universe of non-carrying and non-clearing member firms, and subsequently apply that understanding in a streamlined application of rules to effectively and efficiently regulate this bifurcated universe of member firms.

Stonehaven appreciates the opportunity to offer comments on the proposed rule set for LCFB and would be pleased to discuss any of the points made in this letter in more detail. Should you have any questions, please contact Steven Jafarzadeh at (212) 616-7678.

Sincerely,

/s/ Steven Jafarzadeh, CAIA, CRCP
Managing Director, CCO & Partner
Stonehaven, LLC

BUTLER CAPITAL PARTNERS

April 28, 2014

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

Our firm, Butler Capital Partners (CRD #114242), is a FINRA member specializing in placement agent services for unregistered private placements, per our Form BD. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Butler Capital Partners has fourteen employees and specializes in capital raising for hedge fund managers.

Sincerely,

Antoine C. Kemper, Jr.
Chief Operating Officer

cc: R. Alan Butler, Jr., Managing Member

[illegible]

203 Store Hill Road · Old Westbury, NY · 11568 · Telephone (516) 333-[illegible]

As a small b/d who has worked hard at great cost of time and capital to be a member of FINRA, I am concerned that there is legislation that is being considered to exempt M&A "brokers" from FINRA membership.

We compete with these M&A brokers. By allowing them to conduct securities transactions (sale of the stock of a private business) what advantage does the FINRA licensed b/d have?

Should we give up our FINRA licenses and get real estate licenses like they have?

Please advise on what our firm should do.

Tom Korzenecki
Principal Managing Director
Grand Avenue Capital Partners LLC
Investment Bankers   Member FINRA/SIPC (crd 135073)
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Dear Ms. Asquith,

We appreciate the opportunity to comment on the proposed rule set change for Limited Corporate Broker Dealers as outlined in Regulatory Notice 14-09. As a placement agent for high quality private equity and venture capital funds, CSP Securities, LP would definitely fit the definition of a firm that would benefit from relief from a number of the rules and regulations required of a registered Broker-Dealer. There are a number of requirements that CSP Securities, and other firms such as ours, are currently subjected to through the standard FINRA rule book that neither provide customer protection nor serve to enhance FINRA's ability to supervise our activities. The move towards establishing a distinct rule set for Limited Corporate Financing Brokers is to be commended; however, we feel that the modifications proposed fall short of providing significant relief in the areas that we feel are misaligned with the nature of our business. A few examples of requirements currently imposed on firms of our size and scope that are misaligned include:

- SIPC Membership – CSP Securities does not carry customer accounts nor do we engage a clearing firm to clear customer accounts. At no point do we handle customer funds or are we in a position to potentially result in a loss of customer funds, so to require SIPC membership and the related annual assessment is an expense that ultimately carries no value to our Firm.
- Anti-Money Laundering Audit requirement – CSP Securities does not handle customer funds nor do we facilitate the handling of customer funds by a third party. Customer funds utilized to purchase product sold by CSP Securities is handled directly by CSP Securities' client and ultimately, by counsel representing CSP Securities' client. CSP Securities is not directly involved in the transaction dynamics and thus, it is difficult for us to verify source of funds and/or monitor suspicious activities. CSP Securities exercises diligence in reviewing OFAC and FinCEN to insure that there are no issues relative to our target customer base, but beyond that the majority of the elements subject to third-party audit do not apply to our firm. The scope of our AML exposure could easily be encompassed as part of the annual certification of compliance and supervisory processes (3130 / 3012).
- Fidelity Bonds – Similar to our concerns related to SIPC membership, the requirement for CSP Securities to purchase / renew annually a Fidelity Bond with minimum coverage amounts in order to protect customers against loss is in essence requiring our firm to incur an expense for a product that is irrelevant to the type of business conducted by CSP Securities. At no time does CSP Securities handle client funds or securities and thus the potential for loss is nil.
- Suitability Requirements – CSP Securities serves as an introducing agent to General Partners raising capital and is generally not a party to the transaction process; and in all cases is not in a control position such as to require disclosure of profile details such as other investments, financial needs, tax status, investment objectives, etc. The majority of investors covered by CSP Securities can be verified via a third-party public data search, however, this is not always the case. These investors are required to complete comprehensive Subscription documents in which they must disclose acceptance of terms as outlined in the Limited Partnership Agreement and attest to the qualifications necessary of Fund investors. The documentation process is facilitated by fund counsel, a process to which CSP Securities is generally not privy.

Given that the modified structure provides little relief from the primary burdens imposed on truly Limited Corporate Securities firms, we would not be inclined to modify our registration category.

Thank you for your consideration of these comments. It is our hope that FINRA will continue to investigate the needs for a revised rule set for firms, such as CSP Securities, that conduct businesses that fall largely outside that of a traditional broker / dealer.

Very truly yours,

Tiffany Lauterbach
Principal / FinOP
CSP Securities, LP
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April 28, 2014

Via E-Mail To: pubcom@finra.org

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

RE: FINRA Regulatory Notice 14-09, Limited Corporate Financing Brokers

Dear Ms. Asquith:

In February 2014, the Financial Industry Regulatory Authority (FINRA) published Regulatory Notice 14-09 (Regulatory Notice) seeking comments on a proposed rule set (Proposed Rule Set") for member firms that meet the definition of "limited corporate financing broker" (LCFB). It is a positive sign that FINRA acknowledges that LCFB firms do not in fact expose investors and the markets to the same risk as firms who do carry or maintain customer accounts, handle customers' funds or securities, accept customers' trading orders, engage in proprietary trading or market-making or actually market securities products to investors. However, based upon both communications with our clients and our experience in this area, a number of concerns have been identified that are discussed below.

1. As has been noted in prior Comment Letters, the most significant compliance costs for LCFBs include an annual PCOAB Financial Audit, maintenance of a fidelity bond, payment of SIPC Assessments, FINRA Assessments, the annual AML Independent Testing, and the annual internal control review and certification. Of those issues, FINRA has provided some relief with respect to the AML Independent Testing and the annual internal review and certification, but it would appear that FINRA should consider reducing the FINRA General Assessment, as the cost to FINRA to supervise LCFB firms would be significantly reduced. Of greater value to the membership would be in FINRA's addressing the issues that aren't under its direct control. It would appear appropriate and a true benefit for the future LCFB membership for FINRA, in its capacity as an SRO, to work with the SEC, SIPC and the PCOAB to reduce or minimize the financial audit and reporting obligations, fidelity bond requirements and the elimination of the SIPC assessment as the securities are not covered by SIPC.

2. FINRA issued a Frequently Asked Questions (FAQ) on Investment Banking that addressed among other issues, the qualifications necessary to engage in investment banking activities. The clarification in part stated that "the Investment Banking Representative registration category (Series 79) is meant to include investment bankers advising on a marketing plan prepared by a sales team or developing and/or contributing information for marketing materials. However, it

would not include persons who actively market the offering and interact with investors or potential investors, such as a person who is engaging in road show activities. Such a person would also need to be registered as a General Securities Representative (Series 7), Corporate Securities Representative (Series 62) or Private Securities Offerings Representative (Series 82) depending on the type of offering being made". We believe that FINRA should confirm that the Series 79 qualification will be adequate to both structure and "market" the companies of LCFB clients. Additionally, as FINRA required its membership to obtain the Series 7 or Series 62 for essentially the same activities that a LCFB would engage in, FINRA should allow those individuals to maintain those licenses.

3. The majority of the investment banking clients we represent (and who would qualify as an LCFB), were required to note on their Form BD, and in their membership application, that they were in fact engaged in "private placements" of securities (to wit, they participated in a negotiated transaction of a security that was being privately placed). As a result, it would appear appropriate that to the extent the term "private placement" is no longer utilized by FINRA to describe investment banking activities, FINRA further clarify the term "private placements" so that an LCFB does not inadvertently engage in an activity that would be deemed violate the Proposed Rule Set or to work with the SEC to add the activity of investment banking as an identified activity on the Form BD.

In summary, we believe that goals set forth in the Regulatory Notice regarding the Proposed Rule Set is an important step in moving away from a one size fits all regulatory framework for broker-dealers who are engaged in investment banking activities. Thank you for your consideration of our comments. Should you have any questions, please contact the undersigned at 281-367-2454.

Respectfully submitted,

Daniel E. LeGaye
The LeGaye Law Firm, P.C.

The proposed provisions are still too broad for many of these groups, and especially may no longer be required to be registered by virtue of the SEC no-action letter recently issued. We would like to see no audit requirement unless the firm has 20 or more employees or $10 million in net revenues. We also believe that the registration requirements could be limited to just those as an associated person and not necessarily be a need for specific licensing. SIPC membership requirements - fees should be eliminated since there are no customer accounts. FINRA revenue assessment fees should also be eliminated or reduced given the limited level of FINRA supervision oversight. I am sure there are many other areas where the requirements are too broad.

Sincerely,

Greg LeNeave

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member registered under Tessera Capital Partners, LLC. GOAL Consulting LLC specializes in placement agent services to registered investment advisors, trust companies and family office service providers on behalf of asset managers. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Sincerely,
Joseph M. Lydon

Joseph M. Lydon
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(510) 751-3606
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Marcia E. Asquith
Office of the Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Dear Ms. Asquith,

I'd like to thank FINRA for its effort to update its rules for small firms like ours that do not have the need, nor are we permitted, to handle client funds or securities. That said, the SEC no-action letter recently issued to Faith Colish et al so changes the landscape as to make the very limited benefits of applying for LCFB status less than appealing to firms like ours that only provide advisory services for mergers and acquisitions.

Precisely because our Membership Agreement with FINRA does not permit the carrying of customer accounts, the holding of customer funds or the safekeeping of securities, applying for LCFB status would be more logical and beneficial if FINRA were to eliminate the following expensive and arguably redundant activities:

- The need for the PCAOB annual audit
- The $100,000 Fidelity Bond
- Membership of SIPC
- SSOI and Focus Reports

Finally, I would suggest that the word *Limited* in the proposed nomenclature of "Limited Corporate Financing Broker" is a potential problem in that it may detrimentally confuse our clients by suggesting we have reduced our service offerings when in fact they will remain unchanged.

Sincerely,

Keith McCracken

CEO and Managing Partner
McCracken Advisory Partners
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BRIDGE 1 ADVISORS

April 23, 2014

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

Regarding: Rules for Limited Corporate Financing Brokers

Attention: Ms. Martha E. Asquith

Bridge 1 Advisors is a member of FINRA and a Placement Agent. As outlined in the proposed FINRA rule, Bridge would qualify to seek registration as a Limited Corporate Financing Broker.

I applaud FINRA management for recognizing that firms like ours have been regulated in the same manner as firms trading and holding securities with retail and institutional customers. Clearly there is a significant difference in business operations from what they do and what we do in our business. We see this FINRA proposal as an opportunity to focus the appropriate regulation on specific business models versus one size fits all.

A Placement Agent is not a securities dealer but a marketing firm. We do not trade or hold securities but work with clients under contract in the alternative investment space (Private Equity and Hedge Funds). We become for a limited time their marketing arm, generally to assist in increasing assets under management (AUM). Our target market is the institutional investor (Pension Funds, Endowments, Foundations, their Advisors and Consultants) and other qualified investors. Unlike a securities transaction, there are layers of assessment and approvals from internal staff, advisors, consultants, attorneys and investment committees before an investment takes place. This is a process that can take months before an investment and Limited Partnership Agreement is signed by our client and the investor.

As a marketing firm we work with our clients to position and brand their strategy offering a differentiation from the thousands of competitors seeking AUM. Our clients need our expertise and market knowledge to help guide them through the marketing of their strategy.

Member of FINRA; CT Registered Investment Advisor
6 Landmark Square, Suite 400 Stamford, CT 06901
203 359-5652

BRIDGE 1 ADVISORS

We assist our clients in the review and preparation of their collateral materials including the Offering Memorandum (prior to attorney review), web site, due diligence and other related information. All of this is to show a consistent message and explanation of the investment strategy and track record to the potential investor.

Overall, this FINRA proposal is a step toward setting realistic guidelines for Placement Agents. We are overregulated which results in higher costs of doing business with increased time spent dealing with regulations rather than marketing. The question to FINRA - do the current rules reflect our business model and effectively regulate our firm. The answer is NO!

Some examples of this oversight are overwhelming in regard to our business profile.

SIPIC insurance: WHY? – we do not deal with the public nor transact or have custody of securities.

PCAOB: Why? – we are not a public company but yet are required to hire an additional accounting firm to produce this filing.

Fidelity Bond: Why? – the bond includes the coverage of securities, counterfeit currency, credit card forgery and a list of issues that have nothing to do with our business.

SSOI and Focus Reports: Why? Both are documents relating to securities and that related business. Relative to the questions needing response we answer fewer than a dozen entries.

There are more examples like monthly financial reports, net capital requirements and week long FINRA examinations. The one common aspect is that FINRA and the SEC unrelated rules take time and money to comply with these regulations. Rules and Regulations are acceptable if the relate to a business operation, but these and others do not.

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BRIDGE 1 ADVISORS

I understand all these rules and regulations are not issued by FINRA alone so I ask our governing body to work with the SEC to review and relieve marketing firms like ours from the burdens of unnecessary regulation from both entities.

As for the SEC no-action letter issued to Faith Colish, dated January 31, 2014 it offers a perspective for firms like ours. This SEC letter makes it possible to be in a related business like ours without the regulation which is appealing to a small firm. On the other hand, our clients like the comfort of dealing with a broker dealer. It does however bring up the question – at what cost is it reasonable to be a member of FINRA.

Finally, the proposed Rule for Limited Corporate Financing Brokers is a great initial step. I urge FINRA to recognize that more work is necessary to relieve firms like ours from rules and regulations that are unrelated to our business model.

Thank you for the opportunity to comment on this proposed rule.

Respectfully,

Robert G McGreevy
Managing Partner

FINRA representative –

As requested in FINRA Regulatory Notice 14-09, below are the comments of Achates Capital Advisors LLC on the subject rule set.

Summary

The Limited Corporate Financing Broker ("LCFB") rules proposed by Regulatory Notice 14-09 are, in their present form, of no interest to our firm: no benefits of consequence are offered by the rule set, and its restrictions are unacceptable. It is difficult to imagine that most LCFB-eligible firms would not feel the same way.

Preclusion of the Offering of Private Placements to Accredited Investors

Although our small firm meets the criteria for conversion to an LCFB – i.e., it conducts only the types of businesses allowed by proposed LCFB Rule 016(h)(1) – the inability to offer private placements to "accredited investors," rather than only to much narrower "institutional investors," precludes conversion. The other abatements of the broader FINRA rules, which themselves are disappointingly minimal, do not offset this unreasonable stricture.

FINRA states that it has "uncovered serious concerns with the manner in which firms market and sell private placements to accredited investors." Reg. Notice 14-09 n.3. Accordingly, FINRA states that if it were to permit LCFBs to "market and sell private placements to accredited investors," it would have "to expand the applicable conduct rules and other provisions" in the LCFB rules. *Id.* FINRA, however, gives no examples of the "serious concerns" or describes the putative necessary expansion.

Whatever "serious concerns" FINRA has uncovered, they presumably were violations of the applicable suitability, know-your-customer, communications, etc., rules committed by firms of all sizes. Yet FINRA does not contend that these violations were committed disproportionately by LCFB candidates, so as to justify barring them from a segment of the private placement market that larger firms can reach. This puts LCFBs at a serious, and unacceptable, commercial disadvantage.

In any case, there is no indication that such violations would more likely be committed under the proposed LCFB rules. Would these "serious concerns" not also be violations under them as well?

