sifma

Invested in America

March 27, 2017

By Electronic Mail to *pubcom@finra.org*

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20549-1090

Re: FINRA Regulatory Notice 17-06: Proposal to Amend Communications with the Public Rule to Permit the Distribution of Customized Hypothetical Investment Planning Illustrations that Include the Projected Performance of an Asset Allocation/Investment Strategy

Dear Ms. Asquith:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to respond to FINRA's request for comment on Regulatory Notice 17-06 ("RN 17-06" or the "Proposal"),[2] which proposes amendments to FINRA's Communications with the Public Rule (FINRA Rule 2210). The Proposal would create an exception to the rule's prohibition on projecting performance to permit a firm to distribute a customized hypothetical investment planning illustration that includes the projected performance of an asset allocation or other investment strategy, but not an individual security, subject to specified conditions.

I. Executive Summary of Comments

SIFMA applauds FINRA's retrospective rule review efforts. SIFMA believes this process should facilitate the identification of outdated and inefficient rules and

[1] SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over $2.5 trillion for businesses and municipalities in the U.S., serving clients with over $18.5 trillion in assets and managing more than $67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] Regulatory Notice 17-06 (Communications with the Public) (February 2017), available at http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-06.pdf (last visited March 23, 2017).

interpretations while also recognizing and balancing investor protection concerns. We believe that the Proposal reflects the benefits of the rule review process. SIFMA believes that FINRA can further advance its laudable efforts with respect to FINRA Rule 2210 by:

- Clarifying its position with respect to basing projections on past or current particular investments; and
- Accounting for differences between retail and institutional investors.

SIFMA's comments are further discussed in the various sections of this comment letter.

II. Rule Assessment and Proposal Processes

The Proposal is an outgrowth of FINRA's retrospective rule review process.[3] In December 2014, FINRA published a report assessing its rules related to communications with the public.[4] FINRA stated in the report that "the rules and FINRA's administration of them may benefit from some updating and recalibration to better align the investor protection benefits and economic impacts."[5] To that end, the report included several recommendations to enhance the effectiveness and efficiency of the rules.[6]

SIFMA applauds FINRA for its efforts in undertaking an extensive, multi-step assessment process in connection with the Proposal. We understand that FINRA met with and solicited feedback from a broad range of interested parties.[7] The resulting report reflects a thorough and thoughtful data collection and analytic process. Further, the Proposal reflects careful consideration of the feedback and recommendations of interested parties, including SIFMA and its member firms. We encourage FINRA to expand its use of these assessment techniques beyond proposals related to the retrospective rule review process. We believe FINRA, member firms, and investors would benefit from FINRA

---

[3] *See* News Release: FINRA Launches Retrospective Rule Review (April 8, 2014), available at https://www.finra.org/newsroom/2014/finra-launches-retrospective-rule-review (last visited March 20, 2017). *See also*, FINRA Retrospective Rule Review Report: Communications with the Public (December 2014), available at https://www.finra.org/sites/default/files/p602011.pdf (last visited March 6, 2017) and FINRA Regulatory Notice 14-14 (Retrospective Rule Review – Communications with the Public) (April 2014), available at http://www.finra.org/sites/default/files/NoticeDocument/p479810.pdf (last visited March 23, 2017).

[4] FINRA Retrospective Rule Review Report: Communications with the Public (December 2014), available at https://www.finra.org/sites/default/files/p602011.pdf (last visited March 6, 2017).

[5] *Id*. at 12.

[6] *See id*.

[7] *See generally* FINRA Retrospective Rule Review Report: Communications with the Public, at 5-6 (December 2014), available at https://www.finra.org/sites/default/files/p602011.pdf (last visited March 6, 2017).

applying a similar level of economic analysis, and transparency, to most if not all of its rule proposals.

SIFMA commends FINRA for engaging in a retrospective rule review process. SIFMA believes the process will result in changes to existing rules that increase the rules' effectiveness and efficiency without adversely impacting their investor protection goals. SIFMA hopes that FINRA will continue its retrospective rule review process, re-evaluating rules and interpretations on an ongoing basis to ensure they are still relevant and meeting their underlying investor protection mandates in a cost effective and efficient manner.

III. Overview of the Proposal

The Proposal arises from FINRA's assessment of its current Communications with the Public rule and existing guidance in connection with the retrospective rule review. In its Communications with the Public Rule Review Report, FINRA stated "[o]ne area that drew frequent comment involved the restrictions on predictions or projections and performance standards. Many stakeholders favored more permissive use of predictions or projections and alternative performance standards (e.g., hypothetical and back-tested performance, related performance, model performance and targeted returns) and greater clarity with respect to the current requirements."[8] As a result of this analysis, FINRA concluded the Communications with the Public rule could benefit from certain changes to "better align the investor protection benefits and the economic impacts" of the rule.[9]

Specifically, in RN 17-06, FINRA proposes to amend FINRA Rule 2210 to create an exception to the rule's prohibition on projecting performance to permit a firm to distribute a "customized hypothetical investment planning illustration that includes the projected performance of an asset allocation or other investment strategy, but not an individual security."[10]

The Proposal provides an exception to FINRA Rule 2210's prohibition of projections for a customized hypothetical investment planning illustration. The proposed exception would be available for all firms, including firms that operate only an online platform. The proposed exception also could be used with both current and prospective

[8] *Id.* at 3.

[9] *See generally* FINRA Retrospective Rule Review Report: Communications with the Public, at 12 (December 2014), available at https://www.finra.org/sites/default/files/p602011.pdf (last visited March 6, 2017).

