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April 27, 2018

By Electronic Mail to pubcom@finra.org.

Jennifer Piorko Mitchell
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 18-08:
SIFMA Comment on Proposal to Create New FINRA Rule 3290 to Streamline Requirements Regarding the Outside Business Activities of Registered Persons

Dear Ms. Mitchell:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to respond to the request for comment issued by the Financial Industry Regulatory Authority ("FINRA") in Regulatory Notice 18-08 ("RN 18-08")[2] regarding a proposal to consolidate FINRA Rule 3270 (Outside Business Activities of Registered Persons) and FINRA Rule 3280 (Private Securities Transactions of an Associated Person) into a single, streamlined rule that will reduce regulatory burdens on member firms, while still addressing fundamental investor protection concerns relating to registered persons' outside business activities.

In May 2017, FINRA issued Regulatory Notice 17-20, a retrospective review of its outside business activities and private securities transactions rules.[3] SIFMA provided

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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 18-08 (Feb 2018), *available at* www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-18-08.pdf.

3 *See* Regulatory Notice 17-20 (May 2017), *available at* www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-20.pdf.

comments to Regulatory Notice 17-20, expressing support for FINRA's effort to review the effectiveness and efficiency of FINRA Rules 3270 and 3280, and offering insights regarding how the rules can best meet their investor protection objectives through reasonably efficient means.

I. EXECUTIVE SUMMARY

SIFMA supports FINRA's efforts to consolidate FINRA Rule 3270 and FINRA Rule 3280 into a single rule governing the outside business activities of registered persons. Proposed Rule 3290 appropriately narrows firms' obligations to assess and supervise registered persons' outside business activities to those activities that pose the most risk to firms' customers.

Without detracting from the support stated herein, our comments on RN 18-08 highlight various issues that warrant consideration by FINRA during its amendment process for the rules governing outside business activities and private securities transactions. Our comments primarily request that FINRA (1) clarify certain definitions, such as "business activity" and "investment-related" activity, under the proposed Rule; (2) provide guidance on certain obligations under the proposed Rule; and (3) address disparities between the disclosure requirements of the proposed Rule and Form U4.

II. COMMENTS

A. General Comments

SIFMA members understand and support the foundational rationale underpinning FINRA's rules requiring the reporting of registered persons' outside business activities and firms' obligations to monitor, and in some cases approve of, those outside business activities. SIFMA members believe that the framework provided by current Rules 3270 and 3280 has generally served an important investor protection function, ensuring that registered persons do not engage in outside business activities that could result in conflicts detrimental to the interests of investors.

Despite the overall success of the current framework, Rules 3270 and 3280 are potentially less efficient and more burdensome than necessary to further the rules' investor protection goals. The bifurcation of the requirements into two separate rules is cumbersome, and the rules' principles themselves are in some cases unclear and overbroad. FINRA's recent retrospective review of the rules governing outside business activities and private securities transactions found quantifiable verification of these shortcomings. In a survey sent to all FINRA members as part of the review, approximately 60% of the respondents believed that there are outside business activities that should not be included within the scope of the current rules.[4]

Proposed Rule 3290 is a considerable improvement, and SIFMA members applaud FINRA's efforts. The new unified rule more succinctly sets forth firms' and registered persons'

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4 *See* RN 18-08 at n.8.

obligations with respect to outside business activities, which will help reduce confusion and clarify compliance standards. Under the bifurcated approach adopted in Rules 3270 and 3280, SIFMA members have often found inconsistencies and opacity to be impediments to compliance. The proposed Rule will be a marked improvement.

Nonetheless, proposed Rule 3290 retains some of the ambiguous requirements that SIFMA members have previously found problematic. In order to improve the outside business activities framework, we respectfully submit a number of suggestions. Specifically, and as detailed below in Section II.B, we request that FINRA clarify the definitions of "business activity" and "investment-related" activity, so that activities that do not raise investor protection concerns are excluded from the proposed Rule's disclosure requirements. We propose drawing a distinction between "personal" and strictly "business" activities, so that only "business" activities are covered by the proposed Rule. We note that firms' conflict of interest policies will supplement the proposed Rule to provide protection to investors in those instances in which "personal" activities conflict with firm customers' interests.

Addressing these issues is more important today than ever. More Americans are actively contributing to the "gig economy" or "sharing economy" as a way to improve their earnings. Income opportunities through such companies as Airbnb, Lyft, Uber, and others have become pervasive in the past half-decade, and registered persons often participate. Having clear and sound rules governing these outside business activities is vital, and our specific suggestions below are intended to improve the proposed Rule's efficacy in the current environment. Given the quickly evolving nature of these outside income opportunities, SIFMA also suggests that FINRA adopt guidance, such as FAQs, that would allow the Rule to adapt and evolve over time. It would be nearly impossible to anticipate and codify requirements for future advancements in the gig economy environment.

