Regulatory Notice 25-05

Outside Activities

FINRA Requests Comment on a Proposal to Reduce Unnecessary Burdens and Simplify Requirements Regarding Associated Persons' Outside Activities

Comment Period Expires: May 13, 2025

March 14, 2025

Notice Type

- Request for Comment

Suggested Routing

- Compliance
- Legal
- Operations
- Senior Management
- Systems

Key Topics

- Outside Business Activities
- Private Securities Transactions
- Recordkeeping
- Supervision

Referenced Rules & Notices

- FINRA Rule 3210
- FINRA Rule 3270
- FINRA Rule 3280
- Notice to Members 94-44
- Notice to Members 96-33
- Regulatory Notice 17-20
- Regulatory Notice 18-08

Summary

FINRA seeks comment on a proposed new rule to streamline and reduce unnecessary burdens regarding existing requirements addressing the outside activities of member firms' associated persons, including registered persons (the Proposal). The Proposal is the result of FINRA's retrospective review of FINRA's rules governing outside business activities (OBAs) and private securities transactions (PSTs), FINRA Rule 3270 (Outside Business Activities of Registered Persons) and FINRA Rule 3280 (Private Securities Transactions of an Associated Person), respectively. The Proposal would replace two rules—Rules 3270 and 3280—with one rule and is intended to enhance efficiency without compromising protections for investors and members relating to outside activities.

The proposed rule text is in Attachment A. A flowchart illustrating the proposed rule text is in Attachment B. A series of hypothetical questions and answers indicating how Rules 3270 and 3280 currently apply in comparison to how the Proposal would apply is in Attachment C.

Questions concerning this *Notice* should be directed to:

- James S. Wrona, Vice President and Associate General Counsel, Office of General Counsel (OGC), by email or (202) 728-8270;
- Matthew Vitek, Associate General Counsel, OGC, by email or (240) 386-6490; or
- Patricia Ledesma, Senior Economist, Office of Chief Economist, by email or (202) 728-8461.

Action Requested

FINRA encourages all interested parties to comment. Comments must be received by May 13, 2025.

Comments must be submitted through one of the following methods:

- Online using FINRA's comment form for this *Notice*;
- Emailing comments; or
- Mailing comments in hard copy to:
  Jennifer Piorko Mitchell
  Office of the Corporate Secretary
  FINRA
  1700 K Street, NW
  Washington, DC 20006

To help FINRA process comments more efficiently, persons should use only one method to comment.

Important Notes: All comments received in response to this *Notice* will be made available to the public on the FINRA website. In general, FINRA will post comments as they are received.[1]

Before becoming effective, the proposed rule change must be filed with the Securities and Exchange Commission (SEC or Commission) pursuant to Section 19(b) of the Securities Exchange Act of 1934 (SEA or Exchange Act).[2]

Background & Discussion

Existing Rules

Rule 3270 currently prohibits a *registered person* from being an employee, independent contractor, sole proprietor, officer, director or partner of another person, or being compensated, or having the reasonable expectation of compensation, by another person for any business activity outside the scope of the relationship with his or her member unless he or she has provided prior written notice to the member.

Once notified pursuant to Rule 3270, the member must consider whether the proposed OBA will: (1) interfere with or otherwise compromise the registered person's responsibilities to the member or the member's customers or (2) be viewed by customers or the public as part of the member's business based upon, among other factors, the nature of the proposed activity and the manner in which it will be offered. Based on the member's review of such factors, the member must evaluate the advisability of imposing specific conditions or limitations on a registered person's OBA, including where circumstances warrant, prohibiting the activity.

The member also must assess whether a registered person's activity properly is characterized as an OBA or whether it should be treated as a PST subject to the requirements of Rule 3280. A PST is a securities transaction outside the regular course or scope of an associated person's employment with a member.

