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Via FINRA Website

Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 25-04
FINRA Launches Broad Review to Modernize Rules Regarding Member Firms and Associated Persons

Dear Ms. Mitchell:

We are submitting this letter on behalf of the Committee of Annuity Insurers (the "Committee"),[1] in response to FINRA Regulatory Notice 25-04, *FINRA Launches Broad Review to Modernize Rules Regarding Member Firms and Associated Persons* (the "Notice"), issued by the Financial Industry Regulatory Authority, Inc. ("FINRA") on March 12, 2025.[2] The Notice solicits comment on areas FINRA should consider as part of its rule modernization effort, including rules, guidance, and processes that should be a focus for modernization in light of evolving markets, changing business practices, and the adoption of new technologies.

COMMITTEE COMMENTS

The Committee appreciates the opportunity to submit comments in response to this Notice, and supports FINRA's initiative to modernize its rules, guidance, and processes. The Committee supports FINRA's focus on assessing the effectiveness and efficiency of specific FINRA rulesets, guidance, and processes with an eye toward "eliminating inefficiencies and reduc[ing] unnecessary burdens." The Committee particularly appreciates that FINRA has taken a holistic view toward rule modernization in considering (and soliciting comment on) whether certain FINRA rules and processes may overlap with requirements that dual-hatted broker-dealers may be subject to under other regulatory regimes, such as the Investment Advisers Act of 1940, as amended (the "Advisers Act") and/or state insurance law.

[1] The Committee is a coalition of many of the largest and most prominent issuers of annuity contracts. The Committee's 32 member companies represent approximately 80% of the annuity business in the United States. The Committee was formed in 1981 to address legislative and regulatory issues relevant to the annuity industry and to participate in the development of insurance, securities, banking, and tax policies regarding annuities. For over four decades, the Committee has played a prominent role in shaping government and regulatory policies with respect to annuities at both the federal and state levels, working with and advocating before the SEC, CFTC, FINRA, IRS, Treasury Department, and Department of Labor, as well as the NAIC and relevant Congressional committees. A list of the Committee's member companies is available on the Committee's website at www.annuity-insurers.org/about-the-committee/.

[2] *See*, e.g., FINRA Regulatory Notice 25-04, FINRA Launches Broad Review to Modernize Rules Regarding Member Firms and Associated Persons (March 12, 2025), available here.

In this letter, the Committee focuses on six (6) topics that it believes FINRA should prioritize as part of its rule modernization review:

- Harmonizing FINRA's rules with requirements under the Advisers Act and state insurance law;
- Aligning FINRA rules with wholesale distribution activities of registered insurance products;
- Modernizing FINRA rules regarding gifts, entertainment, and non-cash compensation;
- Improving the effectiveness and efficiency of advertising filing and review processes under FINRA Rule 2210;
- Assessing FINRA Rule 1017 and FINRA's membership application review process; and
- Evaluating internal transparency and industry engagement.

1. Harmonizing FINRA's Rules with Requirements Under the Advisers Act and State Insurance Law

Committee members are life insurance companies, most of which have affiliated broker-dealers that distribute and/or sell SEC-registered insurance products ("registered insurance products")[3] and affiliated investment advisers that recommend registered insurance products and/or provide advice to clients through asset allocation or other investment advisory programs. Given this structure, Committee members and their affiliated companies are subject to multiple regulatory regimes, including FINRA rules, federal securities laws and regulations, state securities laws and regulations, and state insurance laws and regulations.

Given the scope and breadth of regulatory requirements to which Committee members must comply, the Committee appreciates FINRA's focus on areas "[w]here . . . FINRA's oversight of its member firms interact with other non-FINRA regulatory requirements in a manner . . . [that causes] unnecessary or duplicative burdens, insufficiently tailored requirements, [or] member firm or investor confusion."[4] The Committee has focused its comments in this letter on areas where FINRA requirements overlap with (1) requirements applicable to the distribution of registered insurance products under state insurance law and (2) requirements applicable to registered investment advisers under the Advisers Act.

a. State Insurance Law

In all states, registered insurance products, and the activities of insurance companies who issue those products, are regulated by the state's insurance regulatory authority. In addition, intermediaries offering insurance products (*e.g.*, insurance producers) are also regulated and licensed by the applicable insurance regulatory authorities. State insurance laws and regulations impose a multitude of regulatory requirements on insurance companies and insurance producers in connection with the issuance, sale, and marketing of insurance contracts relating to such matters as licensing, accounting, investment, solvency, minimum capital, reporting, market conduct and sales practices, and consumer protection. Certain of

[3] Many committee members have affiliated broker-dealers that also offer a full menu of securities products to retail customers.