B. Specific Issues

1. FINRA should clarify the definition of "business activity" under proposed Rule 3290.02(b).

SIFMA members believe that the definition of "business activity" as currently proposed is relatively imprecise; certain terms used within the definition should be more precisely defined to diminish the potential for varied interpretations of the Rule. For example, the definition of "business activity" includes acting as an "officer," "director," or "partner" of an entity other than the member firm. FINRA should clarify that registered persons' business activities will fall under this definition only if they have been *formally* designated as an officer or director through a legal filing or through approval by a board of directors. This will avoid the ambiguities that would necessarily result from determining whether a registered person serves as a "de facto" officer or director. Similarly, the meaning of the term "partner" should be limited to situations in which a registered person has signed a *written* partnership agreement. Furthermore, a registered person's distinction as an officer, director, or partner of a legal entity should only be disclosed when that entity has the purpose of earning income, so that acting in such a capacity for a non-profit organization would be excluded from the Rule.

The definition of "business activity" also includes "receiving *compensation*, or having the reasonable expectation of *compensation*" from an entity other than the member firm for performing a business activity. As currently stated in the proposed Rule, "compensation" could be interpreted very broadly, and FINRA should specify the types of business activities that are and are not encompassed by this vague definition.

For example, as currently written, a registered person selling items on eBay could potentially be swept under the broad parameters of the definition, as the registered person would technically be receiving "compensation" from a person other than the member firm. If the registered person created a formal legal entity, such as a limited liability company (LLC), to sell the items on eBay, any compensation received from such business-motivated transactions would appropriately fall within the definition of "compensation." By contrast, compensation received by a registered person who directly sells his or her belongings on eBay should be excluded from the definition because such activity is strictly personal. Similarly, and as discussed further in the next section, renting out one's residence on Airbnb also results in the receipt of "compensation," but such compensation should not be covered by the definition when received for such nonbusiness-related activity.

2. FINRA should clarify the definition of "investment-related" activity under proposed Rule 3290.02(c).

It is of utmost importance that FINRA more precisely define "investment-related" activity or, in the alternative, provide thorough guidance on the types of activities that fall under this definition. SIFMA members are most concerned with the definition's treatment of "real estate" activities. The definition of "investment-related" includes activities pertaining to "real estate," which is an incredibly expansive field that could encompass numerous activities that do not pose a risk to member firms' customers. SIFMA members propose that the definition only include real estate activities performed for strictly business purposes. For example, activities such as engaging in business as a real estate broker or agent, or forming an LLC to purchase real estate and develop it for profit, should be considered investment-related activity and subject to a risk assessment. However, real estate ownership and activities that are primarily personal and generate limited income, such as receiving rental income from residential properties (*e.g.*, listing a primary residence or vacation home on Airbnb) or creating an LLC to purchase a personal residence, do not create conflicts with firm customers' interests and therefore should not be considered investment-related activity. For instances in which registered persons' personal investments in real estate conflict with firm customers' interests, firms' conflict of interest policies will provide appropriate and tailored procedures for disclosing and seeking approval for such investments.

The definition of "investment-related" also includes activities pertaining to "banking." SIFMA members strongly recommend that FINRA enumerate the activities covered by the term "banking" (*e.g.*, providing custody/safekeeping services, credit card processing, etc.).

3. FINRA should clarify the definition of "transaction-related compensation" under proposed Rule 3290.01(b).

In regards to acting as trustee for an immediate family member, SIFMA members seek guidance concerning the proposed Rule's application to situations in which a registered person is compensated for such activities. FINRA should clarify the meaning of "transaction-related compensation" included in proposed Rule 3290.01(b), which creates a carve-out for transactions on behalf of a registered person's immediate family member for which the registered person receives *no* transaction-related compensation. As written it is unclear whether certain types of compensation, such as receiving a flat fee, would be considered "transaction-related."

4. FINRA should provide specific guidance on the proposed Rule's application to other potentially disclosable activities including the receipt of trail commissions and investing and fundraising through crowdfunding activities.

SIFMA strongly suggests that FINRA takes this opportunity to address the proposed Rule's application to two specific activities that are commonly engaged in by registered persons.

The first of these activities is the receipt of continuing or trail compensation after a business activity has ceased. For example, a registered person may passively continue to receive insurance trail commissions, but no longer actively engage in insurance brokerage activities as part of his or her employment. SIFMA members seek clarity as to whether receipt of such commissions is encompassed by the proposed Rule.[5]

Secondly, investing and fundraising through crowdfunding platforms, such as Kickstarter, Indiegogo, GoFundMe, and CircleUp, have become exceedingly popular, and FINRA should determine whether such activities are encompassed by the definition of "business activity" or "investment-related" activity.