Rule 3280 currently provides that, prior to participating in any PST, an *associated person* (which includes both registered and non-registered persons) must provide written notice to the member with which he or she is associated, describing in detail the proposed transaction and the person's proposed role, and indicating whether the associated person has received or may receive selling compensation in connection with the transaction. If the PST does not involve selling compensation, the member must provide prompt written acknowledgement of the notice and may, at its discretion, require the person to adhere to specified conditions in connection with the person's participation in the transaction. If the PST involves selling compensation, the member must inform the associated person in writing whether it approves or disapproves the person's participation in the transaction. If the member approves participation in the PST for selling compensation, the member must record the transaction on its books and records and supervise the associated person's participation as if the transaction were executed on behalf of the member.

Moreover, through a series of *Notices to Members* issued in the 1990s, FINRA applied these PST obligations to outside investment adviser (IA) activities.[3] These *Notices* state that an associated person's outside IA activities constitute "participation in" PSTs if the person did more than simply recommend the securities transaction (*i.e.*, an IA's effecting or placing an order would constitute "participation in" a PST under the *Notices*). In addition, the *Notices* provide that an associated person's receipt of asset-based or performance-based fees when participating in a PST at an outside IA constitutes "selling compensation," meaning that the member would have supervisory and recordkeeping obligations if it approved the activity.

In response to longstanding questions with respect to the OBA and PST rules, in 2017, FINRA announced in *Regulatory Notice 17-20* (May 2017) our initiation of a retrospective review of these rules (Retrospective Review), followed in 2018 by *Regulatory Notice 18-08* (February 2018) that proposed changes to them (Prior Proposal). Among other things, the Prior Proposal would have eliminated members' supervisory and recordkeeping obligations for outside IA activities. FINRA received 52 comment letters, many of which supported the Prior Proposal or certain aspects of it, and with strong differences in views about the Prior Proposal's treatment of outside IA activities. Informed by these comments, FINRA did not move forward with the Prior Proposal at the time.

Streamlined Proposed Rule to Reduce Unnecessary Burdens

The Proposal in this current *Notice* addresses the non-securities business activities and securities transactions that are outside the regular scope of individuals'

employment with a member, but importantly the Proposal narrows the focus to investment-related activities to reduce unnecessary burdens while maintaining the core investor protections of the existing rules. The Proposal also provides clarifications or exclusions for some activities. For ease of reference in this *Notice*, we refer to non-securities business activities outside the regular scope of individuals' employment with a member as "outside activities" and to securities transactions outside the regular scope of individuals' employment with a member as "outside securities transactions."

The Proposal incorporates concepts from the Prior Proposal that were widely considered improvements over the existing rules. However, the Proposal does not alter members' obligations for outside IA activities, unless the activities are performed at an IA affiliated with the member, which are excluded under the Proposal. The Proposal also maintains the dichotomy in existing Rules 3270 and 3280 of applying obligations for outside activities to registered persons and outside securities transactions to associated persons (which includes both registered and non-registered persons). The Proposal's main features are summarized below, and the flow chart in Exhibit B walks through how the Proposal would work in practice.

Investment-Related Activities

The Proposal focuses on outside investment-related activities that may pose a greater risk to the investing public and members. This will both increase investor protection and decrease burdens on members by eliminating the reporting and assessment of low-risk activities that create white noise (*e.g.*, refereeing sports games, driving for a car service, bartending on weekends). This focus will allow members to dedicate resources to activities presenting higher risk, particularly the risk that customers or the public will view the activities as part of the member's business (*e.g.*, selling crypto assets, fixed annuities, commodities or private placements away from the member).