The clear implication of the restriction is that would-be LCFBs cannot be expected to offer private placements to accredited investors without indulging in some sort of wrongdoing that the new rules do not address. The answer is not to bar LCFBs from the accredited-investor marketplace altogether, but to incorporate in the new rules provisions that address the "serious concerns," and to enforce compliance with them through FINRA's existing range of disciplinary measures. (It seems unlikely that such provisions would "eviscerate the benefits" of the rules, since they scarcely have any benefits of consequence now.)

A final comment on the limitation: SEC Rule 506(c) under Regulation D, recently adopted pursuant to the JOBS Act, now permits the broad marketing of private placements, provided they are sold exclusively to accredited investors. Under the proposed rules, LCFBs would not be able to use Rule 506(c), in an illogical narrowing of access to the very marketplace that Congress sought to expand.

Annual Audit

In addition to permitting the offering of private placements to accredited investors, the proposed LCFB rules should eliminate the requirement for an annual audit.

An LCFB cannot carry customer accounts or handle customers' funds or securities: it cannot accept customer orders to purchase or sell securities nor engage in proprietary trading or market-making. *Proposed* LCFB Rule 016(h)(2). Thus no one who deals with an LCFB can have any financial risk related to its securities positions, purchases or sales, or money handling, because they are not permitted. There is therefore no justification for an expensive annual audit to ensure an LCFB's financial responsibility to and protection of customers (in the sense of investors), since no customer assets are at risk. (But see below for confusion on the definition of "customer.") In view of this, an appropriate outside annual examination of an LCFB's financial statements would be the professional, but more limited and less expensive, "review" under the standards of the AICPA. (*See* AR Sec. 90, http://www.aicpa.org/Research/Standards/CompilationReview/DownloadableDocuments/AR-00090.pdf.)

Definition of Customer

The proposed rules define a "customer" as "any natural person and any entity receiving corporate financing services from a limited corporate financing broker." Proposed LCFB Rule 016(d). They also prohibit, *inter alia*, an LCFB from "accept[ing] orders from customers to purchase or sell securities, either as principal or as agent for the customer." Proposed LCFB Rule 016(h)(2). Thus, on their face, the rules prohibit an LCFB from accepting and executing private placement engagements.

This is obviously not the intent of the rules, inasmuch as LCFBs may "solicit[] potential institutional investors," *id.* (h)(1)(F). However obliquely stated, this must include effecting private placements as agent, or else the LCFB rules can have no utility whatsoever. Moreover, the term "customer" is used elsewhere in the proposed rules in the sense of "investor." *See, e.g.*, Proposed LCFB Rule 211.

A solution to this confusion is not to use the term "customer" to apply to those receiving corporate financing services, but instead to define them as "clients." The distinction between "customers" – investors who buy and sell securities from, to, and through a broker-dealer firm – and "clients" – those who use the firm's corporate financing services – has been employed in Wall Street for decades. The term "customer" (in the sense of an investor) should be defined separately, and the rules entirely rewritten using both definitions.

Return to Non-LCFB Status

Conversion to LCFB status by a currently LCFB-eligible firm may be made simply by requesting an amendment to the firm's FINRA membership agreement. Proposed LCFB Rule 116(b). On the other hand, if such a firm later wishes to return to non-LCFB status for whatever reason, even with no change in its business lines, it must file a continuing membership application and seek an amendment of its membership agreement. Proposed LCFB Rule 116(c). Apart from the administrative time and effort entailed in such a procedure, the firm will effectively have to "buy back" its original status for $5,000, the minimum "material change" continuing membership application fee (absent a waiver). *See* Schedule A to FINRA Bylaws, Section 4(i)(1). This, too, is a substantial disincentive to converting to LCFB status.

Answers to Specific FINRA Questions Raised in Regulatory Notice 14-09

The following responses to the specific questions raised by FINRA should be viewed in the context of the comments above. The questions are repeated in abbreviated form.

1. Do the Rules provide sufficient protection for LCFB customers? Yes, an LCFB customer (in the sense of "investor") would enjoy all the protections for a customer of a non-LCFB: the rules do not compromise any aspect of the existing suitability or "know-your-customer" requirements.

2. Do the Rules appropriately accommodate the scope of the LCFB business model? No.

   (a) An LCFB should be permitted to market and sell private placements as agent to "accredited investors," not just to "institutional investors."
   (b) Proposed Rule 016(h)(1)(F) should explicitly state that an LCFB may act as agent in the sale of private placements, not simply that it may "solicit" investors.
   (c) An LCFB should be permitted to engage in the private placement of Direct Participation Programs.
   (d) An LCFB should be required to undergo only an annual outside review of its financial statements, rather than an Audit.

3. Is the definition of LCFB appropriate? No, as noted in the "Definition of Customer" comment above.

4. Are there firms that would qualify for LCFB status but choose not to elect it? Yes, virtually all broker-dealers that engage exclusively in merger and acquisition advisory and private placement work would qualify, but virtually none, we believe, will choose it under the proposed rules. There are serious limitations on an LCFB's ability to offer private placements, with no meaningful benefits to LCFB status. Indeed, the very word "limited" carries a connotation of an LCFB's inadequacy to would-be clients – quite rightly, given its restricted market access.

5. What is the likely economic impact of the adoption of the LCFB Rules? Because we do not foresee any meaningful number of broker-dealers opting for LCFB status under the proposed rules, we do not believe that their adoption will have any meaningful impact.

6. Estimate the number of firms eligible for the new rule set. Our firm has no estimate, but in a December 20, 2012, e-mail to small FINRA members, FINRA small- firm governors Norensberg, Carreno, and Keenan stated that the forthcoming LCFB proposal was "expected to affect nearly 700 broker-dealers."

7. Are there any registration categories that should be added or eliminated from the Rule? Yes. The allowable activities should include DPP (direct participation program) securities (Series 22 examination), the sales of which are almost always effected as private placements.

8. Should principals and representatives be allowed to retain registrations not required by the Rules? Yes; there is no reason to remove such registrations. FINRA's doing so would be yet another reason not to convert to an LCFB.

9. Does an LCFB make recommendations to customers? And should an LCFB be subject to K-Y-C and suitability rules? An LFCB would not make recommendations to buy or sell securities, other than the buy "recommendation" implicit in offering a private placement to an investor, or the "buy" or "sell" recommendations implicit in a merger and acquisition advisory engagement. And, of course, an LCFB should observe the suitability and K-Y-C rules in selling a private placement as agent.

10. Does the SEC staff no-action letter to Faith Colish impact the analysis of whether a firm would become an LCFB? In view of the no action letter, it is possible that firms that (a) offer only merger and acquisition advisory services and (b) otherwise meet the conditions of the no action letter might decide to abandon their status as broker-dealers and FINRA

GENESIS
MARKETING GROUP

April 28, 2014

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in placement agent services to institutional money managers. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

All the best,

Ron Oldenkamp
President, Genesis Marketing Group

19 North Grant Street, Hinsdale, IL 60521 PHONE: 630.887.1414 FAX: 630.887.1415

Signal Hill

March 20, 2014

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

Re: Request for Comment – Limited Corporate Financing Brokers
Regulatory Notice 14-09

Dear Ms. Asquith:

Signal Hill Capital Group LLC ("Signal Hill") appreciates the opportunity to submit this comment letter on the proposed rule set for firms that meet the definition of limited corporate financing broker ("LCFB"). Signal Hill employs approximately 70 persons in six locations throughout the United States. Our practice is limited to rendering investment banking advisory services only, and, as such, we anticipate we would meet the definition of an LCFB.

Signal Hill commends FINRA for its efforts to adapt its rules to more closely align with firms such as ours. Historically, it has been our experience that FINRA staff and examiners have struggled to apply to us, and others like us, rules and standards designed for firms engaging in retail brokerage business, with unsatisfactory and sometime frustrating results. Regardless of the ultimate outcome of the proposed LCFB rule set, we encourage FINRA to continue its efforts in this regard.

With respect to the newly proposed rule set, it is our view that however commendable the intent, it falls short of offering any meaningful improvement over the status quo. The most substantive proposed change appears to be elimination of the Regulatory Element continuing education requirement for registered personnel. While we support that change, it could – and in our opinion, should – be adopted independent of the creation of new LCFB category, simply by modification of the current rules such that the mere holding of a Series 79 registration would not trigger a need to participate in Regulatory Element continuing education absent some other obligation to do so[1].

The proposed new rule set does virtually nothing to meaningfully address what we believe is the main complaint about the current environment, which is the extraordinary cost

[1] We encourage FINRA to use this opportunity to review its entire approach to the Regulatory Element process. Under the current procedures, employees are required to travel to an offsite location, where they are asked to remove jewelry and turn their pockets inside-out for inspection. Many employees, whose only contact with FINRA is in connection with the bi-annual Regulatory Element process, report finding it to be unduly intrusive and demeaning. FINRA should demand a more nuanced approach from its vendors and should explore ways to deliver continuing education directly to users.

associated with maintaining a standard broker-dealer registration. In particular, an LCFB presumably would continue to be required to undergo an annual independent broker-dealer audit by a PCAOB registered public accounting firm, as well bi-annual AML independent testing. Since, by definition, an LCFB could be neither a broker nor a dealer, nor permitted to hold or even handle customer funds or securities, continuing to subject those firms to those requirements (and costs) makes no sense and offers no protections to anyone. That said, we understand relief from those requirements may be beyond FINRA's jurisdiction.

Likewise, despite having no customer accounts and holding no customer funds or securities, it appears that the proposed rules offer no relief from the current requirement that LCFB firms continue to be members of SIPC. SIPC assessments, which are based on revenues regardless of how generated, are onerous and constitute an unwarranted tax on LCFB firms whose clients are not eligible for SIPC protection in any event.

In response to some of the particular questions raised by FINRA at the end of Notice 14-09, it is our view that:

- most firms that qualify for LCFB status would ultimately choose not to, given the scant incentives for doing so and the strictures such a classification would impose

- the proposed new rules offer little economic benefit to LCFBs over the status quo

- principals and representatives who hold registration categories not included with LCFB Rule 123 should be permitted to continue to retain those registrations. Termination of those registrations offers no benefit to FINRA and would constitute a disincentive to firms that might be considering making the switch, particularly given that pursuant to proposed Rule 240, FINRA specifically reserves the right to subsequently require that a firm revert to existing broker-dealer standards

- the SEC no-action letter recently issued to Faith Colish *et al* significantly impacts the analysis (and desirability) of whether a firm would elect to pursue becoming an LCFB. Many, perhaps most, firms that would meet the eligibility standards for LCFB also satisfy the parameters of the no-action letter. There are no obvious reasons why a firm that did so would nevertheless elect to voluntarily continue to assume the costs and responsibilities associated with being an LCFB when it could relieve itself entirely of those by reliance on the no-action letter. Likewise, pending legislation in the US House of Representatives and Senate may further undermine the appeal of LCFB status.

Thank you for considering these comments. Please contact the undersigned if you have any questions or if we may be of any assistance.

Very truly yours,

Robert E. Patterson
General Counsel

HAMERSLEY™
PARTNERS

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in placement agent services to institutional investors, primarily corporate and public pension plans and investment consulting firms. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCFB). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary in the attached PDF, which has earned my strong support.

Regards,

Peter Pavlina

Managing Principal

PFM Perkins
Fund Marketing

April 28, 2014

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

Perkins Fund Marketing ("PFM") has been a FINRA member since October of 1998. We provide professional alternative investment marketing services to fund managers including hedge and private equity funds. PFM employs ten professionals, seven of which are Series 7, 82 and/or 63 registered representatives and three of which are Series 24 registered principals.

PFM's professional marketing representatives bring broad and deep experience in the financial services sector. Some of the benefits we provide to fund managers include:

- PFM's full service approach which allows fund managers the ability to devote their immediate and limited resources to portfolio management rather than marketing and sales.
- Access to deep and trusting investor relationships built through years of quality service provided by our professionals. PFM's investor contacts expect us to bring to them high quality, pre-screened opportunities on which significant due diligence has been performed with an understanding that we are only introducing the investment opportunity, and that the prospective investor must perform their own due diligence and not rely solely on our work.
- Creating/enhancing marketing materials (which includes ensuring all material is FINRA compliant) and working with fund managers on presentation skills to best articulate their strategy, investment philosophy and risk management process to potential investors.
- Defining the target market, streamlining the marketing process and providing ongoing communication with prospective and current investors.

We are a founding member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCFB).

107 John Street, Southport, CT 06890 Tel: 203.418.2000 Fax: 203.418.2001 www.pfm-llc.com

We would like to highlight the following about our firm which support the very valid points in the 3PM letter:

- We do not open or maintain any customer accounts, we do not accept any customer funds nor do we manage or advise on investments for any investors.
- We do not generate any revenue from investors, only from the fund managers who retain us.

With the above points in mind, we strongly feel that we should not be obligated to pay into customer related programs including SIPC as we do not take custody of customer capital nor open or maintain customer accounts.

I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary which has earned my strong support.

Regards,

Gilman C. Perkins
Principal and Managing Member

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in placement agent services to institutional investors, primarily corporate and public pension plans and investment consulting firms. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCFB). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary in the attached PDF, which has earned my strong support.

Regards,

Andrew Phillips
Principal – Hamersley Partners

RWS

RW SMITH & ASSOCIATES, INC

28 April 2014

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

Dear Ms. Asquith,

RW Smith appreciates the opportunity to comment on Regulatory Notice 14-09, the proposed rule set for Limited Corporate Financing Brokers ("LCFB"). RW Smith supports FINRA's initiative to address the need for a relevant, separate rule set for limited purpose firms, in this instance LCFB firms.

While we applaud the measures FINRA has undertaken to move this important initiative forward, both the establishment of an industry participant working group and the undertaking of a revision of the current rule set to more accurately reflect the LCFB business model in order to more effectively regulate LCFB firms, we believe the proposed rule set needs more work.

If the objective is to understand the LCFB business model in order to be able to write appropriate rules and regulations in order to protect the investing public, our markets, and our member firms, then we still have a ways to go on the proposed rule set in 14-09. To that end, RW Smith would like to voice our support of the comment letters submitted by the Third Party Marketers Association ("3PM") and Lisa Roth, respectively, and encourage FINRA to thoughtfully consider both letters and our support of them.

I commend FINRA's focus on understanding the individual categories and business models of their member firms in order to write and enforce appropriate regulation to better protect the investing public and the markets we work in and for, and the LCFB category of firms seems as logical a place to begin as any. As the CEO of an "Other" category of firm, an interdealer broker, the comments made by 3PM regarding SIPC, PCAOB required audits, Fidelity Bonds, Net Capital Requirements, AML and more really resonated with me because they apply to our business model as well. I look forward to being able to contribute to furthering the development of the proposed rule set through to implementation.

Best regards,

Paige W. Pierce
President & CEO, RW Smith & Associates, Inc.

Harris Williams & Co.
middle market

RECEIVED
APR 29 2014
FINRA
Office of the Corporate Secretary

April 28, 2014

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

Subject: Limited Corporate Financing Brokers Proposed Rule Set

Dear Ms. Asquith:

This letter is in response to FINRA's solicitation of public comments on its proposed rule set (the "Proposal") for Limited Corporate Financing Brokers ("LCFB").

Harris Williams LLC d/b/a Harris Williams & Co. ("HW&Co." or the "Firm") is a FINRA-registered broker-dealer that provides mergers and acquisitions advisory and related services ("M&A Services") to companies and their owners. HW&Co. does not extend credit, hold customer accounts or engage in banking or investing transactions on its own or its customers' behalf. The Firm's revenue is comprised entirely of fees derived from M&A Services.

The Firm believes that HW&Co. meets the definition of LCFB under proposed Rule 016(h)(i) because HW&Co.'s M&A Services are encompassed by the activities set forth in 016(h)(1)(A)-(F). Moreover, HW&Co. does not engage in any of the activities set forth in 016(h)(i). FINRA has particularly requested comments concerning the issues set forth below. HW&Co.'s comments are set forth in immediate response thereto.

- Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?

  Yes. One of the benefits of the Proposal is it distinguishes among types of customers and business models and the protections that customers require and the concomitant burdens for the providers of services thereto. For example, HW&Co.'s customers are sophisticated corporate and institutional clients seeking advice on mergers and acquisitions (as opposed to assistance in buying and selling securities as investments, for example). Therefore, protections such as those provided by the best execution and suitability rules or current minimum capital requirements should not be applicable to the Firm as they are to securities brokerage activities. The limited scope of LCFB activities and clients means that rules designed to protect retail customers, account beneficiaries and securities investors are not necessary for an LCFB.

- Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?

  For closer alignment between the proposed LCFB rule set and the nature of LCFB activities and customers, certain of the rules that remain applicable to LCFBs could be modified or removed.

For example, the annual gift limit of $100 may provide meaningful anti-conflicts protection in a retail securities brokerage context. But for an LCFB, such rules result in administrative burdens but do not provide meaningful protection in light of the nature of an LCFB advisory business model and corporate/institutional clients.

- Is the definition of "limited corporate financing broker" appropriate? Are there any activities in which broker-dealers with limited corporate financing functions typically engage that are not included in the definition? Are there activities that should be added to the list of activities in which an LCFB may not engage?

For the avoidance of doubt, it may be helpful to insert language (in **bold**) such as: "advising a company regarding its purchase or sale of **controlling or minority ownership interests** in a business..." It may also increase clarity to enumerate activities such as "advising with respect to strategic alternatives" and "providing valuations". Such services may be provided on a stand-alone basis as well as in the context of an acquisition or divestiture.

- Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?

HW&Co. has no comment.

- What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?

Given the nature of LCFB activities and client base, it is doubtful that LCFB customers would switch firms because of a potential perception of reduced protections. HW&Co. believes that its essential compliance infrastructure will not substantially change upon implementation of the Proposal. However, implementation of the Proposal will meaningfully reduce unnecessary administrative burdens and costs for the Firm.

- FINRA welcomes estimates of the number of firms that would be eligible for the proposed rule set.

HW&Co. has no comment.

- Proposed LCFB Rule 123 would limit the principal and representative registration categories that would be available for persons associated with an LCFB. Are there any registration categories that should be added to the rule? Are there any registration categories that are currently included in the proposed rule but that are unnecessary for persons associated with an LCFB?

HW&Co. believes that the current registration categories are sufficient.

- Should principals and representatives that hold registration categories not included within LCFB Rule 123 be permitted to retain these registrations?

  Probably not; HW&Co. believes that principals and representatives should be permitted to hold non-included registrations only if the firm in question can adequately supervise the activities covered by such registrations, which may be doubtful in the context of an LCFB.

- Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?

  The extent to which an LCFB's advice constitutes "recommendations to customers to purchase or sell securities" is a consequence of the general definition of securities and the forms of business acquisitions and divestitures. The manner in which an acquisition or divestiture is accomplished – the sale or purchase of assets and liabilities or securities is driven by considerations that bear no relationship to the securities laws or FINRA regulations. Given the nature of LCFB activities and client base, an LCFB should not be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) on an LCFB.

- Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014, impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?

  HW&Co. has no comment.

Thank you for the opportunity to provide comments to this important proposed rule set. If you have any questions, please do not hesitate to contact the undersigned.

Sincerely,

Harris Williams & Co.

By: Paul Poggi
Chief Operating Officer
(804) 915-0192

Andrew D. Tino
Chief Compliance Officer
(412) 762-1754

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is an institutional division of Compass Securities Corporation, a FINRA member specializing in institutional outsourced marketing services. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Sincerely,

Sandra Powers
Founder & CEO
ARK Global LLC
An Institutional Division of Compass Securities Corporation
Office: 1-800-676-2921
Mobile: 1-781-572-5288
Email: powers@arkglobalonline.com
44 Washington Street Suite 50
Wellesley Hills, MA 02481

Fells Point Research LLC
Baltimore, Maryland
CRD# [illegible]

Re: Comments on Regulatory Notice 14-09

Fells Point is a firm that provides sell side research to institutional clients. Were we a corporate financing broker, we would fit the criteria for the proposed rule. Why not broaden the rule to include research providers?

Thank you for providing the opportunity to comment.

David W. Pringle
(410) [illegible]

Marcia E. Asquith

Office of the Corporate Secretary FINRA

1735 K Street, NW

Washington, DC 20006-1506

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in Reg D offerings and placement agent services to large US-based institutional investors. I am also a member of the Third Party Marketers Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCFB). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Steven Rubenstein

Arrow Investments, Inc.

Q Advisors
An Investment Banking Partnership

VIA E-MAIL

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

April 25, 2014

RE: Comments on Regulatory Notice 14-09 re Limited Corporate Financing Brokers

Dear Ms. Asquith,

Below are our comments regarding Regulatory Notice 14-09, which was issued in February. As an initial matter, Q Advisors LLC, CRD #127232 ("Q LLC") believes it could fit under the definition of a Limited Corporate Financing Broker ("LCFB") under FINRA's proposed definition. However, there are deficiencies in both the definition and the accompanying proposed regulations that make it unlikely that Q LLC would change its registration from its current status as a Broker-Dealer ("BD") to that of an LCFB, unless the proposed category and attendant rules are altered. Before addressing some of FINRA's direct questions, we will note several issues that we feel merit discussion.

1. **"Institutional Investor."** For the most part, the definition of "Institutional Investor" (including certain types of institutions and benefit plans, as well as persons with total assets of at least $50 million) would permit Q Advisors to continue to offer its services in the manner we have to date. The purchasers or investors in our clients' transactions have consistently met such a definition, with few exceptions. It has never been our practice to solicit investments from persons who are "Accredited Investors" as defined in Regulation D under the Securities Act of 1933. However, it seems to us there could be circumstances in which one of a group of potential investors might fall somewhat below the "Institutional Investor" level – for example, in the case that company insiders, such as directors or officers, were offered securities in a merger, reorganization, or other capital raising transaction.

   It would make sense to either (a) lower the threshold, as other commentators have suggested, to something along the line of "qualified purchasers" as defined in the Investment Act of 1940 (i.e., $5,000,000 in assets), or (b) include a list of exceptions to the "institutional investor" standard. Without lowering the amount or adding exceptions, most current BD's would probably be wary of the new LCFB category in the event an investor even occasionally falls outside of the proposed standard. Taking either one of these steps would enable LCFBs to carry on the work that was done by them previously as BDs, without lowering the standard to the point that FINRA's concerns over private placement offerings to "Accredited Investors" would be triggered.

2. <u>Equity/Debt Raises</u>. We want to ensure that the concept of "capital raising activities" in the LCBD registration category is broad enough to encompass debt, equity or equity-linked instruments, and not solely one category of securities. In addition, the list of permitted activities in the LCFB definition seems somewhat limited to us, and ought to be enlarged to encompass all of the "active" tasks that we undertake on behalf of clients -- negotiations, meetings, valuations, etc. (It might be helpful, in fact, to have a definition of the word "advising," or to add examples in the footnote to the LCFB definition.) Finally, it would benefit our business to be able to pay a referral fee in certain circumstances to unregistered persons who solely provide introductions to new clients.

3. <u>SIPC</u>. We understand that FINRA is not in a position to alter the current requirement of the Securities Investor Protection Corporation ("SIPC") that all licensed Broker Dealers pay fees based upon their income. However, we continue to feel that a conversation needs to be continued regarding the requirement that a firm such as ours, which has <u>no customer accounts</u> and therefore would <u>never</u> be able to take advantage of SIPC protection for our clients, must pay 0.25% of our revenue to SIPC. In light of the proposed new LCFB designation, we feel it is now even clearer that the fees are an unacceptable tax on businesses that are providing no services whatsoever to SIPC's intended beneficiaries. It seems obvious to us that the LCFB designation should be added to the list of exempt entities contained in the SIPC rules.

4. <u>FINRA questions regarding the LCFB registration category (edited)</u>.

   A. ***Are there any activities in which Broker-Dealers with limited corporate financing functions typically engage that are not included in the definition?***

      As mentioned above, services such as acting as a placement agent and providing valuations (rather than just the issuance of fairness opinions) should be included in the list of permitted activities.

   B. ***Are there activities that should be added to the list of activities in which an LCFB may not engage?*** We do not engage in any of the five proposed prohibited activities (carry or maintain customer accounts, hold or accept customer funds or securities, accept orders from customers to purchase or sell securities either as principal or agent for the customer, possess investment discretion on behalf of a customer, or engage in proprietary trading of securities or market-making activities). However, prior comments have expressed concern regarding whether the prohibition on accepting orders from customers to purchase or sell securities would impact an LCFB's activities in recommending M&A transactions or particular structures to its clients. We believe this potential confusion should be explicitly clarified. In addition, as the use of the term "customer" with respect to an LCFB is confusing, in the context of many other FINRA rules, we agree with others that the use of a distinctive word such as "client" would be a better fit for LCFBs.

   C. ***What is the likely impact to an LCFB , other broker-dealers and their competitors of adoption of the LCFB rules?*** For Q Advisors, the new category of LCFB would provide minimal benefits as an alternative to our current registration. Under the LCFB rules, we would still be required to pay fees to SIPC (so far); have a PCAOB-approved auditor; obtain a securities dealer blanket bond (though we do not hold securities for customers); conduct AML testing (though every two years rather than annually) - despite the fact that the definition of an LCFB excludes carrying or maintaining customer accounts; and generally be subject to the remainder of our current regulations, though in some cases "streamlined" ones. Other, unregistered brokers (such as those described in the January 2014 SEC No-Action letter, see below) would retain an economic advantage. However, our clients appreciate our registration, and the new LCFB category as currently envisioned would not provide us with enough benefits to make it worthwhile to switch.

D. ***Registration categories for principals and representatives.*** There does not seem any point to us in limiting principals' and representatives' registrations; the limits on an LCFB's activities would control the actions of each person associated with the firm. The proposed limitations would merely unfairly limit individuals' job mobility.

E. ***Does an LCFB normally make recommendations to customers to purchase or sell securities?*** Please see 4.B. above. In addition, we do not "accept orders" from clients, *per se* (i.e., in the retail customer sense), but making recommendations to our clients in the M&A or private placement realm is a large part of what we do. If the language in the proposed rule is likely to lead to confusion on this point, it should be further clarified.

F. ***Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014 (the "M&A Broker Letter"), impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?*** Yes, we think it is likely that most firms that are currently unregistered will remain so after the issuance of the M&A letter, so long as their activities fall within the parameters set forth therein. If a firm sometimes diverges from that model (e.g., a buyer in a client transaction will not "control and actively manage" a purchased entity), it may determine that it must register as an LCFB. On the other hand, the financial and regulatory differences between a regular BD and an LCFB are minimal, so such an M&A Broker might decide to register as a full BD instead.

Thank you in advance for your attention to these issues. Please contact me directly if you have any questions or would like additional information.

Sincerely,

Michael S. Quinn, Member and CCO

M & R
MONAHAN & ROTH, LLC
WWW.MONAHAN-ROTH.COM

Lisa Roth
930 First Avenue
San Diego, CA 921[illegible]
Phone 6[illegible]9-283-15[illegible]

April 28, 2014

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

I have collaborated with the Third Party Marketer's Association (3PM) to develop comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider the thoughtful and informed commentary submitted by 3PM, which I support in its entirety.

For many years, decades even, industry professionals including myself have advocated for smarter rulemaking regarding certain sub-sectors of the FINRA membership; mostly small firms. This particular sector (corporate finance BDs) has been a central target due to the unique challenges of conforming to FINRA rules. I, along with others, have made presentations to FINRA staff, the Small Firm Advisory Board, the PCAOB and SIPC in hopes of fostering a clear understanding of the manner in which LCFB firms operate, the risks associated with our businesses, relative cost and impact of rulemaking, and concepts for rule changes that would better serve the mission of our regulators.

With respect to the particular LCFB initiative, it was communicated that steps to clarify this segment of the industry and develop a unique rule set had the interest and support of FINRA's CEO, Rick Ketchum. So, BD executives spent considerable time meeting amongst ourselves to vet ideas, draft concept releases, discuss our FINRA examination experiences and develop best practices. We also met with FINRA senior staff to discuss and describe the scope and associated risks of relevant business models. This substantial effort was undertaken with the goal of assisting FINRA in developing a better understanding of LCFB firms. It is somewhat disappointing then, that fundamental concepts of the LCFB business model are not reflected in the proposed rule set. Notwithstanding my appreciation for FINRA's contribution in getting to the stage of a rule proposal, I believe it is important to overcome this communication breakdown. After all, LCFBs represent approximately 10% of the FINRA membership.

Following the release of 14-09, members of 3PM reconvened a working group intent on more clearly articulating the business we conduct. This time, we considered fundamental governing principles like 'know your customer'.

CIP and suitability. We addressed the potential for [illegible] misunderstandings and unintended consequences in the context of a rulemaking regime. We challenged ourselves to find a way to present our ideas in a manner that would overcome whatever communication failures had previously transpired.

It is my sincere belief that we have furthered our goal, crystallizing foundational concepts in the 3PM letter. In it, we propose the elimination of troublesome sounding words (like "customer"), tightening up suitability requirements relevant to the timing of placements (such as a requirement for an ongoing due diligence process) and addressing the functional roles and required qualifications of counterparties (such as federally regulated intermediaries). We directly addressed each of questions posed in the Notice.

I know that you will read the 3PM letter, and likely judging by its length and scope you will appreciate the effort that went into the presentation of comments, ideas and recommendations. What I wanted to convey in this letter of mine, is a bit of the back-story in hopes that you will leverage the contribution of the industry in furthering the concept through to implementation.

Best regards,

Lisa Roth
President, Monahan & Roth, LLC

39 Broadway, Suite 3300, New York, New York 10006-3019

Via email: pubcom@finra.org

April 28, 2014

RE: Regulatory Notice 14-09:
Limited Corporate Finance Brokers

Integrated Management Solutions USA LLC ("IMS") is pleased to comment on Regulatory Notice 14-09 ("RN 14-09"), Limited Corporate Finance Brokers ("LCFB"). IMS is one of the largest providers of compliance consulting and financial accounting services to the financial services industry, providing such services to about 100 FINRA members, among others types of financial services firms.[1] We counsel clients daily on the scope of permissible broker-dealer activities under various FINRA, SEC and other rules. At any one time, we have several New Member Applications or Continuing Membership Applications submitted to FINRA on behalf of clients. We believe that our regular, daily experience with FINRA's membership categories and rules, SEC and other rules, and how they are implemented by the various regulators, enables us to assess the impact of RN 14-09 on current or future FINRA members from both a regulatory and business perspective.

[1] The statements in this comment letter incorporate the views of IMS, not those of our clients.

<u>The Regulatory and Congressional Landscape for Advisory Services since Dodd-Frank</u>

FINRA's LCFB proposal must be evaluated in context with other recent SEC and FINRA actions taken under both the Dodd-Frank and JOBS Acts, as well as pending Congressional legislation, with respect to the activities of broker-dealers that do not carry, clear or maintain customer accounts or even handle customer funds or securities (collectively, "<u>Proposals Concerning Non-Custodial Brokers</u>"). These include Crowdfunding[2]; the no-action letters issued to AngelList[3] and FundersClub;[4] the Six Lawyers No-Action Letter regarding the regulation of merger and acquisition brokers (the "<u>Six Lawyers Letter</u>")[5] and FINRA's proposal to improve the membership application process.[6]

Congress has also indicated its interest in taking some of these decisions away from both the SEC and FINRA. In H.R. 2274,[7] the House seeks to amend the Securities Exchange Act of 1934 (the "<u>34 Act</u>") and modify the FINRA registration and regulatory processes when a broker

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[2] SEC Release Nos. 33-9470; 34-70741; File Number S7-09-13; and RN 12-34.