[4] *See* Notice at pg. 4.

these state insurance law requirements imposed on insurance producers can, at times, overlap with FINRA requirements imposed on broker-dealers that sell registered insurance products.

One example of such an overlap lies in training and continuing education ("CE") requirements. Under the NAIC Suitability in Annuities Transactions Model Regulation ("Model 275"), all recommendations by agents and insurers must be in the best interest of the consumer.[5] Model 275 also imposes express training obligations on insurers and insurance producers with respect to annuities. These are intended to ensure that licensed insurance producers understand annuity products generally and also understand the annuity products issued by a specific issuer. The insurer's supervisory system also must include product-specific training that explains all the material features of its annuity products to its licensed insurance producers.

Model 275's training obligations apply to insurance producers that also serve as registered representatives associated with FINRA member broker-dealers. FINRA imposes its own CE requirements through its two mandatory programs: the Regulatory Element and the Firm Element.[6] The Firm Element of FINRA's CE program requires broker-dealers to establish a formal training program to keep registered persons, including individuals who maintain solely a permissive registration consistent with Rule 1210.02, up to date on topics related to professional responsibility and to the role, activities, and responsibilities of the registered person.[7] The content presented during training intended to comply with Model 275 invariably overlaps with content developed by an affiliated broker-dealer to comply with the Firm Element. The Committee believes that there are circumstances where registered representatives and their firm should be granted express authority to rely on training under Model 275 to satisfy requirements under FINRA's Firm Element requirement (and any other applicable CE requirements on a state-by-state basis).

b. Advisers Act

Many Committee members have affiliated investment advisers that recommend registered insurance products and/or provide advice to clients through asset allocation or other investment advisory services. Those investment advisers are typically registered with the Securities and Exchange Commission ("SEC") and subject to the Advisers Act and the regulations thereunder. Other Committee members are registered as broker-dealers and as investment advisers. We refer to FINRA member firms that are dually registered as investment advisers or that have an affiliated investment adviser as "dually-registered firms." There are a number of areas where FINRA rules and/or guidance impose burdensome requirements on dually-registered firms and their associated persons in situations where the firms and/or their registered representatives are functioning *solely* in their investment advisory capacity. Below are two examples of this overlap and suggestions as to how the withdrawal and/or modification of certain FINRA guidance would help ease regulatory burdens on dually-registered firms.

Communications Regarding Advisory Services. FINRA's General Counsel's office issued an interpretive letter in 1998 indicating that NASD Rule 2210, the predecessor to FINRA Rule 2210, prohibits the use of performance projections by persons dually-registered with a member firm and an investment adviser.[8] This letter applies Rule 2210 to materials relating to

[5] NAIC's Model 275 can be found here.

[6] *See* FINRA Rule 1240 (Continuing Education).

[7] *See* FINRA Rule 1240(b)(2).

[8] *See* Interpretive Letter to Dawn Bond, FSC Securities Corporation, July 30, 1998, available at https://www.finra.org/rules-guidance/guidance/interpretive-letters/dawn-bond-fsc-securities-corporation ("FSC Letter"). For the sake of convenience, we discuss this letter in the context of FINRA Rule 2210 even

services provided by a dual registrant, FSC, solely in its investment advisory capacity. Accordingly, the letter prohibits the use of material that is permissible (but subject to restrictions, limitations, and affirmative obligations) under Rule 206(4)-1 under the Advisers Act. The justification for FINRA's response was as follows:

> Response: NASD Conduct Rule 2210 (Rule) sets forth specific requirements on the use of advertisements and sales literature by members when communicating with the public . . . As a registered broker/dealer and member of the NASD, FSC and its registered representatives are subject to all of the requirements in the NASD Conduct Rules . . .