The Proposal defines "investment-related activity" as pertaining to financial assets, including securities, crypto assets, commodities, derivatives (such as futures and swaps), currency, banking, real estate or insurance. The term includes, but is not limited to, acting as or being associated with a broker-dealer (BD), issuer, insurance agent or company, investment company, IA, futures commission merchant, commodity trading advisor, commodity pool operator, municipal advisor, futures sponsor, bank, savings association or credit union. The term also includes personal securities transactions (sometimes referred to as "buying away"),[4] other than transactions in accounts that are known to the member under, or otherwise delineated in, Rule 3210 (*e.g.*, securities held at other members, as well as transactions in certain securities, such as mutual funds, Section 529 plans and variable annuities).[5]

Registered and Associated Persons' Prior Written Notice Obligations

The Proposal maintains existing requirements regarding prior written notice. As is required today, under the Proposal, a registered person who intends to participate in an outside activity and an associated person (including a registered person) who intends to participate in an outside securities transaction must provide prior written notice to the member. The written notice must describe in detail the proposed activity or transaction, the person's proposed role therein and whether the person will receive selling compensation.[6]

As is true under the current rules, the notice requirements are different depending on whether the notice is of an outside activity, an outside securities transaction not for selling compensation, or an outside securities transaction for selling compensation. A single notice is used for an outside activity, while a separate notice is required for each outside securities transaction unless an exception applies that allows the use of a single notice (*e.g.*, a series of related securities transactions not involving selling compensation).[7]

Members' Responsibilities Upon Receiving Notice

Upon receiving written notice of a registered person's outside activity or an associated person's outside securities transaction, the member must assess whether it:

- Is properly characterized.
  - A person submitting a notice of an activity may, mistakenly or intentionally, mischaracterize it (*i.e.*, submitting a notice of an outside activity when it is an outside securities transaction or an outside securities transaction for selling compensation).
  - Under this provision, a member must analyze whether the activity is properly characterized to determine its obligations, which will vary depending on the proper designation of the proposed activity, as discussed below.
- Involves the member's customer(s).
- Will interfere with or otherwise compromise the person's responsibilities to the member or the member's customers.
- Will be viewed by the member's customers or the public as part of the member's business based upon, among other factors, the nature of the proposed activity and the manner in which it will be offered.

These assessment factors are consistent with the existing requirements under Rule 3270 for an OBA, with the minor addition that the member must consider whether the activity or transaction involves the member's customer(s). While Rule 3280 does not include these explicit assessment factors when considering a PST, we understand that many members perform a similar analysis today.

A member's obligations after conducting an assessment are the same under the Proposal as they are under existing rules. As with the existing rules, the member would have differing obligations depending on the activity.

- For a registered person's outside activity, the member must consider imposing specific conditions or limitations on the outside activity, including where circumstances warrant, prohibiting the activity, but there is no acknowledgement or approval requirement.
- For an associated person's outside securities transaction not for selling compensation, the member must provide the associated person prompt written acknowledgement of such notice and may, at the member's discretion, require the associated person to adhere to specified conditions in connection with the associated person's participation in the transaction, but there is no approval requirement.
- For an associated person's outside securities transaction for selling compensation, the member must make a reasonable determination of whether to approve, approve subject to specific conditions or limitations, or disapprove each proposed securities transaction and must notify the associated person in writing of such determination.

Exclusions

The Proposal contains several exclusions from the rule's coverage.

- First, the Proposal excludes an associated person's (including a registered person's) non-BD activity on behalf of a member or its affiliate (*e.g.*, IA activity at a dually registered firm and IA, insurance or banking activity conducted at an affiliate). Activity performed on behalf of a dually registered firm is not considered activity performed away from the member. The exclusion for activity conducted at an affiliate recognizes members' ability to implement meaningful controls across business lines.
- Second, the Proposal excludes outside securities transactions among immediate family members for which there is no selling compensation. This exclusion is consistent with Rule 3280.

- Third, the Proposal excludes outside securities transactions subject to Rule 3210 (*e.g.*, securities in an account held at another member) and transactions delineated in Rule 3210.03 (*e.g.*, mutual funds, Section 529 plans, variable annuities). This exclusion is consistent with Rule 3280.
- Fourth, the Proposal excludes personal investments in non-securities and the purchase, sale, rental or lease of a main home or dwelling unit or personal-use rental property, as defined for purposes of the Internal Revenue Code. These exclusions recognize the lower risks to customers and members associated with these activities and the inefficiency of members' having to expend significant resources reviewing them.