[3] SEC No-Action Letter, dated March 28, 2013, available at http://www.sec.gov/divisions/marketreg/mr-noaction/2013/angellist-15a1.pdf.

[4] SEC No-Action Letter, dated March 26, 2013, available at http://www.sec.gov/divisions/marketreg/mr-noaction/2013/funders-club-032613-15a1.pdf.

[5] SEC No-Action Letter, dated Jan. 31, 2014, revised February 4, 2014; available at http://www.sec.gov/divisions/marketreg/mr-noaction/2014/ma-brokers-013114.pdf. We note, somewhat ruefully, given the amount of time that has elapsed, that the Six Lawyers Letter largely incorporates a proposal first made in 2005 by the Task Force of the American Bar Association's Section of Business Law on Private Placement Broker-Dealers ("<u>ABA Task Force Report</u>"). 60 Bus. Law. 959 (2005) or http://www.sec.gov/rules/other/265-23/gvniesar091205.pdf. The ABA Task Force Report contains a very useful analysis of earlier rulings, by regulators and courts, to define the scope of permissible broker-dealer private placement activities. We fully agree with the statement by the Report's authors, as true in 2005 as it is today, that:

> The impetus for this Report is a widely held perception by many members of the Committee mentioned that there exists a major disconnect between the various laws and regulations applicable to securities brokerage activities, and the methods and practices actually in daily use by which the vast majority of capital is raised to fund early stage businesses in the United States. (Id.)

[6] RN 13-29; RN 10-01. In addition, proposed amendments to Regulation A, known as Regulation A-plus, are also part of this liberalizing regulatory trend. Reg A-plus, if adopted, will allow issuers more flexibility when using an exemption from the SEC's registration requirements for securities offerings.

[7] Introduced June 6, 2013

advises the ownership transfer of smaller, privately held companies.[8] The House bill provides for a notice-filing registration procedure and more limited ongoing regulatory compliance requirements.[9] This bill has already been passed by the House.[10] A contemporaneous Senate bill, S. 1923,[11] goes even further. It seeks to amend the 34 Act by exempting from registration brokers who advise the ownership transfer of smaller, privately held companies.

The Fundamental Flaw

Regrettably, there is a fundamental flaw that permeates all of the Proposals Concerning Non-Custodial Brokers, including the LCFB proposal: the failure to regulate on the basis of risk.[12] We believe that an assessment of the business risk that these activities may cause in the marketplace would result in a much simpler, unified regulatory approach to the non-custodial or advisory activities of broker-dealers. Instead of perpetuating the archaic notion that receipt of transaction-based compensation automatically requires registration as a broker-dealer,[13] the analytic focus of all regulators should be on risk and risk management. As discussed below, these multiple Proposals Concerning Non-Custodial Brokers have resulted in the Balkanization[14] of financial services activities. Our recommendation would be for a joint committee composed of the SEC, FINRA and NASAA[15] to review the risks inherent in broker-dealer advisory services, with the intent of implementing a simple, unified regulatory approach. This committee

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[8] [illegible]
[9] [illegible]
[10] Passed on January 14, 20[illegible]
[11] Introduced January 14, 2[illegible]
[12] Interestingly, although [illegible] assessment of risk that may [illegible]
[13] We recognize that this c[illegible]
[14] Bal·kan·ize, Bal·kan·ized [illegible] small, quarrelsome, ineffec[illegible] usually ineffectual factions [illegible]
[15] North American Securities [illegible]

[illegible]

What is an LCFB?

Overall, RN 14-09 limits the activities of LCFBs to a short list of exclusive activities. Specifically, the following activities are encompassed:

(1) advising companies and private equity funds on capital raising, the purchase or sale of a business or assets, and corporate restructurings (including, without limitation, a going-private transaction, divestiture or merger);

(2) advising a company regarding its selection of an investment banker;

(3) assisting an issuer in the preparation of offering materials;

(4) providing fairness opinions; and

(5) qualifying, identifying or soliciting potential institutional investors.

Explicitly ineligible for LCFB status are firms that engage in a self-evident range of activities: firms that carry or maintain customer accounts, handle customers' funds or securities, accept customers' trading orders, exercise investment discretion on behalf of customers or engage in proprietary trading or market-making.[16] Collectively, most of these are traditional activities for which FINRA membership is mandatory. Nor may LCFBs engage in transactions involving municipal securities.

Is There a Benefit to Being or Converting to LCFB Status?

If an existing broker-dealer client that already provided only the limited list of services set out in RN 14-09 were to ask us if they should convert to LCFB status, our answer would be a resounding "no!" For a current FINRA member, there is hardly any business or regulatory advantage to changing its status.[17] Nor would we recommend a firm contemplating FINRA registration to seek LCFB status. There are too many intrinsic limitations to LCFB status, as discussed below. This Emperor has no clothes.

Sadly, LCFBs are one of the most poorly thought-out, and useless, proposals FINRA has come up with a long time. Some examples should suffice. There are no demonstrable cost savings for an LCFB firm. Such firms are still subject to the SEC's net capital rules, must file periodic FOCUS Reports, the Supplemental Statement of Income Report and Form Custody,[18] maintain the same books and records as other broker-dealers and must have an annual audit conducted by a PCAOB-registered auditor. A fidelity bond is mandatory. An LCFB must still pay for SIPC coverage because of the definition of "Customer" in the Securities Investor

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[16] Actually, proprietary trading or, specifically certain market-making, does not necessarily trigger a requirement to become a FINRA member. There are many entities that engage in these activities and, as SEC registrants, elect to join a national securities exchange instead of joining FINRA. Many professional proprietary traders are not registered as broker-dealers at all. Moreover, some of the enumerated permissible LCFB activities are currently provided by many parties that are not registered with the SEC and thus are not even eligible for FINRA membership.

[17] We do not regard as a significant advantage the fact that LCFBs won't need to conduct an annual compliance meeting or that they won't need to deal with the regulatory element of the continuing education rule.

[18] Form Custody is particularly strange since by definition there should be virtually nothing for a non-custodial broker to report. Fortunately, it doesn't take much time to complete or file it.

Protection Act of 1970.[19] There are no benefits in terms of the registration process, for either the firm or its Registered Representatives; it can still take up to 6 months and require the filing of many meaningless documents. Under the LCFB proposal, in fact, the Registered Representatives of a firm who have the current standard FINRA licenses would apparently be penalized because they would be eligible for fewer registration categories.[20] The Firm still needs a Chief Compliance Officer and all Registered Persons must conduct the same know-your-customer and suitability[21] analysis as traditional broker-dealers, report outside business activities and are still subject to the firm element of Continuing Education compliance. An LCFB must have an AML Program in place in accordance with a new FINRA rule calling for biennial independent testing as opposed to annual independent testing.[22]

Most shocking is the restriction that LCFBs can only serve corporate issuers and only institutional investors. The failure to include partnership and limited liability company issuers ignores a very significant pool of investment opportunities that many existing FINRA members

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[19] SIPA Sec. 16(2). We note that clients of an LCFB would not benefit from its membership in SIPC except under very unusual circumstances, if any.

[20] Though the text of RN 14-09 seems to indicate that this is so, the text of the accompanying proposed Rule 121 seems to contradict that notion since it incorporates by reference NASD Rules 1021 and 1031, which clearly do not limit people from maintaining registrations so long as they remain active in the investment banking or securities business. We note that the proposed Rule 123 seems to exclude or disregard proposed Rule 121.

In addition, we continue to be appalled by the perpetuation of what we call the current "use it or lose it" rules where, if a registration is not used for two years, it lapses. We believe that the securities industry is the only one whose professionals lose their licenses even if they leave and use the competencies of those licenses in some related venue, such as when a sell-side person works on the buy-side for a few years, causing his or her licenses to lapse.

There are other professions where licenses do not lapse in a manner requiring requalification by examination. For example, we are aware of an attorney who has decades of experience as a prosecutor and in the private sector, too. She currently is employed by an agency of the United States government and when she finishes her tenure there, we doubt that this current member of the New York Bar would be required to requalify by examination to resume practicing law. Why should SEC Chair Mary Jo White be treated any differently than securities industry professionals, especially seasoned ones, who leave broker/dealers? We are also reminded that the FINRA person who is FINRA's designated contact for RN 14-09 and the Chairman and CEO of FINRA are both members of the D.C. Bar and we doubt that they would need to requalify by examination in order to practice law either.

[21] LCFB Rule 211(a) specifically spells out the suitability analysis to be undertaken with respect to retail customers, yet LCFBs are not authorized to transact business with retail customers. Who edits these proposed rules?

[22] At least the proposed rule does not define the time period between testing activities based on the calendar year as does current Rule 3310. This is wise.

service by raising money for non-corporate private equity funds or hedge funds. We regard this as a classic error of ignoring a huge constituency of FINRA members that raise money for those issuers. In addition, by ignoring high-net worth individuals, FINRA ignores a key customer base for many hedge funds — supposedly, the very client base an LCFB is intended to serve. These blatant omissions also demonstrate FINRA's failure to understand business practices and the market place. By ignoring other well-established and understood categories of investors, such as "qualified purchasers," FINRA eviscerates the utility of, and sabotages, the LCFB proposal.[23]

What is truly dismaying is these activities are subject to a set of newly proposed LCFB Rules that explicitly incorporate many of the existing FINRA Rules. Rather than have a succinct, useful set of rules that would, of necessity, be incorporated into an LCFB's WSPs, two sets of rules must be consulted to determine the appropriateness of a firm's business activities. Most of the proposed LCFB Rules merely parrot existing FINRA and NASD Rules. That clumsy approach alone would deter many firms from requesting LCFB status because it is a compliance trap waiting to happen. We sincerely hope that this approach of mandating a separate set of rules (currently, more than 45 separate rules), coupled with explicit references to other FINRA Rules, as the price of admission for a supposedly simplified regulatory status dies a very quick death.

We are baffled by FINRA's continued insistence on net capital (recognizing it is an SEC Rule) as the price of entry into the proposed new category of FINRA membership. Given the limited risk and scope of activities of an LCFB, in particular, and in the other carve-outs in the Proposals Concerning Non-Custodial Brokers, in general, we believe the net capital rule serves

[23] We read the endnotes of RN 14-09 wherein FINRA expresses concern about opening the floodgates of the new member category to serve accredited investors who may not be nearly as sophisticated as institutional investors. On the other hand, there are many potential investors that are sophisticated though they are not necessarily institutional. The authors of this letter regard themselves as being sufficiently sophisticated. Why should we not be able to be served by this new category of FINRA member?

no benefit either as a measure of fiscal integrity or as a meaningful barrier to entry into the business covered by the LCFB rules. We believe that, alternatively, the net capital rule should be replaced by a requirement to carry a significant insurance bond that could cover more than just what the existing fidelity bond rule covers. Reliance on market-based insurance underwriting standards, with insurers having their money and reputations on the line, would provide more realistic investor protection. Non-custodial brokers have no need for annual audited financial statements that no one reads or relies upon other than the regulators. With no customer funds or securities at risk, even the filing of periodic FOCUS Reports by non-custodial brokers is of marginal, if any, utility.

What this LCFB proposal appear to be is a last-minute attempt by FINRA to catch-up as the SEC begins to exempt certain activities from broker-dealer registration. If this is the best FINRA can do, the horses have already escaped past the barn door. It seems apparent to us that FINRA drafted the proposed LCFB Rules without hearing the concerns of many industry experts. Perhaps FINRA conferred with some industry participants who prefer the status quo since they are currently subject to it anyway. Members of a club enjoy preferences when the threshold for membership in the club remains high. After all, their thinking is that since they had to run through the gauntlet of the FINRA membership process, why shouldn't new participants do the same?

Effective regulation begins with an assessment of risk. A drastic re-evaluation of the role of regulators for firms with limited risk with respect to customers and the marketplace is needed. This should serve as a wake-up call to FINRA and other regulators.

<u>Why the Balkanization of Financial Services Activities?</u>

We have watched with great interest as both the SEC and FINRA have begun carving out certain broker-dealer activities from the maw of mandating FINRA registration for those receiving transaction-based compensation. Clearly, this has also prompted a Congressional response. With Crowdfunding, the SEC recognized the limited risk if an issuer were willing to raise only up to $1 million. Under the AngelList, FundersClub and Six Lawyers Letters, people engaged in certain restricted advisory activities can avoid SEC registration, presumably again because of the limited risk their activities create for investors. Under FINRA's proposals in RN 13-29, there are hesitant steps to simplify and improve the membership application process. With LCFBs, FINRA apparently acknowledges that institutional investors don't need the same set of protections as retail customers. What's new about that?

This piecemeal approach to regulating carved out activities is time-consuming and inefficient. Instead, FINRA, in conjunction with the SEC and NASAA, should be proposing rules that demonstrate sophisticated analysis based on risk, economic realities and financial and functional distinctions. Of course, FINRA can't do this unilaterally. Nor would such action, or the continued Balkanization of regulatory approaches, be cost effective. What the industry needs is a simplified, rational and uniform approach to the regulation of broker services. This would also benefit the end-users of such brokerage services. The key dictates for such an undertaking should be risk assessment and cost efficiency. The industry understands this; our customers expect it. Our regulators should be promoting customer protection and market integrity but not through the continuation of rules that are complex and often counter-productive. Rules should not have unintended consequences that are worse than what the rules were designed to prevent.

* * * * *

Thank you for the opportunity to comment on RN 14-09. Should you have any further questions, please feel free to call Howard Spindel at 212-897-1688 or Cassondra Joseph at 212-897-1687, or contact us by e-mail at hspindel@intman.com or cjoseph@intman.com, respectively.

Very truly yours,

Howard Spindel
Senior Managing Director

Cassondra E. Joseph
Managing Director

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

April 2, 2014

Re: Request for Comment: Limited Corporate Financing Brokers
Regulatory Notice 14-09

Dear Ms. Asquith,

The AIW, LLC team comprised of experienced American Society of Appraisers and National Association of Certified Valuation Analysts, has conducted thousands of engagements for businesses across hundreds of Standard Industrial Classification and North American Industry Classification System codes for diverse purposes. AIW appreciates the opportunity to submit this comment letter on the proposed rule set for Limited Corporate Financing Broker ("LCFB").

Issue Statement

As a whole, does the proposed rule, the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014, and Senate Bill 1923 ("the bill"); **prevent** a safe harbor for bad actors, money laundering or the funding of terrorism?

Brief Answer

No. The proposed rule for LCFB's recognizes the need for a Client Identification Program (CIP) (rule 209) along with an Anti-Money Laundering Compliance Program (AML) (rule 331) but for "institutional investors" only.[1] Meanwhile, the SEC no-action letter and the bill provide a safe harbor for Private Placement transactions involving "accredited investors." FINRA has established that they have "...uncovered serious concerns with the manner in which firms market and sell private placements to accredited investors."[2] Together, the proposed rule, the SEC no-action letter, and the bill create a critical flaw in the oversight necessary to ensure the illegal and insidious activity of some unregulated, unlicensed, and unsupervised M&A Brokers do not receive a free pass. This flaw places our national security at risk.

[1] FINRA Regulatory Notice 14-09 Attachment A.
2 *Id.* Pg 9.

