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September 23, 2016

VIA EMAIL

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

Re: Regulatory Notice 16-29: Gifts, Gratuities and Non-Cash Compensation Rules

Dear Ms. Asquith:

The Investor Rights Clinic at the Elisabeth Haub School of Law at Pace University, operating through John Jay Legal Services, Inc. (“PIRC”),¹ welcomes the opportunity to submit this comment letter regarding FINRA’s proposed amendments to its Gifts, Gratuities and Non-Cash Compensation Rules. PIRC supports FINRA’s regulation of gifts, gratuities and non-cash compensation as an important part of its role in protecting investors by minimizing conflicts of interest and the appearance of impropriety. However, PIRC believes that the best way to accomplish this goal would be to ban all gifts or non-cash compensation that could lead to conflicts of interest. In the absence of an outright prohibition, we support FINRA’s proposed amendments to regulate the terms of gifts, gratuities and non-cash compensation to the extent that they prevent conflicts of interest.

Gift Limit Increase

PIRC does not support FINRA’s proposed increase to the gift limit under Rule 3220 (Influencing or Rewarding Employees of Others) and Rule 3221 (Restrictions on Non-Cash Compensation) from \$100 to \$175 per person per year. Current FINRA Rule 3220 “prohibits any member or person associated with a member, directly or indirectly, from giving anything of value in excess of \$100 per year to any person where such payment is in relation to the business of the recipient’s employer...The rule seeks both to avoid improprieties that may arise when a

¹ PIRC opened in 1997 as the nation’s first law school clinic in which law students, for academic credit and under close faculty supervision, provide pro bono representation to individual investors of modest means in arbitrable securities disputes. See Barbara Black, *Establishing A Securities Arbitration Clinic: The Experience at Pace*, 50 J. LEGAL EDUC. 35 (2000); see also Press Release, Securities Exchange Commission, SEC Announces Pilot Securities Arbitration Clinic To Help Small Investors - Levitt Responds To Concerns Voiced At Town Meetings (Nov. 12, 1997), available at <http://www.sec.gov/news/press/pressarchive/1997/97-101.txt>.

member firm or its associated persons give anything of value to an employee of a customer or counterparty and to preserve an employee's duty to act in the best interests of that customer."²

PIRC believes that gift giving, especially in the absence of a universal fiduciary standard, increases the risk that member firms and associated persons will provide conflicted investment advice rather than advice in the customer's best interest. While the \$75 inflation-related increase may not materially affect the underlying goal of avoiding impropriety and conflicts of interest, increasing the limit sends a message condoning this type of gift giving. Therefore, PIRC advocates for a limit of \$0 under FINRA Rules 3220 and 3221 to avoid unacceptable conflicts of interest; however, at a minimum, PIRC supports maintaining the \$100 limit in Rules 3220 and 3221.

Application to All Securities Products

PIRC supports FINRA's proposal to extend Rule 3221 to cover all securities products, rather than only direct participation programs, variable insurance contracts, investment company securities, and public offerings of securities. However, PIRC believes that Rule 3220, as well as Rule 3221, should expressly state that it applies to all securities products.

Incorporating Gifts Received

PIRC supports FINRA's proposal to incorporate gifts received by a member firm or its associated persons into Rule 3220 and proposed Rule 3221. This incorporation furthers FINRA's stated goal for Rule 3220, which is to avoid improprieties and "preserve an employee's duty to act in the best interests of [the] customer."³ Gifts received by a member firm or its associated persons raise similar conflicts of interest and improper incentives concerns as those given to a member firm or its associated persons. In order to protect the integrity of regulated investment activity and to protect the interests of customers, the proposed gifts rule should encompass not only gifts given, but gifts received as well.

***De Minimis* Threshold**

In the absence of a general prohibition on gift giving, PIRC supports FINRA's proposal for a *de minimis* threshold below which firms would not have to keep records of gifts given or received in an effort to prevent firms from passing on compliance costs to customers. However, we believe the *de minimis* threshold should be \$25 rather than \$50. This should help ensure that such gifts are truly of nominal value and that the lack of recording those gifts will not adversely affect investors.

Internal Sales Contests

PIRC strongly supports FINRA's proposed ban of product-specific internal sales contests. However, we feel that this proposal does not do enough to prevent conflicts of interest. Other types of non-cash compensation contests can encourage a broker to invest without

² *Regulatory Notice 16-29*, Financial Industry Regulatory Authority, Aug. 2016, 3.

³ *Id.*

considering the suitability of the investment for the customer, let alone the customer's best interest. Banning all internal sales contests would help ensure customers do not end up with unsuitable investments. This would also further promote "an employee's duty to act in the best interests of [the] customer," the stated goal of Rule 3220.⁴ PIRC believes the ban should also be extended to proposed Rule 3221.

Business Entertainment at Training Sessions

In question 6 of the Regulatory Notice, FINRA seeks feedback about aligning entertainment at training sessions paid for by offerors with FINRA's general business entertainment rule. PIRC does not support non-cash compensation, including business entertainment, given or received by member firms and associated persons. This includes business entertainment provided at training sessions paid for by offerors. We believe that the structure of proposed Rule 3221, which does not permit payment or reimbursement for entertainment or expenses of guests or associated persons at training sessions, is sufficient to limit the risk of improper incentives that arise through extravagant use of business entertainment at training sessions. Non-cash compensation can harm investors by providing an incentive to brokers that competes with customers' best interests. We believe aligning the business entertainment approach with the rules on training sessions would improperly incentivize brokers, as training sessions should have an educational basis and offeror-funded business entertainment can not only distract from learning, but can encourage attendance for inappropriate reasons. If FINRA does choose to align the two approaches, the frequency requirement for training sessions should be tailored to the length of a training session rather than the general business entertainment approach under each member's written policies and supervisory procedures. This should help ensure that the business entertainment is appropriate and not extravagant under the circumstances of a training session.

Consolidation of Rules and Recordkeeping

PIRC supports consolidating the rules governing gifts, gratuities and non-cash compensation, as such consolidation should eliminate the risk that someone will overlook these rules or be unaware that there are multiple compliance rules governing this subject. Additionally, consolidation should simplify compliance by allowing member firms to look in one easily accessible place for guidance on recording any gift, gratuity, or non-cash compensation they receive.

⁴ *Id.*

Conclusion

PIRC supports FINRA's regulation of gifts, gratuities, and non-cash compensation as a way to minimize the risk of improprieties and conflicts of interest. While we support FINRA's continued amendments to improve and consolidate these rules, we believe further revision is necessary to preserve an employee's duty to act in the best interests of the customer and avoid conflicts of interest. PIRC believes that customers should be a broker's number one priority, and FINRA rules should serve to ensure that investors' interests are protected.

Respectfully yours,

Pace Investor Rights Clinic

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