It is inappropriate to apply FINRA's communication rules to dually-registered firms and their associated persons if a communication relates solely to investment advisory activity and is subject to Rule 206(4)-1 under the Advisers Act and/or the anti-fraud provisions of the Advisers Act. Investment advisory services often are fundamentally different from brokerage services in terms of the role that is played and the parties for whom services are performed (*e.g.,* offering and selling securities as a direct or indirect agent of the issuer while distributing securities to the market, as compared to providing investment advice solely as an agent to advisory clients). Applying FINRA's communications rules, which contemplate an entity acting on the "sell" side to an entity acting *solely* on the "buy" side, makes little sense and often confuses investors as to the role engaged in by the dually-registered firm and its associated persons and the protections and regulatory regime that apply.

> The FSC Letter also states that:
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> Regarding NASD rules, it is important to determine if these materials are being used by registered persons of the member and may be considered advertisements or sales literature related to *promoting the member's securities business*. For example, some dually registered persons engage in activities limited to writing financial plans for a fee that do not include references to specific securities . . . The NASD has not required that the member name be included on such financial plans. If, however, particular securities are recommended . . ., NASD Conduct Rule 2210 would require disclosure of the member's name on the materials.

We are not aware of FINRA consistently following its own guidance that is quoted in italics above. "Promoting the member's securities business" refers to a broker-dealer promoting its *brokerage* business. It does not refer to a dually-registered firm promoting its or its affiliate's *investment advisory* business. In the second and third sentences above FINRA distorts the plain meaning of "securities business" to include merely referring to specific securities or to recommending securities. There is no legal basis for interpreting this language in this manner. A mere reference to securities or a recommendation of securities is *not* tantamount to promoting a dually-registered firm's brokerage business. It is worth remembering that no investment adviser can avoid providing advice about securities - the definition of investment adviser literally entails a person engaged in the business of providing advice about securities for compensation. Thus, every investment adviser provides investment advice about securities. Accordingly, many, if not most, investment advisory marketing pieces will refer to securities. FINRA's conclusion above has thus meant that virtually any advertisement by a dually-registered firm regarding its investment advisory services is subject to Rule 2210. If a marketing piece promotes a dually-registered firm's investment advisory services and refers to securities it does *not* somehow become a promotion of the firm's *brokerage* activities. FINRA should begin interpreting the phrase "promoting the member's securities business" in a manner consistent with its plain meaning.

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though the letter preceded this rule and relates to NASD Rule 2210. Likewise, we reference FINRA in discussing the letter even though the letter was issued by NASD Regulation, Inc.

> The FSC Letter similarly states:
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> NASD Conduct Rule 2210 governs all member communications with the public, including all third party materials used by a member or its registered persons. In administering the rule, however, NASD Regulation has not required the filing of marketing materials that are used exclusively to solicit on behalf of an advisory business. In accordance with this policy, the staff has not required filing of third-party marketing materials that: (i) purport to solicit customers for investment advisory services; (ii) *do not include the member's name; and (iii) do not contain references to mutual funds, variable annuities or other securities*." (Emphasis added).[9]

Similar to the point made above, the mere reference to a dually-registered firm's name or to securities does *not* somehow transform a communication created by a third-party investment adviser (that is not a broker-dealer) into a marketing piece promoting the *brokerage* business of a dually-registered firm. FINRA's interpretation of the italicized language is unsupportable and divorced from the plain meaning of the words. Unfortunately, the FSC Letter results in investment advisory material created by third-party investment advisers (that are not broker-dealers) being subject to Rule 2210 merely because they are handed to dually-registered firms and reference securities or the name of the dually-registered firm (even if such firm acts solely in its investment advisory capacity with respect to an investment advisory program). The result is illogical. If one applied FINRA's logic in the FSC Letter to the investment advisory regulatory regime, then almost every single marketing piece used by a legal entity that is both an investment adviser and a broker-dealer would be subject to Rule 206(4)-1 under the Advisers Act, *including those that only discuss the entity's brokerage services* (simply because it refers to the name of the entity or refers to securities).