Statement of Facts

According to BizBuySell, the largest marketplace for sale listings with inventory of over 45,000 businesses for sale, the transfer of securities is continuing,[3] predicting approximately $10 trillion will be transferred. The majority will be in privately held stock in privately held businesses,[4] giving criminals and terrorists' opportunity if these transactions go unmonitored as proposed in the rule, the bill, and the SEC no-action letter. Such sales imply there will be gaps between regulatory rules and statutory requirements, creating fertile ground for money laundering, embezzlement, terrorist financing, public corruption, and racketeering.[5] The U.S. Department of Treasury estimates as much as $15 to $20 million per year was laundered internationally to the Al Qaeda organization responsible for the September 11, 2001 attacks on the United States.[6] Stanford School of Law reported an annual damage estimate of nearly $700 billion in 2007 due to civil securities fraud.[7] The rules included in the Bank Secrecy Act of 1970 are tools to assist against AML and the funding of terrorism. The CIP and AML are now outlined under the "Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001" - the USA PATRIOT Act.[8]

Unregistered M&A Brokers and other unregistered intermediaries will avoid scrutiny under the SEC no-action letter, the bill in current form, and the proposed rule. These unregistered individuals, in addition to forgoing any oversight, will be able to conduct business without having to follow AML procedures along with CIP, which is an integral part of AML.[9]

CIP assists the U.S. Department of Treasury with fighting terrorism funding, combating money-laundering activities, and providing investor protection.[10] Terrorists and criminals use money laundering and shell companies to receive and distribute illicit funds by purchasing all or substantially all of the assets of a business enterprise with cash. It is imperative that unregistered M&A Brokers be required to comply with CIP.

To disguise criminal or terrorist activity, criminals may merge or acquire businesses that might engage in legitimate transactions to establish credibility in the business community. Terrorists groups require significant assets to create and service the infrastructure of the group. Terrorists and criminals often use stolen or falsified identification to pay for their operations.[11] This allows terrorists to avoid watch lists, assist in terrorist funding transactions and gain access to restricted areas[12]. It is even easier to obscure intentions in transactions when CIP is not followed by the

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[3] BizBuySell, Available at http://www.bizbuysell.com/news/media_insight.html
[4] Jackman, R.F., & Christman, P.G., *The $10 Trillion Opportunity* 22 (2nd ed. 2005).
[5] Association of Certified Fraud Examiners, *Financial Institution Fraud* 17 (2009).
[6] Shawn Turner, *U.S. Anti-Money Laundering Regulations: An Economic Approach to Cyber laundering*, 54 Case W. Res. L. Rev. 1389, (2003).
[7] *Securities Fraud*, 24 Fraud Mag. 57 (2009).
[8] 115 STAT 272 § 351-352 (2001).
[9] FINRA, *Anti-Money Laundering* Available at http://www.finra.org/Industry/Issues/AML/
[10] 68 Fed. Reg. 25091 (May 9, 2003).
[11] Scott, K.H., *MSU lab helping FBI hunt down terrorists*. (Mar. 11, 2003). Available at www.allbusiness.com/public-administration/955156-1.html
[12] Gartenstein, D., & Dabruzzi, K., *The convergence of crime and terror: law enforcement opportunities and perils*., Center for Policing Terrorism, (Mar. 26, 2007). Available at

unregistered M&A Broker. Enforcement agencies are aware that money laundering occurs in the private sector but there has been little reporting of money laundering and possible terrorist financing issues among the clients of private-sector business transactions.[13]

Discussion of Law

I encourage staff to read cases involving M&A Brokers who deal with sophisticated or "accredited investors."

Matthew Smith Company, Inc. v. Donald Chill

United States Commodity Futures Trading Commission v. Hunter Wise Commodities...Fred Jager 9:12-cv-81311

The Commodity Futures Trading Commission is uncovering and prosecuting those who break the law and is not granting safe harbors. For example see exhibit A.

Conclusion

Harry Markopolos, Certified Fraud Examiner, during his testimony before the Financial Services Subcommittee on Capital Markets said, "My team and I tried our best to get the SEC to investigate and shut down the Madoff Ponzi scheme with repeated and credible warnings."[14]

My first credible warning is an unregistered M&A Broker, engaged as an intermediary, with a safe harbor from oversight, is a disaster waiting to happen. LCFB and M&A Brokers should have the same qualifications and meet the same standards as a FINRA regulated investment banking representative, to include oversight. We have spent too much treasure and blood to allow rule sets excluding "accredited investors", SEC no-action letters, and the bill to become law as it all creates safe harbors.

The solution is:

A. REGISTRATION BY NOTICE-FILING

B. EXAMINATION REQUIREMENTS

B. MONITORING PRIVATE PLACEMENTS

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www.reas.gr/index.php?option=com_content&view=article&id=707&catid=21&Itemid=63.

[13] Shelly, L., & Melzer, S, "The Nexus of Organized crime and terrorism: Two case Studies in Cigarette Smuggling.", *International Journal of Comparative and applied Criminal Justice*, 32(1), 43-63 (2008).

[14] *Chasing Madoff*, 23 Fraud Mag. 36 (2009).

Please contact me with any questions you may have about these comments.

Lou Stough, CFE
Certified Fraud Examiner

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About the author:

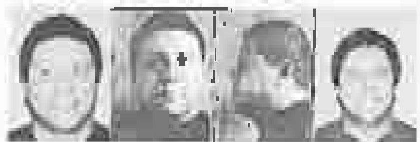
Over thirty years of combined experience in Financial Services and Law Enforcement, specializing in Criminology & Ethics, Financial Transactions & Fraud Schemes, Legal Elements of Fraud, and Fraud Investigation. Degrees and experiences are: Masters in Paralegal Studies, M.B.A., M.S. Administration of Justice, B.S. Criminal Justice, Certified Fraud Examiner (CFE) Deputy Provost Marshal U.S. Army, DOD Hostage Negotiation Course, Indiana State Police Academy, Adjunct Professor, General Securities Principal, Chief Compliance Officer, Registered Representative, Registered Investment Banker and Registered Investment Advisor, Series 7, 24, 66, 79, 99, Insurance License, and Certified Business Intermediary (CBI).

Exhibit A

Wanted by the FBI

WANTED BY THE FBI

LUIS FERREIRA



DESCRIPTION

CAUTION

RWI

Reliance Worldwide Investments, LLC

April 25, 2014

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

RE: Request for Comment, Regulatory Notice 14-09
Limited Corporate Financing Brokers

Dear Ms. Asquith:

Reliance Worldwide Investments, LLC ("RWI") welcomes this opportunity to comment on the proposed rule set for Limited Corporate Financing Brokers.

RWI is a full service general securities firm, licensed to conduct business in 38 States. The firm generates considerable revenues from investment banking activities. While the majority of these revenues are generated internally, a portion of our overall revenues are produced by independent contractor registered representatives who conduct approved outside business activities as business brokers. The majority of these independent contractors limit their securities practice to clearing the securities of their privately-held company investment banking transactions through our firm.

The vast majority of our investment banking clients are privately-held corporations involved in acquisitions, divestitures, and mergers. Typically, these transactions have a debt and/or equity capital structuring component.

With respect to FINRA's request for comment concerning the following issues:

Question 1. Does the proposed rule set provide sufficient protections to customers of an LCFB? If not, what additional protections are warranted and why?

The protections are sufficient to the extent that an LCFB customer, directly or indirectly, benefits from Rule 209 Know Your Customer, Rule 211 Suitability, Rule 221 Communication with the Public, Rule 324 Borrowing From or Lending to Customers, Rule 327 Outside Business Activities of Registered Persons, Rule 331 Anti-Money Laundering Compliance Program, various supervisory rules etc.

However, our firm would suggest the FTC Red Flag Rule should also apply to LCFBs. Even though there are no covered accounts per se, the LCFB would be in possession of certain confidential and sensitive information regarding their customers. It is reasonably foreseeable that those customers might be exposed to risks associated with identity theft.

[illegible]

Office Loca[illegible]
[illegible]
[illegible]
60089

Mailing Address
[illegible]
[illegible]
[illegible]

P: [illegible]
F: [illegible]

[illegible]
[illegible]

Question 2. Does the proposed rule set appropriately accommodate the scope of LCFB business models? If not, what other accommodations are necessary and how would customers be protected?

To the extent that an LCFB's business model would be providing investment banking services (advising companies regarding the purchase or sale of a business or assets, or corporate restructuring, or divestitures or mergers) to customers who are privately-held corporations, the answer would be no.

An analysis of U.S. companies by size reveals that over ninety-nine percent of businesses generate less than $50 million in annual revenues (U.S. Census Bureau, 2009). Established small to mid-size private businesses (operating for 3 years or more) have annual sales ranging from about $1 million to $75 million. Best estimates indicate there are approximately 8.1 million established businesses in the U.S. Factoring in companies with multiple owners, there are approximately 10.2 million owners. (davemead.blogspot.com/2012/02 baby-boomers-again-think-about-selling.html).

The vast majority of the purchasers of these privately-held companies are private equity groups and accredited investors.

In 2013, nearly 40% of all private equity deals were valued below $25 million while 80% were valued below $100 million (*Pitchbook* 4Q 2013 *Private Equity Breakdown*, p. 9).

There are 2,797 private equity firms headquartered in the United States. The largest investors in private equity include public and private pension funds, endowments and foundations, which accounted for 64% of all investment in private equity in 2012. And, during the last five years, private equity has invested almost $30 Billion in more than 1,987 U.S.-based companies that had filed for bankruptcy. (http://www.pegcc.org/education/fact-and-fiction).

To our firm's knowledge, there is no publicly available information regarding the number of private equity groups that qualify as institutional investors.

If FINRA excludes accredited investors and private equity from the list of potential investors a LCFB could "qualify, identify, and solicit," the pool of potential transaction participants available to LCFBs would be severely limited. Such a limitation would represent a tremendous disadvantage, from a competitive perspective. We are firmly convinced this factor alone would preclude firms that service this substantial marketplace from considering LCFB registration.

Given FINRA's "serious concerns" cited in Endnote 3 to Regulatory Notice 14-09, additional safeguards would be required to adequately protect investors from "the manner in which firms market and sell private placements to accredited investors." Without further specificity on this issue, it is not possible for our firm to provide constructive suggestions regarding additional customer protection, at this time. We find this statement by FINRA quite disturbing, and look forward to the future issuance of applicable guidance, FAQs, etc. on this matter.

From a practical perspective, we strongly urge FINRA to consider allowing LCFBs to conduct business with accredited investors, and incorporate adequate safeguards into the proposed rules addressing the "serious concerns" identified by FINRA regulatory programs. It would also seem prudent to apply those new rules to all applicable Broker-Dealers as well.

I cannot stress strongly enough -- our firm believes limiting the parties that could be "qualified, identified, and solicited" to institutional investors (thereby excluding accredited investors and private equity groups), would eviscerate a LCFB's ability to conduct investment banking business in its privately-held customer's best interests.

Question 3. Is the definition of "limited corporate financing broker" appropriate? Are there any activities in which broker-dealers with limited corporate financing functions typically engage that are not included in the definition? Are there activities that should be added to the list of activities in which an LCFB may not engage?

It is always difficult to know when broader terms with "less specificity" provides the best, workable solution. However, other potential activities performed for privately-held companies that might be considered for inclusion would be:

- Advise and assist in preparing a business for sale
- Advise customer regarding the value of the business
- Advise and Assist customer in preparing financial modeling
- Advise about financing alternatives and financial impact
- Assist customer is evaluating prospective/competing offers
- Advise about transaction structures, terms and conditions
- Advise and assist customer in preparing for due diligence
- Advise about commonly recurring business transition issues
- Acting solely as a Finder (introducing potential parties to a transaction)
- Provide expert witness and litigation support services

Question 4. Are there firms that would qualify for the proposed rule set but that would choose not to be treated as an LCFB? If so, what are the reasons for this choice?

Yes. See response to Question 2 above, regarding accredited investors and private equity groups and the limitation imposed by restricting "qualifying, identifying or soliciting" to institutional investors.

Question 5. What is the likely economic impact to an LCFB, other broker-dealers and their competitors of adoption of the LCFB rules?

As proposed, there is di minimis financial advantage to an existing broker-dealer in applying for LCFB registration.

If asked, most FINRA Members would probably tell you they would like to see the direct, and indirect, costs of membership reduced. I'm sure you won't be surprised to know they would also like their taxes to go down as well! However, we are all realistic enough to understand there are costs associated with being in this industry, and that we all have to pay our own fair share. Psychologically, it is always easier to bear that burden if we perceive there is a value proposition created, and substantive benefit provided, as a result of the expenditure of those funds.

In the spirit of that commentary, our firm sees six cost reduction areas FINRA may wish to consider. Some combination of these suggested items and others might go a long way toward creating a value proposition, and thereby increase the attractiveness of an LCFB to prospective candidates:

- PCAOB Audit – Consider establishing criteria under which a "Review" would be conducted, rather than the more expensive PCAOB Audit, such as:
  - Under a certain revenue or asset size
  - Firms who do not borrow money
  - Firms who have no indirect or external investors
  - Firms who do not issue fairness opinions

  As LCFBs do not carry or maintain customer accounts, hold or handle customer funds or securities, exercise discretion over customer accounts, or engage in proprietary trading or market-making, there is less risk to investors associated with this business model.

- SIPC – Reduce or eliminate the requirement for an assessment on privately-held company securities transactions, as it is outside the general scope of intended SIPC insurance protection.

- Fidelity Bond – Reduce or eliminate the requirement for a bond. As stated above, since LCFBs do not carry or maintain customer accounts, hold or handle customer funds or securities, exercise discretion over customer accounts, or engage in proprietary trading or market-making, there is less risk to investors associated with this business model.

- FINRA Revenue Assessment – Reduce the assessment calculation based upon an analysis of the lower cost to FINRA associated with regulatory oversight of an LCFB as compared to other Broker-Dealer business models.

- Net Capital Requirement – For some of the same reasons cited in the PCAOB Audit discussion above, "right-size" the amount.

- Continuing Membership Application process – Reduce the cost, and streamline the process, whereby a LCFB would be able to return to its prior Broker-Dealer status (as long as it met the current requirements of that prior status). The requirements/process as stated in the proposed rule set may very well be perceived as a disincentive to many Broker-Dealers who might otherwise consider LCFB registration.

Question 5. FINRA welcomes estimates of the number of firms that would be eligible for the proposed rule set.

Our firm has no specific estimate, however, it is aware of certain information which may provide some insight on this issue:

- Within the securities industry: On December 20, 2013, FINRA Small Firm Governors Norensberg, Carreno, and Keenan sent an email entitled "Small Firm Update" regarding the FINRA Board of Governors December 2013 meeting. In this email it was stated that the forthcoming LCFB proposal was "expected to affect nearly 700 broker-dealers." No information was provided alluding to the basis for such an expectation. According to Chairman Ketchum's Management Report on Financial Operations, "as of December 31, 2012, FINRA oversaw nearly 4,300 broker firms . . ." Therefore, if the 700 broker-dealer number is assumed to be correct, approximately 16.3% of all current FINRA broker-dealer firms would be affected.

- Outside the securities industry: A Business Broker is generally defined as a person who assists individuals in selling or buying a small or mid-size business. The activities of a business broker can range from simply introducing two parties to more complicated functions such as analyzing a business's financial statements, marketing the business for sale, and assisting the client's other advisors in negotiation the terms of a transaction. **It is estimated that there are approximately 3,000 – 4,000 business brokers in the United States.** A business broker is often utilized by companies who are interested in selling, but not large enough to attract the interest of traditional investment banks. Most investment banks work on transactions with companies generating in excess of $100 million dollars in revenues. **An analysis of U.S. companies by size reveals that over ninety-nine percent of businesses generate less than $50 million in annual revenues.** It is this large, underserved market that business brokers service. (http://www.cvbba.com/images/APMAA_Reg_Issues_3-17-2010.pdf)

  Our firm believes business broker firms are typically small businesses composed of one to ten producing brokers. Shane Hansen, an attorney who represents business broker associations testified in a U.S. House of Representatives hearing on June 12, 2013: "Accordingly, a very high percentage of M&A brokers are not registered with the SEC and so, technically, are violating the registration requirements in federal securities laws today." Therefore, our firm believes it would be safe to say that in excess of 300 business brokerage firms would be eligible to become securities licensed, and such firms could potentially qualify under the proposed rule set. Although, we consider it unlikely that any of them would have an interest, in no small part due to the M&A Broker No-Action Letter that was issued by the SEC on January 31, 2014, the passage of H.R. 2274 by the U.S. House of Representatives (422 to 0), and the current bill in the Senate Banking, Housing, and Urban Affairs Committee (S. 1923).

