



NASAA

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

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November 5, 2013

Submitted electronically to rule-comments@sec.gov

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Release No. 34-706012, File Number SR-FINRA-2013-025

Dear Ms. Murphy:

On behalf of the North American Securities Administrators Association (“NASAA”),¹ I hereby submit the following comments in response to Release No. 34-706012, File No. SR-FINRA-2013-025 entitled Notice of Filing of Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as modified by Amendment No. 1, to Adopt Rules Regarding Supervision in the Consolidated FINRA Rulebook.² NASAA previously filed its comments to FINRA’s proposed rule on August 6, 2013 in response to Release No. 34-69902.³ NASAA appreciates the opportunity to offer its comments on the above-referenced proposal, which amends FINRA’s proposal to incorporate and eliminate duplicative National Association of Securities Dealers (“NASD”), Financial Industry Regulatory Authority (“FINRA”), and New York Stock Exchange (“NYSE”) rules and guidance regarding supervision.

While NASAA continues to generally support FINRA’s efforts to consolidate its rulebook, NASAA remains concerned that FINRA has failed to adequately address issues raised in NASAA’s original comment letter to the proposal. Specifically, NASAA remains concerned with (1) FINRA’s failure to require its members to capture and review oral customer complaints; (2) FINRA’s failure to reinsert language requiring its members to reasonably design their supervisory procedures to comply with FINRA Rule 2010, including the supervision of business

¹ NASAA is the association of the 67 state, provincial, and territorial securities regulatory agencies of the United States, Canada, and Mexico. NASAA serves as the forum for these regulators to work with each other in an effort to protect investors at the grassroots level and to promote fair and open capital markets.

² 78 Fed. Reg. 6283 (Oct. 22, 2013).

³ See letter from A. Heath Abshire, President, NASAA, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (Aug. 6, 2011) available at <http://www.sec.gov/comments/sr-finra-2013-025/finra2013025-18.pdf>.

lines that do not necessitate broker-dealer registration; and (3) FINRA's failure to maintain "Heightened Supervision" requirements for certain producing managers. FINRA's deletion of proposed One-Person Office of Supervisory Jurisdiction ("OSJ") Supplementary Material (Rule 3110.03) and FINRA's failure to expand the period in which its members must retain certain records raise additional concerns for NASAA.

I. Failure to Include Oral Complaints in the Definition of Customer Complaints

In its response to the comments of NASAA and others, FINRA reiterated its position that capturing and assessing oral customer complaints is too difficult and failed to amend its definition of customer complaints to include oral complaints.⁴ For the reasons articulated in NASAA's prior comments, NASAA continues to strongly disagree with this position and urges FINRA to adopt a rule requiring its members to capture, acknowledge, and respond to *all* customer complaints. As NASAA noted in its prior comments, and as FINRA concedes in its response, many FINRA members were already required to capture and assess oral complaints pursuant to NYSE Rules prior to 2008, when FINRA introduced an interim rule removing the requirement to capture oral complaints.⁵ NASAA notes that for many years prior to the 2008 interim rule, NYSE-member firms captured and assessed oral complaints without the aid of more recent technological advancements that would undoubtedly make the capture and assessment of such complaints even less burdensome. For example, brokers today have keyboards at their fingertips and could easily memorialize a customer's oral complaint – much more easily than could be done in the days before computer technology became ubiquitous. Given the advancements in technology, NASAA fails to see why it is now too difficult for FINRA members to capture, review, and, if required, report oral complaints. Also, NASAA remains concerned that FINRA failed to address the issues presented by customers with a diminished capacity that may prevent the effective communication of a complaint in writing. NASAA urges FINRA to reconsider this important issue for the reasons outlined in NASAA's prior comments.

II. Failure to Include Originally Proposed Language Regarding the Supervision of Non-Securities Business Lines

In its original proposal, FINRA included language that for a firm's supervisory system to be "reasonably designed to achieve compliance with FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade), it must include supervision of all of the member's business lines

⁴ Letter from Patricia Albrecht, Associate General Counsel, FINRA, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (Oct. 2, 2013), at 18, available at <http://www.sec.gov/comments/sr-finra-2013-025/finra2013025-20.pdf>.

⁵ *Id.* at 18 n.74.

irrespective of whether they require broker-dealer registration.”⁶ FINRA subsequently removed this language from its proposal. In its comments, NASAA urged FINRA to reconsider the removal of this requirement, citing the complexity of today’s financial marketplace and the myriad financial services and products offered to investors by their brokers.⁷ NASAA believes that FINRA should include this provision in its most recent amendments to the proposed rule. In its response to comments, FINRA points to, as reason for deleting the language at issue, “potential differences with supervision requirements otherwise applicable to those business lines [that do not require broker-dealer registration].”⁸ NASAA believes that FINRA members could design supervisory procedures in such a way as to eliminate these potential conflicts. Given the landscape of today’s financial marketplace and state securities regulators’ continued concern regarding the supervision of non-broker-dealer business lines, it is NASAA’s continued view that FINRA has missed an opportunity to make clear that its members must have in place supervisory procedures that are reasonably designed to ensure that associated persons maintain high standards, commensurate with FINRA’s Standards of Commercial Honor and Principles of Trade, in all dealings with the public, irrespective of the business lines in which they engage.