The SEC recently undertook a comprehensive review of Rule 206(4)-1 under the Advisers Act and significantly updated the rule. Among other things, the amended rule considered investment advisers that also are registered as broker-dealers. We suggest FINRA conduct a similar review with respect to Rule 2210 and amend it (and other communication rules) so that FINRA does not force dually-registered firms and their personnel to make disclosures that are designed for entities that offer and sell securities in offerings, but not for entities engaged in discretionary portfolio management or other investment advisory services. The Committee recommends that FINRA withdraw or significantly modify the FSC Letter to clarify that material used by member firms and/or their associated persons to exclusively promote investment advisory services should not be subject to FINRA's communication rules.

License Restrictions for Dual-Hatted Individuals. FINRA's guidance related to licensing in connection with investment advisory services performed by dual-hatted individuals dates back to NASD Regulatory Notices 94-44 and 96-33. The guidance notes that a limited registered representative (such as a representative who only holds a Series 6 license) may not execute transactions in securities not covered by his or her FINRA registration. Essentially, registration with FINRA as a registered representative subjects an individual to all FINRA rules, regulations, and requirements, including licensing requirements, even if the individual is performing activities solely in his or her advisory capacity. As an example, in NTM 96-33, the NASD stated as follows:

> **Question #4**: Is it appropriate for a limited representative (i.e., a Series 6 Investment Company Representative) to execute Article III, Section 40 transactions in products such as equity securities that are not covered by that registration category?

[9] The FSC Letter also contains overly broad language regarding the licensing obligations of advisory personnel who play a role in overseeing securities trades placed by third-party investment advisers.

> **Answer**: A limited RR who is otherwise in compliance with applicable federal and state registration requirements, such as the SEC's investment adviser registration requirements, may not execute transactions in securities not covered by his or her NASD registration. Registration with the NASD as a representative subjects an individual to all NASD rules, regulations, and requirements, including qualification requirements. Those rules preclude a limited representative from *acting as a representative* in any area not covered by his or her registration category. A limited representative who wishes to execute transactions in securities not covered by his or her registration category is required to pass an appropriate qualification exam (Emphasis added).

The Committee recommends that FINRA reconsider this guidance and limit FINRA's licensing requirements to only those actions taken while an individual is acting on behalf of his or her broker-dealer, or on behalf of a person other than a registered investment adviser, bank, savings and loan association, credit union, or insurance company. This would be consistent with the last two sentences of the above quoted language. In particular, the Committee asks FINRA to clarify that when an individual is carrying out an activity *exclusively* on behalf of an investment adviser, for instance, it is not "acting as a representative." The Committee also asks FINRA to confirm that the phrase "execute transactions in securities" requires that commissions or other transaction-based compensation be paid in connection with the securities transaction.

2. Aligning FINRA's Rules with Wholesale Distribution Activities

Committee members often have broker-dealers whose sole activity is to serve as the principal underwriter or engage in the wholesale distribution ("Distributor BD") of registered insurance products issued by their affiliated insurance company. These Distributor BDs do not maintain any customer accounts or hold any customer funds or securities. Those customer account relationships are instead maintained by affiliated insurance companies (under insurance laws) and separate retail broker-dealers that sell the registered insurance products. Further, these Distributor BDs are often staffed with appropriately registered personnel who are employed by their affiliated insurance companies or other management companies and also associated with the Distributor BDs.

Limited Ruleset for Distributor BDs. The Committee recommends that FINRA adopt a limited ruleset specifically for Distributor BDs. Their activities are low-risk, and many existing FINRA rules impose burdensome requirements that offer no evident investor protection benefits, given that these firms do not maintain customer accounts, funds, or relationships. For example, FINRA Rule 3110 imposes prescriptive inspection cycles based on whether a particular location is classified as an Office of Supervisory Jurisdiction ("OSJ"), branch office, supervisory branch office, or non-branch location. These inspection cycles are based entirely on how an office is classified, but fail to account for the risk profile of the broker-dealer. This results in a Distributor BD with limited operations and no customer accounts or relationships being subject to the same inspection requirements as large, retail-focused broker-dealers with more complex operations. In addition, these Distributor BDs are too frequently subject to time consuming, and resource draining requests from FINRA and other regulatory authorities who request information or descriptions of compliance with rules that are inapplicable to their activities.