As our firm does not anticipate any meaningful number of Broker-Dealers electing to apply for LCFB registration, nor do we believe any firms new to the industry will be filing applications for LCFB registration, we do not anticipate a noteworthy impact.

Question 7. Proposed LCFB Rule 123 would limit the principal and representative registration categories that would be available for persons associated with an LCFB. Are there any registration categories that should be added to the rule? Are there any registration categories that are currently included in the proposed rule but that are unnecessary for persons associated with an LCFB?

It would appear appropriate to include Direct Participation Programs within the scope of the LCFB, as most of these transactions typically occur through private placements.

Question 8. Should principals and representatives that hold registration categories not included within LCFB Rule 123 be permitted to retain these registrations?

Yes, subject to the principals and representatives: (1) being associated with a LCFB firm, and (2) remaining current with the regulatory element continuing education requirements during the entire "inactive" period for non-LCFB categories of registration.

FINRA might also wish to consider instituting a prescribed inactive period (for example, 5 years) after which the principals and representatives would have to requalify for those registration categories by examination; however, this prescribed inactive period would be superseded by the current 2 year rule in the event a U-5 was filed and the registrant did not associated with another LCFB or broker-dealer.

Question 9. Does an LCFB normally make recommendations to customers to purchase or sell securities? Should an LCFB be subject to rules requiring firms to know their customers (LCFB Rule 209) and imposing suitability obligations (LCFB Rule 211) to an LCFB?

Yes. The activities listed in the proposed rule set include the words "advising an issuer" and "advising a company" – and it is clearly understood that there is almost always a fee involved when providing such services. Thus, the act of advising, be it oral or in writing, involves either an actual recommendation or some form of implicit recommendation by the person providing the advice. Our firm believes this is true irrespective of whether the advice provided is acted upon or not.

Not only do we believe K-Y-C and Suitability apply to LCFBs, we also believe AML and the FTC Red Flag Rule apply (as previously discussed in Question 1 above).

Question 10. Does the SEC staff no-action letter issued to Faith Colish, et al., dated January 31, 2014, impact the analysis of whether a firm would become an LCFB? Is it likely that some limited corporate financing firms will not register as a broker consistent with the fact pattern set forth in the no-action letter, or will they register as an LCFB?

Most firms eligible for LCFB registration are also effectively able to operate within the parameters set forth in the M&A Broker SEC No-Action Letter issued on January 31, 2014. There is no logical reason for such firms to incur the regulatory compliance obligations and associated costs when presented with a "free pass." This M&A Broker No-Action Letter gives new meaning to the old salesman's pitch, "no cost and no obligation."

Unfortunately, the SEC has disregarded investor protection in favor of a small, vocal special interest group who seeks to avoid regulatory oversight and has spent in excess of $700,000 (to date) in attorney and lobbyist fees to achieve that result.

For years, Attorney Shane Hansen has represented M&A Broker associations in their efforts to secure exemption from registration, initially with the SEC and other regulators, and now in their efforts to secure an exemption through legislation (H.R. 2274 and S. 1923).

In his written statement, testifying under oath on June 12, 2013 to the United States House of Representatives Committee on Financial Services, attorney Hansen states:

> "Accordingly, a very high percentage of M&A brokers are not registered with the SEC and so, technically, are violating the registration requirements in federal securities laws today. Their registration violations may put their clients' transactions at risk of being rescinded if the post-closing business does not run as hoped or is run into the ground by the buyer. Registration violations put the M&A brokers at risk for regulatory enforcement and sanctions, as well as their livelihood ..."

If these business broker associations are unsuccessful in their efforts to effect legislation sympathetic to their cause, the vast majority of their membership will unswervingly continue to ignore and violate securities laws in their ordinary course of conducting business -- just as they have since 1985. It is simply unconscionable to allow this group to continue to violate securities laws to the potential detriment of investors involved in M&A Broker transactions.

In 1985, the U.S. Supreme Court ruled in *Landreth Timber Co. v. Landreth*, and a companion case *Gould v. Reufenacht*, that transactions involving the sale of closely-held company stock are "securities" within the meaning of the Securities Act of 1933, and require compliance with Section 15(a) of the Exchange Act (if applicable).

When was the SEC Division of Trading and Markets granted the authority to enact No-Action Letters in potential contraversion to, and/or without deference to, US Supreme Court decisions? I personally believe this is a dangerous path to traverse. I can only assume this has occurred under the guise of "assisting the Commission in establishing rules and issuing interpretations on matters affecting the operation of the securities markets." Second guessing the U.S. Supreme Court and creating an exception inconsistent with its repetitive, consistent decisions may very well border on unbridled arrogance. What prospective benefit is so overwhelmingly that it would justify such actions?

I urge FINRA, in the strongest possible way -- encourage the SEC to reconsider the direction it is taking on this matter and the conflicting message it is sending to licensed M&A Brokers, unlicensed M&A Brokers, private equity groups, institutional investors, and individual investors.

We should not be surprised to see a flood of business cards with the title "Investment Banker" on them, including attorneys and CPAs who now believe the May 17, 2010, SEC **Denial of No-Action Request** has been superseded. This denial was issued with regard to a letter submitted by the law offices of Brumberg, Mackey & Wall, P.L.C. ("BMW").

The SEC cited several reasons for the denial, but one of them was:

> "Moreover, the Staff believes that that receipt of compensation directly tied to successful investments in ... securities by investors introduced ... by BMW [the law firm] would give BMW a "salesman's stake" in the proposed transactions and would create heightened incentive for BMW to engage in sales efforts. Accordingly, the Staff believes that your proposed activities would require broker-dealer registration."

M&A transactional attorneys typically utilize either hourly billing for the services rendered, or one of three types of alternative fee arrangements: (1) a fixed fee, (2) a fixed fee with a collar, or (3) a "broken deal"/success fee. Until the M&A No-Action letter was issued, securities laws preclude lawyers and CPAs from receiving contingent compensation as a percentage of the total price of a successfully completed transaction. Now that has changed. Does the SEC no longer believe there is a "salesman's stake" involved ... or does that just not matter any longer?

WHAT IS THE SCOPE OF THIS PROBLEM ... HOW MANY WILL BE AFFECTED?

Consider the published statistics:

1. The SBA indicates:
   a. There are **23 million** small businesses in America that account for **54% of all U.S. sales**,
   b. Small businesses provide **55% of all jobs**, and
   c. The number of small businesses in the U.S. has increased 49% since 1982.

2. Best estimates indicate there are approximately **8.1 million established businesses in the U.S.** Factoring in companies with multiple owners, there are approximately 10.2 **million owners**.
   a. Established businesses are defined to be companies in business for at least 3 years and having a work location outside the owner's home, and

b. Well established small to mid-size private businesses have annual sales ranging from about $1 million to $75 million.

3. PriceWaterhouseCoopers study determined:
   a. **1 out of every 2** company owners plan to sell their business within the next 10 years, and
   b. People 55 or older own 30 % of all businesses with employees.

4. PriceWaterhouseCoopers Trendsetter Barometer Survey of Business Owners found:
   a. **51%** of business owners were planning to sell their companies to third-party purchasers, and
   b. **14%** of business owners were planning on selling to their employees.

5. Conservative estimates forecast the number of Baby-Boomer owned businesses that will be put on the market for sale in the **next 5 to 10 years will be between 1.36 and 2 million firms, and 2.5 to 3.8 million firms over the next 20 years.**

6. It is estimated that these transaction will result in the transfer of **$10 Trillion** of wealth.

7. Industry estimates indicate **80%** of a small to mid-size business owner's total net worth is attributed to their business.

How is it that this substantial number of individual investors (comprising this group of sellers) – and a like number of buyers – are not deemed to be deserving of regulatory oversight and protection? Especially when these senior citizen sellers are counting on the proceeds from these sales, which for most of them represents a once-in-a-lifetime liquidity event, to fund their retirement.

I personally find this surprising, and very disturbing ...

Is it reasonable, rational or prudent to believe the M&A Broker transaction marketplace can properly police itself? Our firm does not believe so.

Thank you for considering our firms comments, and please contact us if have any questions or require clarification regarding any of our remarks.

Sincerely,

RELIANCE WORLDWIDE INVESTMENTS, LLC

Kenneth Sweet
Managing Member, Principal

JLT Capital Partners
| Business Development For Exceptional Asset Managers |

April 28, 2014

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

JLT Capital Partners LLC is a FINRA member (CRD# 158345) specializing in placement agent services for alternative asset managers. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which I strongly support.

Thank you for your consideration.

Sincerely,

James L. Tovey
Managing Principal

29 Londonderry Road, Windham, NH 03087 | Tel: 603.552.3376 | www.jltcapitalpartners.com
Securities Offered Through JLT Capital Partners LLC | Member FINRA/SIPC

PROFESSOR ANDREW F. TUCH

COMMENTS ON PROPOSED RULE SET FOR LIMITED CORPORATE FINANCING BROKERS (FEBRUARY 2014)

April 28, 2014

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506
Via Electronic Mail (pubcom@finra.org)

Dear Ms. Asquith

I am submitting this letter in response to the invitation by the Financial Industry Regulatory Authority in Regulatory Notice 14-09 to comment on its proposed rule set for limited corporate financing brokers ("LCFBs").[1] In light of the time frame in which FINRA has invited comments, I focus on the implications of the proposed rule set for those LCFBs that engage in traditional investment banking activities.

By way of background, I am a law professor who has researched and written in the areas of securities and financial regulation. In recent years, my writing has focused on the liability of broker-dealers, including investment bankers.[2] The views expressed in this letter are solely my own, and the institutional affiliation provided below is given for identification purposes only.

I. THE DEFINITION OF LCFB

The proposed rule set will apply to LCFBs and persons associated with LCFBs. An LCFB is defined in terms of the activities in which it engages (Proposed Rule 016(h)), and thus the proposed rule set applies to firms, and to persons associated with firms, whose activities do not extend beyond certain enumerated activities (Proposed Rule 014). Generally speaking, the enumerated activities encompass the traditional investment banking activities of advising firms on securities offerings, mergers and acquisitions, and restructurings.[3] The

[1] See FINRA, Regulatory Notice 14-09, Limited Corporate Financing Brokers, February 2014.

[2] Most of my publications are publicly available at www.ssrn.com.

[3] As to the activities traditional performed by investment bankers, see Alan D. Morrison & William J. Wilhelm, Investment Banking. Institutions, Politics, and Law 22 (2007); James D. Cox et al., Securities Regulation: Cases and Materials 115 (7th ed, 2013); and Bruce Wasserstein, Big Deal: 2000 and Beyond 556 (2000).

The term mergers and acquisitions is used broadly to include numerous types of often overlapping transaction categories, including purchases and sales of businesses or assets, going-private transactions and divestitures.

enumerated activities also include assisting in the preparation of offering materials on behalf of an issuer and providing fairness opinions, which are also activities traditionally performed by investment bankers.[4] However, the proposed rule set would not apply to firms that underwrite securities offerings (another traditional investment banking activity). It is nevertheless clear that the proposed rule set would apply to firms that engage in the traditional investment banking activities other than securities underwriting.

II. FINRA Regulation of Investment Banking

To begin, I applaud FINRA for specifically addressing the regulation of investment banking activities. Although these activities are not typically performed by traditional broker-dealers, as FINRA's Regulatory Notice acknowledges, they generally fall within the definition of broker in the Securities Exchange Act.[5] In general terms, I understand that firms and individuals engaging in investment banking activities, including advising on securities offerings and M&A, have registered with FINRA.[6] In legal scholarship, little attention has focused on the requirement for those engaged in investment banking activities to register as broker-dealers. Your proposed rule set is likely to lead to broader discussion of the regulation of investment banking activities and FINRA's role in it – a desirable development.

III. Content of Rules

The proposed rule set includes relatively minor reforms to the content of the rules that apply to firms and individuals engaging in investment banking activities. With the exceptions noted below, the proposed rule set largely includes those rules in FINRA's existing Manual relevant to broker-dealers satisfying the definition of LCFB, although some accommodations have been made for LCFBs. The proposed rules set will provide certainty to LCFBs as to the rules with which they must comply. At the same time, the proposed rule set is unlikely to change the regulatory burden facing LCFBs. It is also a piecemeal set of rules, rather than a broad-based rule set comparable to the conduct rules that apply to other market gatekeepers, such as lawyers and accountants.

The proposed rule set would seem to omit rules concerning two important matters. The first concerns fairness opinions. Rule 5150 has been omitted, an apparent unintended oversight considering the explicit reference to fairness opinions in the definition of LCFB.

[4] The proposed rule set enumerates two other activities: qualifying, identifying, and soliciting potential institutional investors; and advising on the selection of an investment banker. The former activity may well be performed by investment bankers, although it differs from other enumerated activities since its focus is on investors, rather than corporate clients engaging in transactions. The latter activity is clearly not one performed by an investment banker and its inclusion therefore suggests that LCFBs perform activities beyond investment banking.

[5] Securities Exchange Act of 1934 § 3(a)(4)(A), 15 U.S.C. § 78c.

[6] This approach was supported most recently by the SEC in a no-action letter. *See* Letter re: Merger and Acquisition Activities of Foreign Firms in Reliance on Rule 15a-6, SEC No-Action Letter, July 12, 2012, *available at* http://www.sec.gov/divisions/marketreg/mr-noaction/2012/ernstyoung071212-15a6.pdf. However, no-action relief was provided for certain advisers to private-company M&A transactions. *See* Letter re: M&A Brokers, SEC No-Action Letter, January 31, 2014 (revised February 4, 2014), *available at* http://www.sec.gov/divisions/marketreg/mr-noaction/2014/ma-brokers-013114.pdf.

The second concerns rules relating to information barriers. The proposal rule set would benefit from an explicit reference to FINRA guidance on these measures to cabin information flows.[7]

IV. Enforcement of Rules

The proposed reforms overlooks the more pressing issue of the extent to which FINRA enforces its rules against firms and individuals engaging in investment banking activities. As a regulator concerned with deterring its members and their associated persons from harming investors and others, FINRA must be concerned not only with the content of its rules, but also with their enforcement. The proposed reforms suggest no change in FINRA's enforcement intensity against firms and individuals performing investment banking activities.

The issue of enforcement by FINRA of its rules against those engaged in investment banking deserves close scrutiny. In "The Untouchables of Self-Regulation," a paper forthcoming in the *George Washington Law Review*,[8] I examine the extent to which FINRA enforces its rules against both investment bankers and firms for the conduct of their investment bankers. (I define investment banking to include the investment banking activities referred to above; those activities are therefore largely consistent with the activities enumerated for LCFBs in the proposed rule set, but exclude private placement activities). The study covers the period January 2008 to June 2013.

As the paper explains, I find remarkably weak enforcement intensity against investment bankers and their firms. During the 66-month period under investigation, FINRA sanctioned 4,116 individuals and 1,645 firms. Of these 4,116 individuals, only 18 were investment bankers, and only 10 of these were sanctioned for misconduct toward their clients (rather than toward other actors, such as their firms). Of the 1,645 firms FINRA sanctioned, only seven involved the misconduct of their investment bankers.

