

**VIA ELECTRONIC MAIL**

September 23, 2016

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

Re: Proposed Amendments to Gifts, Gratuities and Non-Cash Compensation Rules

Dear Ms. Asquith:

On August 10, 2016, the Financial Industry Regulatory Authority (FINRA) published its request for public comment on proposed amendments to FINRA Rule 3220 (Influencing or Rewarding Employees of Others), as well as on proposed FINRA Rule 3221 (Restrictions on Non-Cash Compensation), and proposed FINRA Rule 3222 (Business Entertainment) (collectively referred to in this letter as the Proposal or Proposed Amendments).<sup>1</sup> Among other significant changes, the Proposed Amendments would increase the gift limit from \$100 to \$175 per person per year and include a \$50 de minimis threshold below which firms would not have to keep records of gifts given or received. The Proposal also amends the non-cash compensation rules to cover all securities products, rather than only direct participation programs (DPPs), variable insurance contracts, investment company securities and public offerings of securities. Lastly, the Proposal creates a new rule addressing business entertainment that, among other things, requires firms to promulgate written policies and procedures related to business entertainment along with corresponding books and records requirements.

The Financial Services Institute<sup>2</sup> (FSI) appreciates the opportunity to comment on this important Proposal. FSI strongly supports FINRA's retrospective rule review efforts, which are vital to increasing the transparency and accountability of rulemaking, and will ensure that FINRA's rules remain relevant and are appropriately designed to achieve their objectives. With regard to the gifts and gratuities, non-cash compensation, and business entertainment rules in particular, FSI appreciates the careful and thoughtful manner in which FINRA collected input from various stakeholders, including FSI and our members, while developing potential common sense changes to update the existing rules and to better ensure that the rules adequately address their intended goals. FSI supports updating the gifts and gratuities and non-cash compensation rules and instituting specific business entertainment rules in the manner proposed and we offer suggestions

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<sup>1</sup> See Regulatory Notice, Gifts, Gratuities and Non-Cash Compensation Rules August 2016, available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-16-29.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-16-29.pdf)

<sup>2</sup> The Financial Services Institute (FSI) is an advocacy association comprised of members from the independent financial services industry, and is the only organization advocating solely on behalf of independent financial advisors and independent financial services firms. Since 2004, through advocacy, education and public awareness, FSI has been working to create a healthier regulatory environment for these members so they can provide affordable, objective financial advice to hard-working Main Street Americans.

for ways the Proposal could be improved to provide clarity to FINRA members. FSI supports the non-cash compensation requirements and will not be providing additional comment on those provisions because the majority of FSI members have already adopted compliance programs that exceed the requirements of the non-cash compensation rules.

### **Background on FSI Members**

The independent financial services community has been an important and active part of the lives of American investors for more than 40 years. In the U.S., there are approximately 167,000 independent financial advisors, which account for approximately 64.5% percent of all producing registered representatives.<sup>3</sup> These financial advisors are self-employed independent contractors, rather than employees of Independent Broker-Dealers (IBD).

FSI member firms provide business support to financial advisors in addition to supervising their business practices and arranging for the execution and clearing of customer transactions. Independent financial advisors are small-business owners who typically have strong ties to their communities and know their clients personally. These financial advisors 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. Due to their unique business model, FSI member firms and their affiliated financial advisors are especially well positioned to provide middle-class Americans with the financial advice, products, and services necessary to achieve their investment goals.

### **Discussion**

FSI appreciates the opportunity to comment on the Proposed Amendments to FINRA's gifts, gratuities, non-cash compensation, and business entertainment rules. FSI provides suggestions, outlined in our comments below, to improve the Proposal and provide greater clarity to FINRA members.

#### **I. Firms frequently misapply the gift and gratuities rules so FINRA should consider providing clarification in the Proposed Amendments**

The gifts and gratuities rules state that they are applicable specifically to "any person, principal, proprietor, employee, agent or representative of another person where such payment or gratuity is in relation to the business of the employer of the recipient of the payment or gratuity."<sup>4</sup> Despite this clear definition, many, and perhaps even the majority, of FINRA member firms have interpreted this rule to apply to gifts given by financial advisors to their individual retail clients. Given this common misperception, FSI believes the Proposal regarding gifts and gratuities will benefit from additional clarification.

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<sup>3</sup> The use of the term "financial advisor" or "advisor" in this letter is a reference to an individual who is a registered representative of a broker-dealer, an investment adviser representative of a registered investment adviser firm, or a dual registrant. The use of the term "investment adviser" or "adviser" in this letter is a reference to a firm or individual registered with the SEC or state securities division as an investment adviser.

<sup>4</sup> See Regulatory Notice, Gifts, Gratuities and Non-Cash Compensation Rules August 2016, available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-16-29.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-16-29.pdf)

FSI has observed that firms extend the gifts and gratuities rule requirements to gifts their associated individual financial advisors give to their individual retail clients. We believe firms do so in an overabundance of caution. While this approach results in many firms going above and beyond what is required by the rule, the resources they use to apply the rule requirements to their associated financial advisors could be redirected to other important areas of compliance. Indeed, the very purpose of FINRA's retrospective review is to determine whether the rules meet their objectives while aligning with the economic impacts. In this particular case, FSI believes the rule has created an environment where the misinterpretation and misapplication has resulted in unnecessary economic impact. If FINRA were to clarify for firms that the requirements do not apply to gifts provided to individual retail clients, firms would then be free to re-allocate the resources to other compliance efforts and programs. FSI therefore suggests that FINRA include a clear definition of the application of the rule by explicitly stating in the rule text that it does not apply to gifts given by individual registered financial advisors associated with a FINRA member firm to their individual retail clients.