III. Elimination of “Heightened Supervision” of Producing Managers in NASD Rule 3012(a)(2)

In its response to comments, FINRA dismissed NASAA’s concerns regarding the elimination of current NASD Rule 3012(a)(2)’s “Heightened Supervision” requirements for producing managers.⁹ As NASAA previously noted, the current rule requiring heightened supervision of certain producing managers is clear and easily understood and applied.¹⁰ NASAA still has concerns regarding FINRA’s decision to replace this clear requirement with the more ambiguous risk-based approach in the current proposal. While NASAA generally supports the flexibility offered by risk-based approaches, in this context it is NASAA’s view that the more prescriptive approach in the current rule better serves the interest of protecting investors from possible conflicts of interest present in the supervision of producing managers.

IV. Removal of One-Person OSJ Supplementary Material

In its amendments to the proposal, FINRA removed in its entirety proposed Rule 3110.03, which included supplementary material regarding One-Person OSJs. The deleted material “expressly

⁶ SEC Release No. 34-69902; File No. SR-FINRA-2013-025 (July 1, 2013) *available at* <http://www.sec.gov/rules/sro/finra/2013/34-69902.pdf>.

⁷ See NASAA Letter, *supra*, note 3 at 2.

⁸ FINRA Letter, *supra*, note 4 at 4.

⁹ *Id.* at 21.

¹⁰ NASAA Letter, *supra*, note 3 at 2-3.

provided that the registered principal at a one-person OSJ (“on-site principal”) cannot supervise his or her own sales activities and must be under the effective supervision and control of another appropriately registered principal (“senior principal”).”¹¹ Citing compliance costs and potential burdens raised by a number of industry commenters, FINRA deleted this material from its proposal. In NASAA’s view, the deleted material provided clear instruction and sensible requirements regarding the supervision of One-Person OSJs, which, as FINRA recognizes, “present unique supervisory challenges.”¹² While NASAA supported the provisions of the deleted material, the harm that may have resulted from its removal is remediated by further changes designed to make it clear that self-supervision is inappropriate, and we encourage FINRA to follow up on its commitment to continue to examine the unique challenges posed by One-Person OSJs.

V. Failure to Extend the Period for which Correspondence and Internal Communications Must be Retained

While NASAA did not comment on the issue of record retention in its original comment letter, NASAA agrees with the Public Investors Arbitration Bar Association’s (“PIABA”) position that the period in which FINRA members must maintain correspondence and internal communications should be extended from three years to six years.¹³ Given that FINRA members are required to maintain certain records for a period of six years, the burden of doing the same for correspondence and other internal communications is minimal especially given the importance of such information.

NASAA further rejects FINRA’s position that imposing a three year retention period promotes consistency in the rules regarding FINRA members’ obligations to retain records. As PIABA previously noted, FINRA members are already required to maintain certain customer records for a period of six years. PIABA additionally points out that no inconsistency is created by requiring FINRA members to retain records for a period longer than required under SEC rules.¹⁴ More significantly, as PIABA also argued, because FINRA Arbitration Procedures allow investors to file claims for a period of six years, if firms are permitted to destroy correspondence and internal communications after three years, significant pieces of evidence may be lost to investors, limiting their ability to pursue their claims.¹⁵ In NASAA’s view, a three-year retention

¹¹ FINRA Letter, *supra*, note 4 at 8.

¹² *Id.* at 9.

¹³ See Letter from Scott Ilgenfritz, President, PIABA, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (July 29, 2013), at 9-11, available at <http://www.sec.gov/comments/sr-finra-2013-025/finra2013025-12.pdf>.

¹⁴ See *id.*


¹⁵ *Id.*

period does not add consistency to the rules, but instead increases inconsistency at the expense of investors.

VI. Conclusion

While NASAA supports FINRA in its efforts to incorporate and eliminate duplicative NASD, FINRA, and NYSE rules and guidance regarding supervision and supports many of the changes proposed by FINRA, it is NASAA's view that several of the changes, as currently proposed, continue to weaken investor protection, while others miss opportunities to strengthen it. NASAA appreciates the opportunity to offer its comments, and should you have any questions regarding the comments in this letter, please do not hesitate to contact Joseph Brady, NASAA General Counsel, at jb@nasaa.org or 202-737-0900.

Sincerely,

A handwritten signature in black ink that reads "Andrea Seidt". The signature is written in a cursive, flowing style.

Andrea Seidt
NASAA President
Ohio Securities Commissioner