The Committee's request is not without precedent – in 2016, FINRA adopted a dedicated ruleset for Capital Acquisition Brokers ("CABs"), recognizing that "less extensive supervisory requirements" were appropriate because CABs' activities were "limited to specific, lower risk capital raising."[10] The Committee believes that similar treatment is warranted with respect to

[10] *See*, e.g., FINRA Regulatory Notice 25-06, FINRA Requests Comment on Modernizing FINRA Rules, Guidance, and Processes to Facilitate Capital Formation (March 20, 2025), available here; *See also* Regulatory Notice 16-37, SEC Approves FINRA's Capital Acquisition (CAB) Rules (Oct. 17, 2016), available here.

broker-dealers whose business activities are limited to acting as principal underwriter or wholesale distributor of registered insurance products issued by an affiliate.

Supervision of Insurance Company Personnel. The Committee asks that FINRA issue additional guidance which would serve to create practical and workable boundaries regarding a broker-dealer's supervisory obligations, if any, over personnel involved in the distribution of registered insurance products at an affiliated insurance company. In 1968, the SEC issued a release (the "1968 Release") excusing an insurance company from registering as a broker-dealer if a wholly-owned subsidiary was instead registered as a broker-dealer and, among other things, assumed "full responsibility for the securities activities of all insurance company personnel engaged directly or indirectly in the variable annuity operations."[11] While it is clear that insurance agents selling registered insurance products are considered to be engaged in the variable annuity operation, the 1968 Release did not further elaborate upon which other insurance company personnel should be considered to be "engaged directly or indirectly in the variable annuity operation" and thus associated with the broker-dealer. This lack of guidance has led to regulatory uncertainty and overreaching by FINRA staff into activity which is properly regarded as activity engaged in by the insurer. Committee members note that over time, significant resources are expended on debates with, and education of, FINRA, SEC and state securities regulatory staff related to the intricacies of interpreting and applying the 1968 Release under specific factual situations.

3. Modernizing Rules Regarding Gifts, Entertainment, and Non-Cash Compensation

The Committee recommends that FINRA review its rules regarding gifts, entertainment, and non-cash compensation with the goal of modernizing their requirements. The Committee notes that in April 2014, FINRA launched a retrospective review of its gifts, gratuities, and non-cash compensation rules to assess their effectiveness and efficiency.[12] In December 2014, FINRA published a report on its review, noting that the rules could benefit from updating to better align the investor protection benefits and economic impacts.[13] In August 2016, FINRA published Regulatory Notice 16-29 ("RN 16-29") soliciting comments on changes to the gifts, gratuities, and non-compensation rules, but ultimately decided not to move forward with the proposal.[14] The Committee believes that FINRA's conclusion in its December 2014 report – namely that the rules could benefit from updating – is even truer today, 10 years later. The Committee highlights below two areas where FINRA's non-cash compensation rules would benefit from amendments and/or further guidance.[15]

Interpretive Position Regarding the Combination of Education Meetings with Other Non-Cash Awards. FINRA Rule 2320(g)(4)(C) sets forth the requirements with respect to training and education meetings ("T&E Meetings") held for associated persons by

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[11] *See* Distributions of Variable Annuities by Insurance Companies Broker-Dealer Registration and Regulation Problems Under the Securities Exchange Act of 1934, Exchange Act Release No. 34-8389 (Aug. 29, 1968).

[12] *See* FINRA Regulatory Notice 14-15, FINRA Requests Comment on the Effectiveness and Efficiency of its Gifts and Gratuities and Non-Cash Compensation Rules (April 8, 2014), available here.

[13] FINRA Retrospective Rule Review Report: Gifts, Gratuities, and Non-Cash Compensation (December 2014), available here.

[14] *See* FINRA Regulatory Notice 16-29, FINRA Requests Comment on Proposed Amendments to Its Gifts, Gratuities and Non-Cash Compensation Rules (Aug. 8, 2016), available here.