Applying optimal deterrence theory, the paper argues that the self-regulation of investment bankers offers no credible deterrence against professional misconduct. It further argues that the costs of self-regulation likely exceed its benefits (measured in terms of deterrent force), and therefore that the self-regulation of investment bankers by FINRA should be considered a failure. Of course, these conclusions depend on the view that some wrongdoing by investment bankers and their firms escapes detection and sanction. That view is based on an extensive consideration of empirical evidence (regarding certain forms of misconduct by investment bankers) as well as anecdotal evidence. However, because the underlying level of wrongdoing by investment bankers is unknown, it is not possible to demonstrate conclusively whether FINRA fails to effectively enforce its rules against investment bankers and their firms. Some doubt will inevitably remain.

Nevertheless, the problem may be considered in more concrete terms. As is well-known, Delaware courts often opine on investment banking conduct in the course of adjudicating

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[7] FINRA guidance is provided by NASD, Joint Memorandum on Chinese Wall Policies and Procedures, Notice to Members No. 91-45 (1991) (explaining the "minimum elements" for "adequate" Chinese walls).

[8] The paper will be available on www.ssrn.com in coming days.

disputes in M&A transactions. In 2011, for instance, the Delaware Court of Chancery criticized investment bankers for "secretly and selfishly manipulat[ing] the sale process to engineer a transaction that would permit [their firm] to obtain lucrative … fees."[9] The following year, it criticized a prominent investment banker for failing to disclose a material conflict of interest with his client, a failure the Court described as "very troubling" and "tend[ing] to undercut the credibility of … the strategic advice he gave."[10] The disputes involved alleged conduct that would seem at least to have infringed FINRA Rule 2010, which requires broker-dealers and their associated persons to "observe high standards of commercial honor and just and equitable principles of trade." In both of these cases, the investment bankers involved were registered with FINRA. According to FINRA BrokerCheck, however, none has faced disciplinary action. While not conclusive, this evidence raises questions about FINRA's enforcement activities against investment bankers.

Moreover, the actions that FINRA did bring against investment bankers or firms for the conduct of investment bankers (during the period under analysis) are a rather odd assortment, one suggesting no particular enforcement priorities. I do not mean to belittle some of the actions; although small in number, some involve either individuals from prominent firms or apparently serious misconduct. At the same time, most of the disciplinary matters FINRA did bring against investment bankers or against firms for the conduct of investment bankers would have registered little interest among investment bankers. For example, one investment banker was sanctioned for violating his employer's internal policies while "attempting to procure investment banking and consulting business … from a publicly-traded company."[11] He had used his personal e-mail account (rather than one provided by his firm) to communicate with the potential client and had posted messages about the client on the Yahoo! message board, including "[t]his one looks like a gem" and "[s]till digging into this one but looks like the real deal."[12] FINRA sanctioned another investment banker for embellishing his experience by falsely telling a prospective client that he had advised on a reverse takeover and for misleading another potential client about the work he was doing for it.[13] Not persuaded, the clients went elsewhere – but the banker faced FINRA discipline.[14] Given the nature of these matters, it is surprising that FINRA's enforcement intensity is not significantly stronger than the data in my study suggest.

V. APPLICATION OF THE PROPOSED RULE SET

One further concern with the proposed rule set relates to its application. It will clearly apply to so-called boutique investment banking firms – firms that do not engage in traditional

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[9] In re Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 818 (Del. Ch. 2011).

[10] In re El Paso Corp. S'holder Litig., 41 A.3d 432, 442 (Del. Ch. 2011).

[11] FINRA Letter, No. 2011030840301, Re: Christopher A. Carra, June 29, 2012.

[12] *Id.*

[13] FINRA Letter, No. 2010021116001, Re: Richard S. From, Oct. 5, 2011.

[14] He was fined $5,000 and suspended for associating with a FINRA member for 30 days. *Id.*

broker-dealer activities (such as managing client funds or executing client trades) or in other financial activities, such as commercial banking or asset management. But will the rule set also apply to the broker-dealer affiliates of financial conglomerates – enterprises that engage in a broad and diverse range of financial activities, but whose broker-dealer affiliates may engage in a narrow range of activities?

There is a clear danger is seeking to streamline the rules for financial conglomerates, even for their broker-dealer affiliates that may satisfy the definition of LCFB. Financial conglomerates are significantly more likely to face conflicts of interest than boutique investment banking firms. Otherwise put, financial conglomerates have greater incentives and opportunities than boutiques to engage in misconduct, such as skewing their advice to clients and misusing non-public client information.[15] Empirical evidence confirms these dangers.[16]

I would therefore recommend clarifying the propose rule set to provide that it applies only to broker-dealers who enterprise-wide activities satisfy the definition of LCFB. There is no apparent basis for providing any accommodations to broker-dealers affiliated with financial conglomerates, even if those broker-dealers satisfy the definition of LCFB.

Nevertheless, FINRA must ensure that it does not create unjustified distinctions between investment bankers working for financial conglomerates and those working for investment banking boutiques. After all, these individuals may well perform largely identical functions. Yet, if the proposed rule set applies only to the latter type of firm, those investment bankers would seem to benefit from some regulatory relief. One area in which the proposed rule set provides relief is continuing education requirements. Why so? It is difficult to understand the benefits of imposing education requirements on investment bankers that differ depending on the type of firms employing them. However, there would seem to be merit in tailoring education requirements to the distinctive work that investment bankers perform, whatever business model their employer adopts.

* * *

Thank you for the opportunity to comment on the Regulatory Notice. I would be pleased to discuss these comments further.

Andrew F. Tuch
Associate Professor of Law
Washington University School of Law
atuch@wustl.edu

[15] For further discussion, see Andrew Tuch, Financial Conglomerates and Information Barriers, J. CORP. L (2014) (forthcoming), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2363312.

[16] *Id.*

FRONTIER SOLUTIONS

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in private placements of alternative investments to institutional clients. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Please contact me directly by phone at (404) 879-5130 or via email at dvick@frontiersolutions.com should you have any questions or require further information.

Sincerely,

George Vick

George Vick
Chief Compliance Officer
Frontier Solutions, LLC

FORTRESS
GROUP

April [illegible], 2014

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith

My firm is a FINRA member specializing in private placement of alternative asset funds (private equity, private credit, real estate, and natural resource funds) to institutional investors. I am also a member of the Third Party Marketer's Association (3PM).

I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCBD). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary, which has earned my strong support.

Sincerely,

Bruce A. Williamson

FORTRESS GROUP, INC.
Bruce A. Williamson, CFA
Managing Director & Chief Compliance Officer

HAMERSLEY™
PARTNERS

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

Re: Regulatory Notice 14-09

Dear Ms. Asquith,

My firm is a FINRA member specializing in placement agent services to institutional investors, primarily corporate and public pension plans and investment consulting firms. I am also a member of the Third Party Marketer's Association (3PM). I have had an opportunity to review 3PM's comprehensive comments regarding the rule set proposed by Regulatory Notice 14-09 for Limited Corporate Finance Brokers (LCFB). I urge FINRA's Board to carefully consider 3PM's thoughtful and informed commentary in the attached PDF, which has earned my strong support.

Regards,

Michael Wren

EXHIBIT 5

Below is the text of the proposed rule change. Proposed new language is underlined.

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Capital Acquisition Broker Rules

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010. GENERAL STANDARDS

014. Application of the By-Laws and the Capital Acquisition Broker Rules

All persons that have been approved for membership in FINRA as a capital acquisition broker and persons associated with capital acquisition brokers shall be subject to the FINRA By-Laws (including the schedules thereto), unless the context requires otherwise, and the Capital Acquisition Broker Rules. Persons associated with a capital acquisition broker shall have the same duties and obligations as a capital acquisition broker under the Capital Acquisition Broker Rules.

The terms used in the Capital Acquisition Broker Rules, if defined in the FINRA By-Laws, shall have the meaning as defined in the FINRA By-Laws, unless a term is defined differently in a Capital Acquisition Broker Rule, or unless the context of the term within a Capital Acquisition Broker Rule requires a different meaning.

015. Application of Rules to Municipal Securities

FINRA Rule 0150 shall apply to the Capital Acquisition Broker Rules.

016. Definitions

When used in the Capital Acquisition Broker Rules, unless the context otherwise requires:

(a) "Associated person of a capital acquisition broker" or "person associated with a capital acquisition broker"

The term "associated person of a capital acquisition broker" or "person associated with a capital acquisition broker" means: (1) a natural person who is registered or has applied for registration under the FINRA rules; (2) a sole proprietor, partner, officer, director or branch manager of a capital acquisition broker, or other natural person occupying a similar status or performing similar functions, or a natural person engaged in the investment banking or securities business who is directly or indirectly controlling or controlled by a capital acquisition broker, whether or not any such person is registered or exempt from registration with FINRA under the FINRA By-Laws or the FINRA rules; and (3) for purposes of FINRA Rule 8210, any other person listed in Schedule A of Form BD of a capital acquisition broker.

<u>**(b) "By-Laws"**</u>

<u>The term "By-Laws" means the By-Laws of the Corporation or the FINRA By-Laws.</u>

<u>**(c) "Capital Acquisition Broker"**</u>

<u>(1) A "capital acquisition broker" is any broker that solely engages in any one or more of the following activities:</u>

<u>(A) advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;</u>

<u>(B) advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;</u>

<u>(C) advising a company regarding its selection of an investment banker;</u>

<u>(D) assisting in the preparation of offering materials on behalf of an issuer;</u>

<u>(E) providing fairness opinions, valuation services, expert testimony, litigation support, and negotiation and structuring services;</u>

<u>(F) qualifying, identifying, soliciting, or acting as a placement agent or finder with respect to institutional investors in connection with purchases or sales of unregistered securities; and</u>

<u>(G) effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company through the purchase, sale, exchange, issuance, repurchase, or redemption of, or a</u>

business combination involving, securities or assets of the company, to a buyer that will actively operate the company or the business conducted with the assets of the company, in accordance with the terms and conditions of an SEC rule, release, interpretation or "no-action" letter that permits a person to engage in such activities without having to register as a broker or dealer pursuant to Section 15(b) of the Exchange Act.

(2) "Capital acquisition broker" does not include any broker or dealer that carries or acts as an introducing broker with respect to customer accounts, holds or handles customers' funds or securities, accepts orders from customers to purchase or sell securities either as principal or as agent for the customer (except as permitted by paragraphs (c)(1)(F) and (G)), has investment discretion on behalf of any customer, engages in proprietary trading of securities or market-making activities, or participates in or maintains an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933.

(d) "Capital Acquisition Broker Rules"

The term "Capital Acquisition Broker Rules" means Capital Acquisition Broker Rules 010 through 1000.

(e) "Commission"

The term "Commission" means the Securities and Exchange Commission.

(f) "Customer"

The term "customer" shall not include a broker or dealer.

(g) "Exchange Act" or "SEA"

The term "Exchange Act" or "SEA" means the Securities Exchange Act of 1934, as amended.

(h) "FINRA"

The term "FINRA" means, collectively, FINRA, Inc., FINRA Regulation, Inc. and FINRA Dispute Resolution, Inc.

(i) "Institutional Investor"

The term "institutional investor" means any:

(1) bank, savings and loan association, insurance company or registered investment company;

(2) governmental entity or subdivision thereof;

(3) employee benefit plan, or multiple employee benefit plans offered to employees of the same employer, that meet the requirements of Section 403(b) or Section 457 of the Internal Revenue Code and in the aggregate have at least 100 participants, but does not include any participant of such plans;

(4) qualified plan, as defined in Section 3(a)(12)(C) of the Exchange Act, or multiple qualified plans offered to employees of the same employer, that in the aggregate have at least 100 participants, but does not include any participant of such plans;

(5) other person (whether a natural person, corporation, partnership, trust, family office or otherwise) with total assets of at least $50 million;

(6) person meeting the definition of "qualified purchaser" as that term is defined in Section 2(a)(51) of the Investment Company Act of 1940; and

(7) any person acting solely on behalf of any such institutional investor.

(j) "Member"

The term "Member" means any individual, partnership, corporation or other legal entity admitted to membership in FINRA under the provisions of Articles III and IV of the FINRA By-Laws.

(k) "Person"

The term "person" includes any natural person, partnership, corporation, association, or other legal entity.

(l) "Securities Act"

The term "Securities Act" means the Securities Act of 1933, as amended.

100. MEMBER APPLICATION AND ASSOCIATED PERSON REGISTRATION

101. Electronic Filing Requirements for Uniform Forms

All capital acquisition brokers and persons applying for membership in FINRA as a capital acquisition broker are subject to FINRA Rule 1010.

102. Filing of Misleading Information as to Membership or Registration

All capital acquisition brokers are subject to FINRA Rule 1122.

111. Membership Proceedings

(a) Definitions

All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1011.

(b) Safe Harbor for Business Expansions

All capital acquisition brokers are subject to NASD IM-1011-1.

(c) General Provisions

All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1012.

112. New Member Application and Interview

(a) All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1013.

(b) An applicant for membership that seeks to qualify as a capital acquisition broker must state in its application that it intends to operate solely as a capital acquisition broker.

113. Department Decision

(a) All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1014.

(b) In reviewing an application for membership as a capital acquisition broker, the Department shall consider, in addition to the standards for admission set forth in NASD Rule 1014, whether the applicant's proposed activities are consistent with the limitations imposed on capital acquisition brokers under Capital Acquisition Broker Rule 016(c).

114. Review by National Adjudicatory Council

All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1015.

115. Discretionary Review by FINRA Board

All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1016.

116. Application for Approval of Change in Ownership, Control, or Business Operations

(a) All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1017.

(b) An existing FINRA member that seeks to change its status to a capital acquisition broker and is already approved to engage in the activities of a capital acquisition broker, but which does not intend to change its existing ownership, control or business operations, must file a request to amend its membership agreement or obtain a membership agreement to provide that: (1) the member's activities will be limited to those permitted for capital acquisition brokers under Capital Acquisition Broker Rule 016(c); and (2) the member agrees to comply with the Capital Acquisition Broker Rules.

(c) Subject to paragraph (d) of this Rule, a capital acquisition broker that seeks to terminate its status as such and continue as a FINRA member must file an application for approval of a material change in business operations pursuant to NASD Rule 1017, and must amend its membership agreement to provide that the member agrees to comply with all FINRA Rules.

(d) If during the first year following an existing FINRA member's amendment to its membership agreement pursuant to paragraph (b) of this Rule, a capital acquisition broker seeks to terminate its status as such and continue as a FINRA member , the capital acquisition broker may notify FINRA of this change without having to file an application for approval of a material change in business operations pursuant to NASD Rule 1017. The capital acquisition broker must file a request to amend its membership agreement to provide that the member agrees to comply with all FINRA Rules, and execute an amended membership agreement that imposes the same limitations on the member's activities that existed prior to the member's change of status to a capital acquisition broker.

118. Application to Commission for Review

All capital acquisition brokers and applicants for membership in FINRA as a capital acquisition broker are subject to NASD Rule 1019.

119. Foreign Members and Associates

(a) Foreign Members

All capital acquisition brokers are subject to NASD Rule 1090.

(b) Foreign Associates

All capital acquisition brokers are subject to NASD Rule 1100.

121. Registration Requirements

(a) Status of Persons Serving in the Armed Forces of the United States

All capital acquisition brokers are subject to NASD IM-1000-2.

(b) Failure to Register Personnel

All capital acquisition broker-dealers are subject to NASD IM-1000-3.

(c) Registration Requirements – Principals

All capital acquisition brokers are subject to NASD Rule 1021.

(d) Registration Requirements – Representatives

All capital acquisition brokers are subject to NASD Rule 1031.

122. Qualification Examinations

(a) Qualification Examinations and Waiver of Requirements

All capital acquisition brokers are subject to NASD Rule 1070.