Clarifications

The Proposal clarifies members' obligations in several areas. For instance, an issue that has arisen is whether and to what extent Rules 3270 and 3280 apply to portfolio managers and investment committee members. The Proposal clarifies that an associated person would need to provide prior written notice and receive prior written approval for such activity. However, if the member approves the activity, it would not be required to supervise and maintain records for an associated person who is acting as a portfolio manager or investment committee member for registered investment companies, unregistered investment companies, business development companies, real estate investment trusts and entities that are recognized as tax exempt, unless the associated person is selling such entities' shares for selling compensation.

The Proposal also makes clear that, if an individual is associated with more than one member and is engaged in an outside securities transaction for selling compensation, the members may develop a written allocation agreement regarding regulatory obligations.

Outside IA Activity

As highlighted above, through a series of *Notices to Members* issued in the 1990s, FINRA applies PST requirements to outside IA activities.[8] This guidance would remain in effect under the Proposal. As such, an associated person's IA activities constitute "participation in" PSTs if the person did more than simply recommend the securities transaction (*i.e.*, an IA's effecting or placing an order would constitute "participation in" a PST under the *Notices*). In addition, the *Notices* provide that an associated person's receipt of asset-based or performance-based fees when participating in a PST at an outside IA constitutes "selling compensation," meaning that the member would have supervisory and recordkeeping obligations if it approved the activity.

Commenters responding to the Retrospective Review and the Prior Proposal had opposing views on whether FINRA members should be responsible for supervising and recordkeeping outside IA activity, including activity performed at unaffiliated IAs. While many commenters strongly supported eliminating or substantially modifying the requirements for outside IA activities, concerns were also raised that doing so could pose risks to investors.

Although the Proposal maintains the status quo regarding members' responsibilities for outside IA activity, FINRA is interested in updating the prior feedback we received and learning of current experiences and views with respect to outside IA activity. To better understand the complexity of the issues and interested persons' positions, this *Notice* provides a discussion below, following the economic impact assessment, of the comments we previously received on that topic.

Economic Impact Assessment

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the potential economic impacts, including anticipated costs, benefits, and distributional and competitive effects, relative to the current baseline, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives. FINRA invites comments on all aspects of this assessment and requests that commenters provide empirical data or other factual support wherever possible.

Economic Baseline

The economic baseline is current Rules 3270 and 3280, in addition to related guidance and current practices. As discussed above, Rule 3270 applies to registered persons while Rule 3280 applies to associated persons, whether registered or not. All such individuals and members are subject to these rules, irrespective of business model, client base and product type. These rules set the minimum standards for reporting outside activities to members, but members may apply stricter criteria and prohibit or limit particular activities.

The number of individuals subject to both rules (*i.e.*, the number of approved FINRA-registered persons) is 633,933, registered with 3,279 members. In addition, non-registered associated persons are subject to Rule 3280 but not Rule 3270. While FINRA does not know the exact number of non-registered associated persons, we estimate that there are approximately 500,000 such persons, composed of, among others, non-registered fingerprinted individuals (NRFs) and non-registered owners and officers.[9]

In 2017, FINRA conducted a retrospective review of Rules 3270 and 3280 that included a survey of members.[10] Approximately 80 percent of the members that

responded to the 2017 survey stated that they have received at least one written notice in the last five years pursuant to Rule 3270. Approximately 40 percent of the registered persons of those members provided written notices. Based on Form U4 information, nearly 50 percent of currently registered persons report one or more other businesses (outside their relationship with the member), covering almost 98 percent of members. Registered persons reported a broad range of non-investment-related activities.[11]

Rule 3280 requires associated persons to provide prior written notice before participating in any manner in PSTs. In the 2017 survey, approximately 40 percent of the responding members stated that they had received at least one written notice in the prior five years pursuant to Rule 3280. Approximately 19 percent of the associated persons within those members provided written notices.