To further highlight the benefit of clarification of the application of the rule, FINRA stated in the Regulatory Notice that it has fielded a number of questions about the application of these rules since their inception.<sup>5</sup> By clarifying the application of both of these rules, FINRA staff will no longer need to expend resources in responding to the questions, which allows them to spend their time and energy elsewhere. Clarification seems a common sense approach to freeing up both member and FINRA resources.

## **II. FSI requests guidance on the types of transactions subject to the gift and gratuities rules**

FSI believes the Proposal would greatly benefit from additional clarification on the provision of the rule that prohibits, "any member or person associated with a member, directly or indirectly, from giving *anything of value* in excess of \$175 per year to any person where such payment is in relation to the business of the recipient's employer." (emphasis added)<sup>6</sup> FSI is concerned that, "anything of value" is vague and may unintentionally cause confusion for FINRA members. For example, would an advisor's time constitute "anything of value" under these rules, considering how some advisors charge based on an hourly rate? Therefore, we request that FINRA include clarification of whether "anything of value" includes only tangible things which can be purchased with currency or if it also includes items of intangible value or items that may have a current market value or an anticipated market value in the near future, say one year. To the extent FINRA can provide firms examples of what would be considered "anything of value" and examples of things that are not, this would provide additional clarification to FINRA members in complying with the rule.

## **III. FSI applauds FINRA for adopting a principles based approach to the business entertainment rule and encourage FINRA to consider the same approach with gifts and gratuities**

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<sup>5</sup> See Regulatory Notice, Gifts, Gratuities and Non-Cash Compensation December 2014, available at <https://www.finra.org/sites/default/files/p602010.pdf>

<sup>6</sup> See Regulatory Notice, Gifts, Gratuities and Non-Cash Compensation Rules August 2016, available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-16-29.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-16-29.pdf)

FINRA has proposed a limit of \$175 for gifts and gratuities, regardless of geographic area or individual cost of living. FSI instead believes that adopting a principles based approach would better achieve the regulatory goal of protecting investors while still maintaining the flexibility, practicality, and efficiency of the rule.

A principles based approach would allow firms to tailor their compliance to more accurately take into account the economic differences between geographical areas. The Bureau of Economic Analysis has calculated the relative value of the dollar across all fifty states.<sup>7</sup> Prices for the same goods are cheaper in some states and more expensive in others, making the “cost of living” different among geographical locations. For example, in Mississippi, \$100 would purchase goods that would cost \$115.34 at the national average price level. Because \$175 will purchase more in Mississippi than it will in New York, the Proposal’s impact will vary significantly. A principles based approach on the other hand, would provide for efficient application of the rule because the limit could be adjusted to account for differences in purchasing power. If FINRA is concerned that a principles-based approach could still result in potential investor harm, FINRA should consider allowing flexibility in the dollar limit but not to exceed a certain amount, regardless. FSI suggests a \$300 absolute limit would be reasonable. Additionally, FINRA could require firms to include in their books and records the rationale for allowing a gift be given in the value range of \$175 to \$300 and exam to ensure adequate documentation.

#### **IV. FSI applauds FINRA for allowing a de minimis threshold and we encourage FINRA to consider increasing the dollar amount**

FINRA has proposed a \$50 de minimis threshold below which firms would not have to report their gift-giving. This particular provision of the gifts and gratuities portion of the Proposal is aimed at eliminating large, lavish gifts that could causes improper relationships, which is why FINRA determined that gifts of low dollar value need not be recorded. FSI applauds FINRA for adopting a de minimis value below which member firms would not need to expend resources to track gifts. As stated above, given the fact that actual dollar value varies based on geographical location, we suggest the de minimis amount be raised to better reflect market realities.

FINRA is admittedly not concerned with regulating gifts of nominal or inconsequential value that do not present the appearance of impropriety.<sup>8</sup> If the de minimus exception remains at \$50 this will surely result in firms tracking seemingly nominal gifts of \$51 or slightly more. Additionally, gifts the firm or advisor receive will often not have an easily determined value and social convention deters people from asking the value of a gift they receive. Consequently, firms who want to be sure not to run afoul of the rule requirements are likely to record every gift received, particularly during the holiday season. We believe this will negate much of the benefit of the exception. FSI suggests a \$100 de minimis exception would actually eliminate the inclusion of nominal gifts, particularly in urban areas and areas with a lower actual dollar value and would better allow firms and advisors to determine which gifts they receive should be recorded.

Without increasing the de minimis threshold, it will be difficult to determine the value of a gift, as the value of a gift is rarely disclosed, which would force gift recipients to determine on their own whether the value of the gift is more than \$50 and therefore needs to be disclosed. The de

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<sup>7</sup> See Bureau of Economic Analysis, “Real Personal Income for States and Metropolitan Areas, 2014” available at [http://www.bea.gov/newsreleases/regional/rpp/rpp\\_newsrelease.htm](http://www.bea.gov/newsreleases/regional/rpp/rpp_newsrelease.htm)

<sup>8</sup> See Regulatory Notice, Gifts, Gratuities and Non-Cash Compensation Rules August 2016, available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Regulatory-Notice-16-29.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-16-29.pdf)

minimis exception may ultimately become meaningless, because the proposed level is so low that firms will have to assume the value of the gift is more than \$50, and firms would be disclosing all gifts received, which is not the intent of the rule. Raising the limit will make for easier identification of value, because many will find it simpler to determine whether a gift given to them is over or under \$100. Raising the threshold will best serve FINRA's interest in recording gifts of consequential value and make for a more efficient and effective disclosure regime.

### **Conclusion**

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

Thank you for considering FSI's comments. Should you have any questions, please contact me at (202) 803-6061.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "D. T. Bellaire". The signature is fluid and cursive, with a large initial "D" and "T" followed by "Bellaire".

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