[10] *See generally* Regulatory Notice 17-06 (Communications with the Public) (February 2017), available at http://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-06.pdf (last visited March 6, 2017).

customers. The hypothetical investment planning illustration may project an asset allocation or other investment strategy, but not the performance of an individual security.

The Proposal requires that there be a reasonable basis for all assumptions, conclusions and recommendations, and that the illustration clearly and prominently disclose the fact that the illustration is hypothetical and there is no assurance that any described investment performance or event will occur. All material assumptions and limitations applicable to the illustration would have to be disclosed.

The Proposal also establishes specific supervisory requirements for the permitted illustrations.

Subject to our comments below, SIFMA believes that these changes will improve the effectiveness and efficiency of the rules without compromising their underlying investor protection goals.

IV. Recommended Changes and Requests for Clarification and Guidance

SIFMA supports the investor protection objectives of the Communications with the Public rule. SIFMA believes that the rule has been largely effective in meeting its intended investor protection objectives.

As a general matter, SIFMA believes the proposed amendment in RN 17-06 would better align the rule's investor protection benefits and economic impacts. Importantly, the Proposal enhances our member firms' ability to provide retail investors with only brokerage accounts access to potentially useful projections currently available to investment advisory clients.

SIFMA respectfully suggests that FINRA consider the following changes to the Proposal, which we believe are consistent with the objectives underlying FINRA's proposed amendment to Rule 2210.

A. Clarification Regarding Basing Projections on Actual Investments

In connection with the Proposal, FINRA states that "basing a projection upon … the past performance of particular investments by an asset manager would not be reasonable."[11] It may be helpful to clarify this point. For example, what if a projection included in communication covered by Rule 2210(d) was based on a variety of factors, and one of the factors was the asset manager's experience with investments? Permitting the factoring of an asset manager's experience with particular investments may support a higher degree of confidence in the projection. If the Proposal does not permit <u>any</u> use of

[11] *See* FINRA Notice 17-06, at 3.

past performance of particular investments, FINRA should consider this issue in future rulemaking efforts. Factoring an asset manger's performance with particular investments into projections may be balanced by heightened disclosure standards, particularly with less sophisticated investors. In this way, principle based rules would provide an easier path to establishing a regulatory scheme with respect to projections.

B. Accounting for Investor Sophistication in Communication Rules

In its request for comment, FINRA raised the important issue of dually-registered firms and consistency between projection related practices for clients with investment advisory accounts versus those with only brokerage accounts.[12] Again, SIFMA commends FINRA for focusing on this point as it helps to better harmonize the communications available to all retail clients. However, in response to FINRA's requests, SIFMA offers that the proposal may not do enough to align the use of projections in communications to institutional investors because of relative flexibility available under the principle-based regulations applicable to investment advisers.

FINRA Rule 2210 already distinguishes between communications to retail investors and institutional investors.[13] In numerous ways, Rule 2210 distinguishes principal approval, filing requirement, and content standards applicable to each type of communication. In doing so, FINRA has sought to limit the definition of "institutional investors" under 2210 to those that FINRA believes "have either the sophistication required to scrutinize member sales material without the benefit of the filing and more prescriptive content standards applicable to retail communications, or have the resources necessary to hire an outside party with this sophistication."[14]

Unlike many retail investors, sophisticated institutional investors desire information on return targets and projections. And, in line with FINRA's objective in limiting the definition of institutional investors, these investors have a better ability to understand the validity of assumptions and practices used in preparing the projections. Finally, existing anti-fraud standards would continue to serve as important controls on inadequate disclosure and other misleading practices.

SIFMA respectfully requests FINRA consider, as part of its ongoing effort to improve its rules, distinguishing the content standards applicable to projections in retail communications versus institutional communications. While the Proposal represents an important advancement on the use of projections, FINRA can use future rulemaking

---

[12] *Id.* at 5, Request for Comment 2 and 3.

[13] *Compare* FINRA Rule 2210(a)(3) and (a)(5) as well as FINRA Rule 2210(b)(1) and (b)(3). *See also* the filing requirements applicable only to retail communications under FINRA Rule 2210(c).

[14] *See* Securities Exchange Act Release 34-66681, at 11 (March 29, 2012).

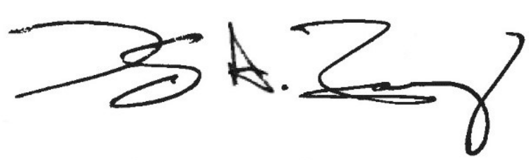
efforts to further distinguish the controls reasonably necessary for institutional communications from those in place for retail communications.

V. Conclusion

SIFMA appreciates the opportunity to comment on the Proposal. SIFMA commends FINRA for undertaking an evaluation of its Communications with the Public in an effort to find ways to improve the rule's effectiveness and efficiency. SIFMA believes the comments included in this letter should foster FINRA's efforts to update these rules and align the rules' costs and investor protection benefits. We look forward to a continuing dialogue with FINRA and working together on this Proposal.

If you have any questions or would like additional information, please contact Kevin Zambrowicz, Managing Director & Associate General Counsel, SIFMA, at (202) 962-7386 (kzambrowicz@sifma.org), or our counsel, Ronak Patel, Kelly Hart, at (512) 495-6444 (ronak.patel@kellyhart.com).

Very truly yours,



Kevin A. Zambrowicz
Managing Director &
Associate General Counsel

cc: Evan Charkes, Co-Chair, SIFMA Compliance & Regulatory Policy Committee
Mary Beth Findlay, Co-Chair, SIFMA Compliance & Regulatory Policy Committee

Ronak Patel, Kelly Hart