Economic Impacts

Relative to the baseline, the proposed rule retains the same broad obligations of associated persons and members with respect to outside activities, but it narrows the range of outside activities that are reportable.

As discussed above, Rule 3270 applies to registered persons and Rule 3280 applies to associated persons. The Proposal preserves this distinct treatment but limits the Proposal's scope to outside activities that are investment related.[12] Activities that are not investment related are common and varied (*e.g.*, refereeing sports games, driving for a car service, bartending on weekends). Removing reporting requirements for such activities would relieve both registered persons and members from costs associated with this reporting and its review. Members may also benefit from focusing the freed compliance resources on those outside activities that are more likely to raise investor protection concerns. There is likely little risk that non-investment-related activities could be perceived by the investing public as part of the member's business.

Under both the Proposal and currently for investment-related outside activities, registered persons must provide their firms with prior written notice of the proposed activity and members must review the proposed activity using specified criteria. The Proposal standardizes the assessment that members must conduct, upon receiving notice, of registered persons' outside activities and associated persons' outside securities transactions, borrowing from the approach used in Rule 3270 with a minor addition—the consideration of whether the activity involved the member's customers.

Relative to the baseline, the Proposal provides clearer and more consistent standards for reviewing both outside activities and outside securities transactions.

We understand that many members already impose these or equivalent requirements. To the extent that members are applying similar or higher standards today, there would be no material impact. For members with lower or less consistent standards, this change will lead to more consistent review and perhaps additional restrictions on outside activities. For the associated persons in firms that currently follow lower or less consistent standards, there would be a cost in terms of business opportunities delayed, limited or prohibited by the member. Investors that interact with these associated persons may face increased search costs for those goods or services as a result.

For outside securities transactions, reportable by associated persons (including registered persons), the Proposal imposes requirements that largely parallel those for current Rule 3280 for PSTs. Relative to the baseline, the Proposal includes assessment criteria for outside securities transactions and excludes activity on behalf of a member and its affiliates, including IA activities, insurance and banking. About 26 percent of members have one or more registered persons working in an affiliated registered IA.[13] The vast majority of member affiliates are under common control;[14] thus, these affiliates may share compliance resources and systems. One potential risk of this approach is that customers could be harmed if supervision by an affiliate is less effective than supervision by the member.[15]

For associated persons employed by more than one member, the Proposal codifies previous guidance offering the option of formal allocation agreements for outside securities transactions for selling compensation between the members such that at least one of the members agrees to oversee the outside securities transactions. This feature allows for some efficiency gains for members that may have been unaware of such previous guidance. About 1.6 percent of all registered persons work for more than one member, impacting 63.2 percent of members.[16] If the registered person is associated with multiple affiliated members, it could facilitate agreements. The proportion of NRFs associated with more than one member is higher, at 4 percent, although the proportion of impacted members is lower (25 percent).[17]

Both members and IAs compete for individuals with similar skill sets. The current rules and the Proposal impose a regulatory burden for members that is not matched by equivalent requirements in the IA industry. Relative to the baseline, the focus on investment-related activities in the Proposal reduces, but does not eliminate, this regulatory burden. The competitive impacts of the Proposal on members and their associated persons depend on the business model of the member (for example, whether IA activities are conducted within a dually registered member or its affiliates) and the policies that the member adopts regarding outside activities. To the extent that associated persons may seek employment with members based on their policies regarding outside activities, some members may face pressure to use a light touch in their assessment of outside activities and the associated determinations. The different treatment of outside activities for non-registered

associated persons versus registered persons can create, on the margin, incentives for some non-registered associated persons to remain unregistered. Under the Proposal, the exclusion of outside activities that are not investment related may reduce or eliminate that incentive to remain unregistered for some individuals.