[15] The Committee acknowledges FINRA's May 29, 2025 rule filing with the SEC that would, among other things, raise the current $100 gift limit in FINRA Rule 3220 (Influencing or Rewarding Employees of Others) to $250. The Committee generally supports FINRA's efforts to raise the gift limit and plans to separately provide comments regarding that proposal.

member firms or offerors. Under the terms of that exception, reimbursement by an offeror is permitted provided that certain conditions are met. In March 2001, FINRA issued an Interpretive Letter taking the position that an "offeror may not pay for golf outings, tours or other forms of entertainment while at a meeting it sponsors for the purpose of training or education."[16] The Committee believes that this interpretive position is overly broad and prescriptive, and fails to take into account the numerous existing safeguards that prevent a T&E Meeting from becoming a lavish event, including: (1) limits on the appropriate location for a T&E Meeting; (2) the prohibition on reimbursement of the costs for guests of the associated person; (3) the limitations for paying for expenses incurred beyond the time necessary for the actual T&E Meeting; and (4) the obligation for the training to occupy "substantially all of the workday." As a result of these significant limitations, the Committee believes that FINRA should adopt a principles-based standard and/or issue guidance recognizing that allowing some type of measured entertainment would not impact the status of a T&E Meeting.

Clarification of an Offeror's Obligations Under FINRA Rule 2320(g)(4)(E). The Committee believes that contributions made by a non-member company under FINRA Rule 2320(g)(4)(E) could be interpreted as imposing a requirement on the non-member company to verify if, for instance, an incentive trip pursuant to FINRA Rule 2320(g)(4)(D) adheres to FINRA rules. The Committee requests that FINRA clarify that the non-member company does not have an obligation to confirm that a member's program conforms to the non-cash compensation rules.

4. Improving the Effectiveness of Advertising Filing and Review Processes under FINRA Rule 2210

The Committee recommends that FINRA adopt a more principles-based and risk-based approach to public communications, particularly regarding filing requirements and supervisory pre-review mandates. FINRA Rule 2210 (Communications with the Public) establishes standards for how FINRA member firms communicate with the public, including those related to the content of communications, principal review and approval, FINRA filing requirements, and recordkeeping. Many of these requirements are prescriptive and require firms to file such communication with FINRA's Advertising Regulation Department (the "Department") and/or subject a communication to principal review based on the type of product discussed in the communication, the expected audience, and/or the medium through which the communication appears. These requirements are excessively complicated and, in the experience of Committee members, do not always bear a relationship with the potential risks that a communication, or the product discussed within a communication, may present.

Pre- and Post-Use Filing Requirements. Of particular note is Rule 2210(b), which provides a list of communications that must be filed on a pre- or post-use basis with FINRA. In Committee members' experience, the list of materials required to be pre-filed or post-use-filed bears almost no relationship to the potential risks these products present. The Committee is particularly interested in the general requirement that all variable product and mutual fund communications be filed with the Department. In the Committee's view, a more risk-based approach to the filing requirements would allow FINRA to deploy its advertising review resources more strategically, which could include spot-checking material related to various types of securities products that the Department believes may present risks to investors, with more attention paid to those products that present a higher degree of risk. This approach would be consistent with FINRA's examination program and guidance concerning member supervisory systems and

[16] Letter from Mary Schapiro, President NASD (March 7, 2001) available here; *See also* Regulatory & Compliance Alert (Summer 2000) at p. 13 ("reimbursement or payment for golf outings, tours or other forms of entertainment while at a location for the purpose of training or education would not be permissible.").

compliance programs and would support FINRA's goal of developing "more efficient and effective regulatory requirements."[17]

In offering this comment, the Committee acknowledges that the general requirement to file all variable product and mutual fund communications stems from certain provisions of the federal securities laws, which exempt such communications from SEC filing requirements if they are filed with FINRA. Despite this point, the Committee believes that FINRA's modernization initiative, coupled with the SEC's focus on facilitating capital formation, presents a unique opportunity for FINRA to explore with the SEC the possibility of a regulatory regime in which variable product and mutual fund communications are exempt from filing, or subject to a principles-based and risk-based approach.