(b) Confidentiality of Examinations

All capital acquisition brokers are subject to NASD Rule 1080.

123. Categories of Registration

(a) Categories of Principal Registration

All capital acquisition brokers are subject to NASD Rule 1022.

(b) Categories of Representative Registration

All capital acquisition brokers are subject to NASD Rule 1032.

(c) Operations Professional

All capital acquisition brokers are subject to paragraph (b)(6) of FINRA Rule 1230.

124. Persons Exempt from Registration

All capital acquisition brokers are subject to NASD Rule 1060.

125. Continuing Education Requirements

All capital acquisition brokers are subject to FINRA Rule 1250.

200. DUTIES AND CONFLICTS

201. Standards of Commercial Honor and Principles of Trade

All capital acquisition brokers are subject to FINRA Rule 2010.

202. Use of Manipulative, Deceptive or Other Fraudulent Devices

All capital acquisition brokers are subject to FINRA Rule 2020.

204. Payments to Unregistered Persons

All capital acquisition brokers are subject to FINRA Rule 2040.

207. Transactions Involving FINRA Employees

All capital acquisition brokers are subject to FINRA Rule 2070.

208. Expungement of Customer Dispute Information from the Central Registration Depository (CRD) System

All capital acquisition brokers are subject to FINRA Rules 2080 and 2081.

209. Know Your Customer

Every capital acquisition broker shall use reasonable diligence to know (and retain) the essential facts concerning every customer and concerning the authority of each person acting on behalf of such customer. For purposes of this Rule, facts "essential" to "knowing the customer" are those required to (a) effectively service the customer, (b) understand the authority of each person acting on behalf of the customer, and (c) comply with applicable laws, regulations and rules.

211. Suitability

(a) A capital acquisition broker or an associated person of a capital acquisition broker must have a reasonable basis to believe that a recommended transaction or investment strategy (as defined in FINRA Rule 2111) involving a security or securities is suitable for the customer, based on the information obtained through the reasonable diligence of the broker or associated person to ascertain the customer's investment profile. A customer's investment profile includes, but is not limited to, the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose to the capital acquisition broker or associated person of a capital acquisition broker in connection with a recommendation.

The capital acquisition broker or associated person may not disclaim any responsibilities under this Rule.

(b) The capital acquisition broker or associated person fulfills the customer-specific suitability obligation for an institutional investor, if (1) the broker or associated person has a reasonable basis to believe that the institutional investor is capable of evaluating investment risks independently, both in general and with regard to particular transactions and investment strategies involving a security or securities and (2) the institutional investor affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's recommendations. Where an institutional investor has delegated decision-making authority to an agent, such as an investment adviser or a bank trust department, these factors will be applied to the agent.

• • • Supplementary Material: --------------

.01 Reasonable Basis Suitability Obligation. Rule 211 requires a capital acquisition broker to have a reasonable basis to believe, based on reasonable diligence, that the recommendation is suitable for at least *some* investors. In general, what constitutes reasonable diligence will vary depending on, among other things, the complexity of and risks associated with the security or investment strategy and the capital acquisition broker's or associated person's familiarity with the security or investment strategy. A capital acquisition broker's or associated person's reasonable diligence must provide the capital acquisition broker or associated person with an understanding of the potential risks and rewards associated with the recommended security or strategy. The lack of such an understanding when recommending a security or strategy violates the suitability rule.

.02 Institutional Investor Exemption. Rule 211(b) provides an exemption to customer-specific suitability regarding institutional investors if the conditions delineated in that paragraph are satisfied. With respect to having to indicate affirmatively that it is exercising independent judgment in evaluating the capital acquisition broker's or associated person's recommendations, an institutional investor may indicate that it is exercising independent judgment on a transaction-by-transaction basis, on an asset-class-by-asset-class basis, or in terms of all of its potential transactions.

221. Communications with the Public

(a) No communication with the public by a capital acquisition broker may:

(1) include any false, exaggerated, unwarranted, promissory or misleading statement or claim;

(2) omit any material fact or qualification if the omission, in light of the context of the material presented, would cause the communication to be misleading;

(3) state or imply that FINRA, or any other corporate name or facility owned by FINRA, or any other regulatory organization endorses, indemnifies, or guarantees the capital acquisition broker-dealer's business practices; or

(4) imply that past performance will recur or make any exaggerated or unwarranted claim, opinion or forecast.

(b) All communications by a capital acquisition broker must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluating the facts in regard to any particular security or type of security, industry, or service.

226. Arbitration Requirements

(a) Arbitration Disclosure to Associated Persons Signing or Acknowledging Form U4

All capital acquisition brokers are subject to FINRA Rule 2263.

(b) Requirements When Using Predispute Arbitration Agreements for Customer Accounts

All capital acquisition brokers are subject to FINRA Rule 2268.

240. Engaging in Impermissible Activities

Upon a finding that a capital acquisition broker or associated person of a capital acquisition broker has engaged in activities that require the firm to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on capital acquisition brokers under Capital Acquisition Broker Rule 016(c), FINRA may examine for and enforce all FINRA rules against such a broker or associated person, including any rule that applies to a FINRA member broker-dealer that is not a capital acquisition broker or to an associated person who is not a person associated with a capital acquisition broker.

300. SUPERVISION AND RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS

311. Capital Acquisition Broker Compliance and Supervision

(a) All capital acquisition brokers are subject to paragraphs (a)(1) through (a)(6), (b)(1), (b)(4), (b)(5), (b)(7), (e) and (f) of FINRA Rule 3110, and Supplementary Materials .01 through .03, .06 through .09, and .11 following FINRA Rule 3110.

(b) A capital acquisition broker must permit the examination and inspection of its premises, systems, platforms, and records by representatives of FINRA and the Commission, and must cooperate with the examination, inspection, or investigation of any persons directly or indirectly using its platform.

313. Designation of Chief Compliance Officer

Each capital acquisition broker must designate and specifically identify to FINRA on Schedule A of Form BD one or more principals to serve as a chief compliance officer.

322. Influencing or Rewarding Employees of Others

All capital acquisition brokers are subject to FINRA Rule 3220.

324. Borrowing From or Lending to Customers

All capital acquisition brokers are subject to FINRA Rule 3240.

327. Outside Business Activities of Registered Persons

All capital acquisition brokers are subject to FINRA Rule 3270.

328. Private Securities Transactions of an Associated Person

No person associated with a capital acquisition broker shall participate in any manner in a private securities transaction as defined in FINRA Rule 3280(e).

331. Anti-Money Laundering Compliance Program

Each capital acquisition broker shall develop and implement a written anti-money laundering program reasonably designed to achieve and monitor its compliance with the requirements of the Bank Secrecy Act (31 U.S.C. 5311, *et seq*.), and the implementing regulations promulgated thereunder by the Department of the Treasury. Each capital acquisition broker's anti-money laundering program must be approved, in writing, by a member of senior management. The anti-money laundering programs required by this Rule must, at a minimum,

(a) Establish and implement policies and procedures that can be reasonably expected to detect and cause the reporting of transactions required under 31 U.S.C. 5318(g) and the implementing regulations thereunder;

(b) Establish and implement policies, procedures, and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act and the implementing regulations thereunder;

(c) Provide for independent testing for compliance, no less frequently than every two years, to be conducted by capital acquisition broker personnel or by a qualified outside party;

(d) Designate and identify to FINRA (by name, title, mailing address, e-mail address, telephone number, and facsimile number) an individual or individuals responsible for implementing and monitoring the day-to-day operations and internal controls of the program (such individual or individuals must be an associated person of the capital acquisition broker) and provide prompt notification to FINRA regarding any change in such designation(s); and

(e) Provide ongoing training for appropriate personnel.

• • • Supplementary Material: --------------

.01 Independent Testing Requirements

(a) All capital acquisition brokers should undertake more frequent testing than required if circumstances warrant.

(b) Independent testing, pursuant to Rule 331(c), must be conducted by a designated person with a working knowledge of applicable requirements under the Bank Secrecy Act and its implementing regulations.

(c) Independent testing may not be conducted by:

(1) a person who performs the functions being tested,

(2) the designated anti-money laundering compliance person, or

(3) a person who reports to a person described in either subparagraphs (1) or (2) above.

.02 Review of Anti-Money Laundering Compliance Person Information

Each capital acquisition broker must identify, review, and, if necessary, update the information regarding its anti-money laundering compliance person designated pursuant to Rule 331(d) in the manner prescribed by FINRA Rule 4517.

400. FINANCIAL AND OPERATIONAL RULES

411. Capital Compliance

(a) (1) Unless otherwise permitted by FINRA, a capital acquisition broker must suspend all business operations during any period in which it is not in compliance with applicable net capital requirements set forth in SEA Rule 15c3-1.

(2) FINRA may issue a notice pursuant to FINRA Rule 9557 directing a capital acquisition broker that is not in compliance with applicable net capital requirements set forth in SEA Rule 15c3-1 to suspend all or a portion of its business.

(b) No equity capital of a capital acquisition broker may be withdrawn for a period of one year from the date such equity capital is contributed, unless otherwise permitted by FINRA in writing. This paragraph does not preclude a capital acquisition broker from withdrawing profits earned.

(c) Subordinated Loans, Notes Collateralized by Securities and Capital Borrowings

(1) All subordinated loans or notes collateralized by securities must meet such standards as FINRA may require to ensure the continued financial stability and operational capability of the capital acquisition broker, in addition to those specified in Appendix D of SEA Rule 15c3-1.

(2) Unless otherwise permitted by FINRA, each capital acquisition broker that is a partnership and whose general partner enters into any secured or unsecured borrowing, the proceeds of which will be contributed to the capital of the broker, must submit to FINRA such information as needed by FINRA to determine whether such proceeds qualify as capital acceptable for inclusion in the computation of the net capital of the broker.

414. Audit

All capital acquisition brokers are subject to FINRA Rule 4140.

415. Guarantees by, or Flow Through Benefits for, Members

All capital acquisition brokers are subject to FINRA Rule 4150.

416. Verification of Assets

All capital acquisition brokers are subject to FINRA Rule 4160.

451. Books and Records

(a) General Requirements

All capital acquisition brokers are subject to FINRA Rule 4511.

(b) Customer Information

Each capital acquisition broker must maintain each customer's name and residence, whether the customer is of legal age (if applicable), and the names of any persons authorized to transact business on behalf of the customer.

(c) Records of Written Customer Complaints

All capital acquisition brokers are subject to FINRA Rule 4513.

452. Assignment of Responsibility for General Ledger Accounts and Supplemental FOCUS Information

(a) Assignment of Responsibility for General Ledger Accounts

Each capital acquisition broker must designate an associated person who is responsible for each general ledger bookkeeping account and account of like function used by the broker and such associated person must control and oversee entries into each such account and must determine that the account is current and accurate as necessary to comply with all applicable FINRA rules and federal securities laws governing books and records and financial responsibility requirements. A supervisor must, as frequently as is necessary considering the function of the account but, in any event, at least monthly, review each account to determine that it is current and accurate and that any items that become aged or uncertain as to resolution are promptly identified and appropriate action is taken.

(b) Supplemental FOCUS Information

All capital acquisition brokers are subject to FINRA Rule 4524.

453. Reporting Requirements

All capital acquisition brokers are subject to FINRA Rule 4530.

454. Member Filing and Contact Information Requirements

All capital acquisition brokers are subject to FINRA Rule 4517.

457. Custodian of Books and Records

All capital acquisition brokers are subject to FINRA Rule 4570.

500. SECURITIES OFFERINGS

512. Private Placements of Securities Issued by Members

All capital acquisition brokers are subject to FINRA Rule 5122.

515. Fairness Opinions

All capital acquisition brokers are subject to FINRA Rule 5150.

800. Investigations and Sanctions

Except for FINRA Rules 8110, 8211, and 8213, all capital acquisition broker members shall be subject to the FINRA Rule 8000 Series, unless the context requires otherwise, provided, however, that:

(a) the term “associated person” as used in the FINRA Rule 8000 Series shall mean “associated person of a capital acquisition broker” or “person associated with a capital acquisition broker” as defined pursuant to Capital Acquisition Broker Rule 016(a); and

(b) the terms “rules” and “FINRA rules” as used in the FINRA Rule 8000 Series shall include the Capital Acquisition Broker Rules.

900. Code of Procedure

Except for the FINRA Rule 9700 Series, all capital acquisition broker members shall be subject to the FINRA Rule 9000 Series, unless the context requires otherwise, provided, however, that:

(a) the term "associated person" as used in the FINRA Rule 9000 Series shall mean "associated person of a capital acquisition broker" or "person associated with a capital acquisition broker" as defined pursuant to Capital Acquisition Broker Rule 016(a);

(b) the terms "rules" and "FINRA rules" as used in the FINRA Rule 9000 Series shall include the Capital Acquisition Broker Rules;

(c) any capital acquisition broker (and its associated persons) may be subject to a fine under FINRA Rule 9216(b) with respect to any rule or By-Laws listed in this Rule.

- Article IV of the FINRA By-Laws -- Failure to timely submit amendments to Form BD.
- Article V of the FINRA By-Laws -- Failure to timely submit amendments to Form U4.
- Article V of the FINRA By-Laws -- Failure to timely submit amendments to Form U5.
- Capital Acquisition Broker Rule 125 – Failure to comply with the continuing education requirements.
- Capital Acquisition Broker Rule 221 – Communications with the public.
- Capital Acquisition Broker Rule 311 – Failure to maintain adequate written supervisory procedures where the underlying conduct is subject to Capital Acquisition Broker Rule 900(c).
- Capital Acquisition Broker Rule 451 – Failure to keep and preserve books, accounts, records, memoranda, and correspondence in conformance with

all applicable laws, rules, regulations and statements of policy promulgated thereunder, and with FINRA rules.

- Capital Acquisition Broker Rule 452 – Failure to comply with the requirements for general ledger accounts.
- Capital Acquisition Broker Rule 453 – Failure to timely file reports.
- Capital Acquisition Broker Rule 454 – Failure to report, review and update executive representative designation and contact information.
- Capital Acquisition Broker Rule 512 – Failure to timely file private placement documents.
- SEA Rules 17a-3(a) and 17a-4 – Record retention rule violations.
- SEA Rule 17a-5 – Failure to timely file FOCUS reports and annual audit reports.
- SEA Rule 17a-10 – Failure to timely file Schedule I.

(d) for purposes of FINRA Rule 9551(a), FINRA staff may issue a written notice requiring a capital acquisition broker to file communications with the FINRA Advertising Regulation Department at least ten days prior to use if FINRA staff determines that the member has departed from the standards of Capital Acquisition Broker Rule 221; and

(e) for purposes of FINRA Rule 9551(d), the pre-use filing requirement referenced in a notice issued and served under FINRA Rule 9551 shall become effective 21 days after service of the notice, unless stayed by a request for a hearing pursuant to FINRA Rule 9559.

1000. Arbitration and Mediation

All capital acquisition broker members shall be subject to the FINRA Rule 12000

Series, FINRA Rule 13000 Series and FINRA Rule 14000 Series, unless the context requires otherwise, provided, however, that:

(a) the term "associated person" as used in the FINRA Rule 12000 Series, FINRA Rule 13000 Series and FINRA Rule 14000 Series shall mean "associated person of a capital acquisition broker" or "person associated with a capital acquisition broker" as defined pursuant to Capital Acquisition Broker Rule 016(a);

(b) the terms "rules" and "FINRA rules" as used in the FINRA Rule 12000 Series, FINRA Rule 13000 Series and FINRA Rule 14000 Series shall include the Capital Acquisition Broker Rules; and

(c) the term "customer" as used in FINRA Rule 12000 Series, FINRA Rule 13000 Series and FINRA Rule 14000 Series shall include customers of capital acquisition brokers.

* * * * *