In summary, the Proposal could increase the efficiency and effectiveness of member compliance resources by clarifying the obligations of a member and associated persons, focusing attention on the activities more likely to lead to investor harm, and standardizing the assessment that members must conduct, upon receiving notice, of registered persons' outside activities or associated persons' outside securities transactions.[18] Such changes may potentially benefit customers through better investor protection, but may also have some effect on the investment-related opportunities offered to them. The reduction in regulatory costs may also have a positive competitive impact relative to segments of the securities industry that lack equivalent requirements for outside activities.

Alternatives Considered

In developing rule proposals, FINRA recognizes that their design and implementation may impose direct and indirect costs on different market participants, including members, associated persons, regulators, investors and the public. Among the alternatives considered:

- A principles-based approach in lieu of the prescriptive approach set forth in the Proposal, which would provide members with more flexibility in developing the systems and the protocols to assess and approve or disapprove OBAs and PSTs. However, we preliminarily believe that the approach presented here better balances the costs and benefits of governing outside investment-related activities while providing regulatory effectiveness, clarity and consistency.
- Applying outside activities requirements to all associated persons (rather than using the existing bifurcated approach of applying PST requirements to associated persons and OBA requirements to registered persons) or adding a requirement for prior written approval for all outside activities. Either one of these changes would have further streamlined the application of the rule, but potentially would increase regulatory costs for associated persons and members, in particular smaller firms.
- A broader scope for the activities covered by the Proposal, to include outside financial services activities beyond investment-related activity, such as acting as an accountant, treasurer or comptroller. The current definition of "investment-related activity" focuses on outside activities that are most likely to lead to investor confusion, conflicts of interest for the registered person and potential investor harm.

- Excluding unaffiliated outside IA activity. About 11 percent of members have one or more registered persons associated with an unaffiliated registered IA.[19] While IA activity is overseen by other regulators, several commenters to the Retrospective Review and the Prior Proposal stressed the investor protection loss that would result from this exclusion, though other commenters strongly disagreed.
- A focus on transaction-based compensation instead of any selling compensation. The former concept can lead to tailoring the compensation arrangement to skirt the rule. "Selling compensation" in FINRA guidance has been interpreted to include asset-based compensation, thereby covering IA activity.

Discussion of Retrospective Review and Prior Proposal Comments Regarding Outside IA Activities

The Prior Proposal would have eliminated the current FINRA member supervisory and recordkeeping obligations for IA activities performed by associated persons at an unaffiliated IA. We indicated in the Prior Proposal that imposing such obligations "has caused significant confusion and practical challenges, including, for example, privacy challenges with a member obtaining account information for customers of an unaffiliated IA through which a member's registered person may be acting in an IA capacity."[20] We also recognized "that these activities are subject to another regulatory regime" and that commenters to the Retrospective Review had "argued that the current approach imposes unnecessary burdens without providing meaningful investor protections over the activities."[21] This aspect of the Retrospective Review and the Prior Proposal generated the most significant comments.

It is important to emphasize at the outset of this discussion that FINRA regulates BDs, while the SEC and the states regulate IAs. BDs and IAs also are subject to different laws and rules. Moreover, while they at times engage in similar activities, BDs and IAs also provide distinct services and advice and employ different fee structures.

While a majority of commenters supported the elimination of the supervisory and recordkeeping requirements for FINRA members regarding IA activities performed by associated persons away from, and often without any affiliation with, the member, other commenters voiced concern over the risks to investors of removing such requirements. Although we are not presently proposing the elimination of BDs' obligations regarding outside IA activities, FINRA is highlighting the points raised on this aspect of the Retrospective Review and the Prior Proposal to foster dialog with interested persons that will help FINRA better understand their positions, the impact of the issues on investors and members, and whether commenters' previous positions have changed due to more recent regulatory, industry and investor practices.