Department Review of Communications. The Committee encourages FINRA to assess its advertising review processes and guidance to provide transparency about how its staff interprets certain FINRA rules and to ensure consistency amongst different FINRA reviewers. Committee members often encounter situations where the Department will adopt an interpretation of FINRA's rules that is inconsistent with and/or directly conflicts with prior interpretations taken by the Department. This situation inevitably leads to FINRA not approving communication pieces that have either been approved in a substantially similar form previously or are currently circulating from other firms of a similar standing. In addition, particularly in the time period after the COVID-19 pandemic, the turn-around time for advertising review has been much longer and has negatively impacted the ability to bring registered insurance products to market in a timely manner.

Modernizing Content Submission Processes. The Committee encourages FINRA to modernize its Advertising Regulation Electronic Files application (the "AREF application") to allow for greater flexibility in the ways in which member firms can provide certain communications to FINRA. For example, the methods through which firms currently submit website content are outdated and could be updated to allow for more modern alternatives, such as links to non-production environments of a website. The Committee believes that a more modern approach would allow for a more productive dialogue between firms and FINRA staff regarding submitted content.

5. Assess FINRA Rule 1017 and FINRA's Membership Application Process

The Committee believes that FINRA should conduct a comprehensive review of FINRA Rule 1017 (Application for Approval of Change in Ownership, Control, or Business Operations) and the associated membership application process with the goal of developing a risk-based, streamlined framework with regard to lower-risk activities. The Committee highlights here two aspects of Rule 1017 that are, in the Committee's view, unnecessarily onerous for member firms given their low risk: (1) assessing if adding a non-material business line constitutes a "material change in business operations" under FINRA Rule 1017(a)(5); and (2) indirect ownership changes requiring a Continuing Membership Application ("CMA") filing under FINRA Rule 1017(a)(4). The Committee also comments generally on the New Membership Application ("NMA") and CMA processes themselves, which have in recent years become an opportunity for FINRA's Membership Application Program Group ("MAP Group") to examine firms on certain "hot topics" that are not necessarily connected to the application's original purpose. As a general matter, the Committee believes that many of the recommended changes identified in FINRA Regulatory Notice 18-23, *Membership Application Proceedings: FINRA Requests Comment on a Proposal Regarding the Rules Governing the New and Continuing Membership Application Process* (July 26, 2018) were headed in the right direction and a re-proposal of those changes would be beneficial.

***Business Line Materiality Decisions*.** FINRA Rule 1017(a)(5) requires a CMA filing for any "material change in business operations." FINRA Rule 1011(l) defines a "material change in

[17] *See* the Notice at pg. 1.

business operations" as including, but not limited to, a change involving: (1) removing or modifying a membership agreement restriction; (2) market making, underwriting, or acting as a dealer for the first time; or (3) adding business activities that require a higher minimum net capital under Securities Exchange Act of 1934, as amended ("Exchange Act") Rule 15c3-1. In Committee members' experience, the difficulty and inefficiency of Rule 1017(a)(5) does not stem from these three enumerated categories of changes, but from the difficulty of analyzing the materiality of other, non-enumerated changes in business operations.

For example, member firms that want to start a new business line have to assess the materiality of that business line with regard to their operations. While NASD Notice to Members 00-73 provides some clarity regarding the type of information broker-dealers should consider when assessing the "materiality" of a proposed change, often times a firm's materiality analysis ends up being submitted to FINRA in the form of a materiality consultation letter (a "MatCon Letter"). The Committee believes that more explicit guidance in this area would be appropriate – for example, the Committee believes that FINRA should explicitly except from the term "material change in business operations" the addition of business lines that do not impact a firm's net capital or customer protection rule status. This type of change would allow firms to be nimbler in their expansion of business lines (which would further facilitate capital formation) and allow FINRA to focus its resources on higher-risk changes to a broker-dealer's operations.

