FINANCIAL SERVICES INSTITUTE
VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS AND INDEPENDENT FINANCIAL ADVISORS

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VIA ELECTRONIC MAIL

May 23, 2014

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

Re: Regulatory Notice 14-15: Retrospective Rule Review – Gifts and Gratuities and Non-Cash Compensation Rules

Dear Ms. Asquith:

On April 8, 2014 the Financial Industry Regulatory Authority (FINRA) released Regulatory Notice 14-15,[1] requesting comment on the effectiveness and efficiency of its gifts and gratuities and non-cash compensation rules. This retrospective review includes a review of the substance and application of the rule as well as FINRA's process to administer the rules in order to determine whether FINRA's rule set is meeting its intended investor-protection objectives by reasonably efficient means.

The Financial Services Institute[2] (FSI) appreciates the opportunity to comment on this Regulatory Notice. FSI is encouraged by FINRA's adoption of economic impact assessment and cost-benefit analysis with regard to rulemaking.[3] The utilization of retrospective review is a vital component of increasing the transparency and accountability of SRO rulemaking, and will ensure that rules remain relevant and are appropriately designed to achieve their objectives. As FINRA progresses through the findings and action phases of the review process, FSI looks forward to providing constructive feedback to address areas in the rule sets that will assist in the retrospective rule review assessment.

Background on FSI Members

The independent broker-dealer (IBD) community has been an important and active part of the lives of American investors for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD firms also share a

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[1] FINRA Regulatory Notice 14-15 (Apr. 2014), *available at* https://www.finra.org/Industry/Regulation/Notices/2014/P479811.

[2] The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has 100 Broker-Dealer member firms that have more than 138,000 affiliated registered representatives serving more than 14 million American households. FSI also has more than 35,000 Financial Advisor members.

[3] *See* Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking (September 2013); *available at* http://www.finra.org/web/groups/industry/documents/industry/p346389.pdf.

number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; primarily engage in the sale of packaged products, such as mutual funds and variable insurance products; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered investment adviser firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial advisers are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their financial goals and objectives.

In the U.S., approximately 201,000 independent financial advisers – or approximately 64 percent of all practicing registered representatives – operate in the IBD channel.[4] These financial advisers are self-employed independent contractors, rather than employees of the IBD firms. These financial advisers provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisers are typically "main street America" – it is, in fact, almost part of the "charter" of the independent channel. The core market of advisers affiliated with IBDs is comprised of clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisers are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other centers of influence.[5] Independent financial advisers get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisers have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisers. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is committed to preserving the valuable role that IBDs and independent advisers play in helping Americans plan for and achieve their financial goals. FSI's primary goal is to ensure our members operate in a regulatory environment that is fair and balanced. FSI's advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

Comments

FSI appreciates the opportunity to submit comments on FINRA's Retrospective Rule Review. In preparing our comments, FSI engaged with various member firms and advisors in order to obtain a variety of views for FINRA to consider. Firms and advisors' input centered on several areas that FINRA may find helpful in assessing the current set of rules regarding gifts and gratuities and non-cash compensation.

- **Have the Rules Effectively Addressed the Problem(s) They Were Intended to Mitigate?** The purpose of the gifts and gratuities and non-cash compensation rules is to "ensure that a member or its associated persons do not do or give anything of value to an employee of a customer that may cause (or appear to cause) the customer's employee to act in a

[4] Cerulli Associates at http://www.cerulli.com/.
[5] These "centers of influence" may include lawyers, accountants, human resources managers, or other trusted advisers.

manner that is inconsistent with the customer's best interests."[6] The rules require member firms to design and implement policies to ensure that associated persons follow the limitations placed upon gifts and gratuities. FSI and its members believe that, overall, the rules are effectively addressing the issues and problems they are intended to mitigate. FSI member firms have indicated that FINRA's rules have been effective in ensuring that violations are prevented and that personnel who supervise, administer, or are subject to the requirements receive appropriate training and education.

- **What have been your experiences with implementation of the rule set, including any ambiguities in the rules or challenges to comply with them?** FSI member firms have not experienced significant difficulties in implementing the requirements under the rule sets. Firms have created written policies and procedures to implement the requirements. Firms have also implemented various methods for providing information, training, and education to advisors regarding the rules' requirements. Overall, the rule sets have been implemented effectively and without major issue.

- **What have been the costs and benefits arising from FINRA's rules? Have the costs and benefits been in line with expectations described in the rulemaking?** FSI member firms have experienced certain costs in implementing the rules' requirements. FSI members have reported the annual costs of compliance to be approximately $10,000 for firms with over a thousand advisors. Firms have hired compliance professionals who dedicate a substantial portion of their time to the rules' requirements. Firms have also reported benefits associated with the rules. For instance, firms recognize and support the fact that the rules provide guidelines which ensure consistency across the industry. The rules also address conflicts of interest that arise, particularly with regard to gifts, gratuities, and non-cash compensation provided by product sponsors to advisors.

- **Can FINRA make the rules more efficient and effective, including FINRA's administrative process?** FSI member firms and advisors believe that the $100 threshold is too low in the current business environment. Firms and advisors recommend raising this threshold to $250 or as high as $500. Raising the threshold to these levels would be unlikely to impact the business relationship between advisors and clients such that the rules no longer effectively address the problems they aim to mitigate. The current low threshold becomes particularly bothersome in instances where advisors want to provide gifts to their clients for such things as anniversaries and weddings, or send flowers to clients as a get well or sympathy gesture. Advisors have reported that the current $100 limit can easily be exceeded through high shipping costs, taxes, or tips paid on meals. The current $100 threshold is also problematic because it allows for generous gifts to be given in communities with lower costs of living but not in major metropolitan areas. FINRA should explore whether a principle-based approach would be more practical instead of the current rules-based monetary threshold on gifts and gratuities. Another option is for FINRA to revise the rule to only require reporting of the gift if it exceeds a certain, reasonable dollar amount. For instance, gifts provided under $200 need not be logged or reported to the firm but gifts exceeding this amount must be logged and reported and firms must review the logs during annual exams.

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[6] NASD Notice to Members 06-06 (Jan. 2006), *available at* http://www.finra.org/Industry/Regulation/Notices/2006/P015876.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with FINRA on this and other important regulatory efforts.

Thank you for your consideration of our comments. Should you have any questions, please contact me at (202) 803-6061.

Respectfully submitted,

David T. Bellaire, Esq.
Executive Vice President & General Counsel