Commenters in Favor of Maintaining FINRA Member Supervision and Recordkeeping for Outside IA Activities

Those commenters in favor of maintaining BD oversight of IA activities performed by associated persons away from the FINRA member expressed several concerns with eliminating such oversight. The primary concern that many of these commenters voiced was that the level of regulatory oversight of IA activities is not as rigorous as oversight of FINRA members' activities. These commenters claimed that the lack of meaningful oversight of IA activities could lead to IA client harm if FINRA members did not oversee some aspects of IA activities performed by associated persons at third-party IAs unaffiliated with a member.

For instance, one commenter asserted that "the SEC has made clear that it is ill-equipped to routinely examine the many investment advisers it regulates. Similarly, due to limitations on many State regulatory resources and budgets, States also substantially lack sufficient resources to examine State-registered investment advisers with any reasonable regularity, if at all."[22] Another commenter claimed that "eliminating FINRA firms' responsibilities in this area would place investors at risk by eliminating day-to-day oversight in favor of . . . intermittent state and federal securities regulators oversight to identify or prevent misconduct."[23]

Another concern that was raised is that many IA firms lack the resources and ability to properly supervise their own IA activities. For instance, one commenter asserted, "Often these investment advisers do not have the resources to develop and maintain comprehensive and independent supervisory, risk, and oversight control systems that [FINRA] member firms are required to have in place."[24]

An association of BDs opined that, where the outside IA activities involves the BD's customers, the BD should take a "holistic view towards investor protection in respect of these clients."[25] According to this association, its members had "reported that they will continue to supervise their advisors' investment-related OBAs (particularly, outside investment advisory activities), despite the proposed rule changes" because "doing so is in the best interest of the clients they serve."[26]

Commenters in Favor of Eliminating FINRA Member Supervision and Recordkeeping for Outside IA Activities

As noted, a majority of commenters favored FINRA's proposal to eliminate the requirement for FINRA member oversight of IA activities performed by associated persons away from FINRA members. Those commenters generally believed that the current requirements impose an unfair burden on FINRA members that often have no connection with the unaffiliated outside IAs beyond their associated persons' separate involvement with such IAs. In addition, commenters noted that IA

activities are subject to a fiduciary obligation and are regulated by the states and the SEC. Commenters also raised issues regarding privacy concerns and the different regulatory requirements, services and types of advice on the IA side with which FINRA members may be unfamiliar.

A common refrain was that IAs are regulated by the SEC, not FINRA, and that FINRA member oversight of outside IA activities is therefore redundant and creates unnecessary compliance costs and burdens without corresponding benefit to the investing public.[27] Some commenters questioned arguments favoring BD oversight of outside IA activities based on investor-protection concerns, given that IAs are subject to a fiduciary standard, and other requirements established by the SEC.[28]

Some commenters also asserted that BDs may be ill-equipped to supervise outside IA activities as they may not be familiar with the outside IA's services, advice and obligations. For example, one commenter stated that "both affiliated and, particularly, unaffiliated IAs often engage in products and strategies that are not supported by the [BD]. Accordingly, to properly supervise such activities, [BDs] need to develop expertise in such products and strategies, which is simply not feasible for small firms, nor would it be a good use of their supervisory resources."[29]

In addition, numerous commenters described the difficulty of obtaining information about an outside IA's clients necessary to supervise the outside IA activities. These commenters stated that IAs often raise privacy and proprietary concerns over providing IA client information to a BD, particularly one that is unaffiliated. A commenter explained, "IAs have their own privacy obligations to their clients and may not be able to share information regarding their clients with unaffiliated member firms even if they are inclined to do so."[30] Commenters also raised the risk to the BD of having to handle private, personal information for unaffiliated IA clients, with one explaining that "the current approach creates privacy challenges for [BDs] with respect to the handling of the personal information of unaffiliated advisory firms."[31]

Moreover, commenters asserted that requiring BDs to oversee outside IA activities could lead to customer confusion regarding which entity is responsible for the IA activities. One commenter explained that requiring a BD to supervise outside IA activities "may potentially lead to customer confusion as to the entity responsible for the transaction and the appropriate regulatory and/or legal standards applicable to the services provided."[32]

Several commenters also opined that BDs may have a business reason for preferring to oversee the outside IA activities of their associated persons. One commenter supporting the proposal to eliminate this obligation stated that "it will reduce costs for investors. Currently, an [IA] will be forced to pay an average of 5 percent to 8 percent of its gross advisory fees to a [BD] for oversight…These costs are usually passed on to the client."[33]

Request for Comment

FINRA requests comment on all aspects of the Proposal. FINRA requests that commenters provide empirical data or other factual support for their comments wherever possible. FINRA specifically requests comment concerning the following questions.

