ST. JOHN'S UNIVERSITY
SCHOOL OF LAW

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Via Email To pubcom@finra.org
Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1735 K Street NW
Washington, D.C. 20006-1506

Re: Regulatory Notice 19-27

Dear Ms. Mitchell:

The St. John's University School of Law Securities Arbitration Clinic (the "Clinic") would like to thank you for the opportunity to comment Regulatory Notice 19-27, and specifically on rules and issues relating to senior investors. The Clinic is a curricular offering where students represent public investors of limited means in disputes against their investment brokers.[1] Our clients are often seniors who have entrusted their retirement savings to brokers and their firms. We see first hand what can go wrong when that trust is violated and offer our comments on senior investors may be better protected.

The Clinic is particularly concerned about brokers borrowing money from senior customers. Currently, Rule 3240 provides a framework for firms to have greater control over lending arrangements between brokers and their customers. Under the rule, brokers are prohibited from borrowing money from or lending money to their customers unless the firm has written procedures that allow for the arrangement. The rule establishes certain criteria that must be met before such a loan is permitted, including that the customer be part of the

[1] For more information, please see http://www.stjohns.edu/law/securities-arbitration-clinic.

broker's immediate family; the broker and customer both be registered with the same broker dealer; the customer be the business of loaning money; or the loan arises out of a personal or business relationship outside of the broker/customer one. In addition, the broker must notify the firm of the intended loan and obtain the firm's written pre-approval of the loan. FINRA has brought disciplinary actions against registered persons who have entered into lending arrangements with senior investors in violation of rule 3240.

The Clinic has dealt with cases involving unsophisticated senior investors lending money to brokers in violation of Rule 3240. In the Clinic's experience, the brokerage firm had policies that prohibited brokers from entering into lending arrangements with their customers; however, the firms were not effectively implementing the policies or monitoring their brokers. For example, where a broker is having financial difficulties, such as having tax liens or judgments entered against the broker, the firm should more closely monitor the broker's interactions with customers.

Senior investors are generally at the height of their wealth accumulation. Brokers generally have a full picture of the senior's financial profile and know how much money the individual has. This makes it particularly easy for a broker to target a senior investor if the broker is having financial difficulties, as well overcome any objections the senior investor may have about loaning the broker money. Accordingly, FINRA must take additional steps to ensure firms are properly enforcing Rule 3240 and watching out for "red flags" from their brokers. It may be helpful to establish "heightened supervision" obligations with respect to brokers who have certain financial disclosures which may make the broker more prone to engage in this type of misconduct.

Firms should also be sensitive to situations where a broker borrowed money from a prospective customer, prior to the individual opening an account with the firm. Brokers should be required to report whether they have borrowed money from any individuals with whom they are now doing business. This will help the firm better supervise the broker-customer relationship and be alert to any red flags that may develop during that relationship, such as additional loans.

Moreover, the Clinic remains concerned that brokers may attempt to circumvent the intention of the rule by claiming a personal relationship with the customer. Senior investors are particularly susceptible to abuses in this regard. In the Clinic's experience senior investors have been charmed by brokers into casual friendship, arguably creating a personal relationship. Senior investors need express protection from brokers who seek to create potentially exploitative relationships with senior investors by creating a façade of friendship. To our knowledge, the Rule has not been interpreted to include these types of disingenuous relationships. However, an express statement of the scope of the relationships covered under the rule may be helpful. The Clinic posits that such statement should clearly outline that only very close relationships, akin to the closeness of familial bonds should be included. Such a statement would provide a clear standard and protect senior investors from the potential of abuses of brokers posing as friends.

Further, many senior investors have no prior experience or knowledge about investing at all and first begin investing once they retire. We appreciate that Rule 3240 places affirmative obligations on the part of the firm to supervise customer-broker loans, we believe seniors will benefit from greater awareness that such loans are presumptively improper. For example, if a firm receives a request to approve a loan by a broker, especially one based on a personal relationship, the firm should be required to follow up directly with the customer to confirm that the loan is appropriate. FINRA may also require that firms send educational materials regarding the concerns with broker loans to senior investors at a regular interval.

Regarding Rule 2165, the Clinic believes that the freezing of disbursements of an account that is believed to be comprised should not be permissive, but rather mandatory. The Clinic is particularly concerned where an investor may be experiencing diminished mental capacity. A permissive rule may offer no protection at all. While encouraging that a firm attempt to resolve a matter with a customer before instituting a temporary freezing of the investor's account(s) is a good first step, more must be done to protect senior investors. By creating a mandatory obligation, the firm would be required to immediately initiate an internal review of the facts and circumstances that caused the firm initially to hold a reasonable belief that financial exploitation against a senior investor has occurred/is occurring. Firms would better protect senior investors by ensuring no matter the situation, a customer's accounts will be frozen until investigation makes clear there was either no real threat, or that such threat existed and is now properly handled.

Finally, in the Notice, FINRA asked whether it should require any additional disclosure or heightened supervision for any particular product or investment strategy that is marketed to senior investors. We believe there should be heighted supervision with respect to certain products, especially those investments which are risky but high yielding. In the Clinic, we see a lot of seniors placed in products such as variable annuities, non-traded REITs, and non-traded Business Development Companies. The seniors are sold these investments as safe, conservative products offering a high annual yield. Of course, our clients sign the documentation placed in front of them by their broker, not reading the documentation yet signing where they are told to sign. It is not till later, when the investor tries to withdraw funds to cover an unexpected medical expense or home repair, that the investor learns that true nature of the investment. The investment may only allow withdrawals with the payment of a substantial penalty, or may not allow withdrawals at all. The investor may learn that the income they had been receiving was really a return of their capital and that the amount was not actually guaranteed. The investor may learn that the investment is worth substantially less that the initial investment, oftentimes in large part due to the high initial costs of the investment.

When senior investors are misled in this way, they are often left without an easy solution. If they wish to pursue arbitration, it may take a year or longer before they receive an award. Success at arbitration is far from guaranteed. The firm may argue that the investment was the senior's idea – a way to generate necessary income, and the senior's understanding of the risk is evidenced by the signed paperwork. If the investor is unable to find representation due to the small dollar amount of the claim or the difficulties asserting damages for an investment that is still held by illiquid, the investor may have little hope of success in the arbitration. In the meanwhile, the investor is without funds that may be necessary for their support.

Accordingly, FINRA may ensure that greater scrutiny is paid to these types of investments at the point of sale. FINRA may deem these types of recommendations as presumptively unsuitable. Brokers may be able to make such recommendations if they are able to overcome this presumption. This will ensure that seniors are not left to attempt to recover for harm after it has occurred, but rather that they will be protected from the beginning.

Again, the Clinic thanks FINRA for the opportunity to comment on these important issues.

Respectfully submitted,

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/s/

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