5. FINRA should specify the types of "material change" to a business or investment-related activity that must be disclosed to member firms pursuant to proposed Rule 3290(a).

The second sentence of proposed Rule 3290(a) states, "In the case of a material change to the *activity*, a registered person must provide the member with updated prior written notice and, with respect to any investment-related activity, receive updated prior approval." In context, "activity" must be interpreted to include both "business activity" and "investment-related" activity. However, SIFMA members suggest that FINRA consider revising this statement to read: "In the case of a material change to the investment-related activity, or a change to business activity that prompts the business activity to be considered investment-related activity, a registered person must provide the member with updated prior written notice and receive

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[5] SIFMA respectfully refers FINRA to two SEC no-action letters in which the SEC staff specifically permits retiring representatives to continue to receive passive compensation without receipt of such compensation being considered an outside business activity. *See* SEC No-Action Letter to SIFMA (Nov. 20, 2008); SEC No-Action Letter to Packerland Brokerage Services (March 18, 2013).

updated prior approval." This will clarify the requirement so that only material changes in business activities (*i.e.*, changes that cause the business activities to fall within the definition of "investment-related") will be disclosed to member firms. Furthermore, the revision will eliminate the requirement to unnecessarily notify a firm when a business activity has changed in nature, but remains noninvestment-related, because this would be an irrelevant change that would not require further review or approval by the firm.

6. FINRA should clarify member firms' obligation to "reasonably supervise" registered persons' compliance with firm imposed conditions or limitations on investment-related activity.

The proposed Rule would require registered persons to provide their member firms with prior written notice of outside investment-related activity. The member firm would then be required to conduct the upfront risk assessment described in 3290(b)(1)(A), and thereafter approve, approve subject to conditions or limitations, or disapprove such investment-related activity. If the member firm imposes conditions or limitations on its approval of a registered person's outside investment-related activity, the member firm would be required to "reasonably supervise" the registered person's compliance with such conditions or limitations pursuant to 3290(b)(3).

SIFMA members request guidance on what constitutes reasonable supervision for purposes of proposed Rule 3290(b)(3). Without further clarity, it would be difficult for member firms to develop systems and internal policies that would meet FINRA's expected supervision standard. SIFMA members recommend that FINRA issue specific examples as to what constitutes reasonable supervision in this context. For example, a member firm could meet the reasonable supervision standard by requiring a registered person to complete an annual attestation confirming that the registered person is in compliance with all conditions and limitations set forth in the member firm's written approval of an outside investment-related activity.

7. FINRA should address the disparities between the disclosure requirements of proposed Rule 3290 and Form U4.

FINRA should address the disparity between the definition of "business activity" under proposed Rule 3290.02(b), which includes acting as an "employee, independent contractor, sole proprietor, officer, director or partner" of an entity other than the member firm, and the definition of "other business" under Section 13 of Form U4, which requires disclosure of a registered person's activity as a "proprietor, partner, officer, director, employee, trustee, agent or otherwise." FINRA should clarify whether the two definitions can be interpreted to cover the same activities, and if not, FINRA should provide guidance on the difference between the two definitions. For example, we are aware that FINRA provided informal guidance stating that a registered person does not need to disclose under Section 13 of Form U4 the creation of an LLC to purchase a personal residence, which may be done for certain privacy reasons. SIFMA members seek clarity as to whether the same activity would therefore fall outside the scope of "business activity" for purposes of the proposed Rule.

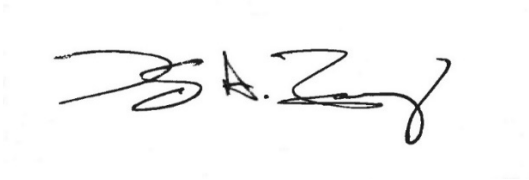
In addition, Section 13 of Form U4 specifically excludes reporting to FINRA of "*noninvestment-related* activity that is *exclusively* charitable, civic, religious or fraternal and is recognized as tax exempt." FINRA should clarify whether noninvestment-related activity on behalf of a tax exempt organization is also exempt from the Rule's proposed requirement to provide a member firm prior written notice of outside business activity.

III. CONCLUSION

SIFMA appreciates the opportunity to comment on RN 18-08. We reiterate our support for the consolidation and streamlining of rules governing registered persons' outside business activities and private securities transactions. We believe the comments included in this letter will further FINRA's effort to reduce the burden of disclosing, assessing, and supervising a broad range of business activities by tailoring the proposed Rule's application to those business activities that pose the most risk to member firms' customers.

We look forward to a continuing dialogue with FINRA. 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, Marlon Paz, at (202) 661-7178 (paz@sewkis.com).

Very truly yours,



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