Indirect Ownership Changes. FINRA Rule 1017(a)(4) requires a CMA for any "change in the equity ownership or partnership capital of the member that results in one person or entity directly or indirectly owning or controlling 25 percent or more of the equity of partnership capital." In Committee members' experience, many CMAs filed in connection with Rule 1017(a)(4) pertain to indirect ownership changes within a broker-dealer's corporate structure that have no direct or indirect impact on the day-to-day operations of the broker-dealer. Despite the fact that the broker-dealer's operations will be identical pre- and post-indirect ownership change, FINRA Rule 1017(a)(4) subjects a firm to a CMA filing, which can often result in substantial delays to the closing of certain transactions. Due to the low-risk nature of most indirect ownership changes, the Committee suggests FINRA create a significantly streamlined process. Such a process could be conditioned on certain factors being satisfied, such as: there will be no change to the direct owner of the broker-dealer; there will be no change to the ultimate owner of the broker-dealer; there will be no change to the day-to-day operations of the broker-dealer; and no new person will be involved in making management decisions for the broker-dealer. In the alternative, an exemption or waiver process for such a CMA would be beneficial as well.[18]

Committee members often have multiple layers of corporate owners above their broker-dealers. For tax, cost, or other reasons, they occasionally swap out one intermediate level holding company above a broker-dealer for a different intermediate level holding company. Similarly, for legal structuring or tax reasons, firms occasionally may seek to add a new intermediate holding company above the broker-dealer (*e.g.*, going from 4 intermediate level holding companies above a broker-dealer to 5 such companies). Such "internal restacking" transactions pose no substantive risks to a broker-dealer or its customers – they merely result in changes to the corporate structure that have no real-world consequences whatsoever to the broker-dealer itself.

More Focused CMA and NMA Reviews. In recent years, Committee members have observed that the MAP Group's reviews often stray from the application's original purpose. This leads to extended review times and forces broker-dealers to address issues that are irrelevant to the application. For example, in connection with nearly every CMA, the MAP Group requests documentation regarding the broker-dealer's ownership structure, including documentation regarding all 10% or greater owners. While this review may be useful for CMAs filed in response to ownership changes, it has no clear purpose for a CMA filed, for example, to operate a new business line. Committee members also recommend that FINRA re-examine its guidance and processes related to non-controlling owners of a member firm in the context of a CMA or an NMA. Committee member experiences with filing CMAs and NMAs has resulted in inconsistent

[18] *See* FINRA Regulatory Notice 18-23 at p. 17-18.

approaches with respect to the level of detail requested and required by the MAP Group on non-controlling firm owners and appears to be subject to the vicissitudes of the reviewing analyst working on the application. In particular, given that many of the owners can be limited partners or non-managing members that have only "economic" interests, and not "management" or "voting" interests in the Firm, the extreme focus on such non-controlling parties is overly burdensome and intrusive, and can serve to create a chilling effect on interest in funding operations of financial enterprises that include broker-dealer operations.

6. Evaluating Internal Transparency and Industry Engagement

The Committee recommends that FINRA evaluate the way in which it interacts with member firms, including through its retrospective rule reviews and Regulatory Notices requesting comment on specific rulesets or topics. The Committee appreciates the substantial involvement of many in the industry on FINRA's various Advisory Committees. However, the Committee believes that further transparency should be provided regarding the activities of the Advisory Committees and FINRA's decision-making process regarding whether they move ahead with certain proposals or initiatives. There are a number of examples over the past 15 years in which FINRA requested comment in connection with a retrospective rule review or Regulatory Notice where, after receiving substantial industry comment, FINRA failed to provide any meaningful update on the status of the proposal. One example is FINRA's retrospective rule review and resulting Regulatory Notice related to gifts, entertainment, and non-cash compensation (discussed above), for which no meaningful update has been provided for nearly 10 years.[19] The Committee believes that FINRA should develop a process through which it reports back to the industry on its various initiatives, including telling the industry whether certain contemplated rule changes will move forward or be closed out.

CONCLUSION

The Committee appreciates the opportunity to provide these comments on the Notice. Please do not hesitate to contact Clifford Kirsch (212.389.5052 or CliffordKirsch@eversheds-sutherland.com) or Eric Arnold (202.383.0741 or EricArnold@eversheds-sutherland.com) with any questions or to discuss this comment letter.

* * *

Respectfully submitted,

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Eric Arnold

FOR THE COMMITTEE OF ANNUITY INSURERS

[19] *See* FINRA Regulatory Notice 16-29.