- What are the alternative approaches, other than the Proposal, that FINRA should consider?
- How would consolidation of the rules governing OBAs and PSTs in the Proposal simplify compliance? What impact would it have on the cost of compliance?
- As is true today under existing rules, the Proposal would apply to registered persons for outside activities and to associated persons for outside securities transactions. Should the Proposal be expanded to apply to all associated persons? If so, why?
- Is the proposed scope of the notice requirement appropriately tailored to balance the interest of members to receive information regarding their registered persons' outside activities and any investor protection concerns?
- As is true today under existing rules, the Proposal would require prior written approval for outside securities transactions for selling compensation and an acknowledgement for outside securities transactions not for selling compensation. Should the Proposal be expanded to require approval for all outside investment-related activity? If not, should the Proposal's acknowledgment for outside securities transactions not for selling compensation be modified? If so, how and why?
- Is the definition of "investment-related activity" appropriate given the regulatory objectives of the Proposal, or should other activities be included in or excluded from the definition? If so, why?
- The Proposal has several exclusions, including for registered persons' personal investments in non-securities and activities conducted on behalf of an affiliate of a member. Are the proposed exclusions appropriate?
- The Proposal does not alter members' obligations for outside IA activities. What are the challenges members face regarding supervising and recordkeeping outside IA activities for selling compensation? Would the removal of the requirement for FINRA member oversight of outside IA activities by their associated persons impact investor protection considering that IAs are regulated by either the SEC or the states? What are the benefits of BD supervision and recordkeeping of outside IA activities for selling compensation?
- When a person is associated with more than one member, the Proposal allows members to develop a formal allocation arrangement whereby at

least one member has the regulatory responsibility, including the supervision and recordkeeping of a proposed outside securities transaction for selling compensation. Are there any competitive effects of such allocation arrangements? Does this flexibility potentially create a disadvantage for some firms regarding how the costs are allocated? Should FINRA consider any other approaches?

- Are there any material economic impacts, including costs and benefits, to investors, issuers and members that are associated specifically with the Proposal? If so:
  - What are these economic impacts and what are their primary sources?
  - To what extent would these economic impacts differ by business attributes, such as size of firm or differences in business models?
  - What would be the magnitude of these impacts, including costs and benefits?
- Are there any expected economic impacts associated with the Proposal not discussed in this *Notice*? What are they and what are the estimates of those impacts?

Endnotes

1 Parties should submit in their comments only personally identifiable information, such as phone numbers and addresses, that they wish to make available publicly. FINRA, however, reserves the right to redact, remove or decline to post comments that are inappropriate for publication, such as vulgar, abusive or potentially fraudulent comment letters. FINRA also reserves the right to redact or edit personally identifiable information from comment submissions.

2 *See* SEA Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the Federal Register. Certain limited types of proposed rule changes take effect upon filing with the SEC. *See* SEA Section 19(b)(3) and SEA Rule 19b-4.

3 *See* Notice to Members 94-44 (May 1994); Notice to Members 96-33 (May 1996).

4 When an individual makes a personal securities investment away from the employing member, and the transaction is not otherwise covered by Rule 3210, the securities transaction is considered "buying away," which is subject to Rule 3280. *See, e.g., Jay Frederick Keeton*, 50 S.E.C. 1128, 1129-30 (1992) (finding a violation of FINRA Rule 3280's predecessor rule where respondent made undisclosed and unapproved purchases in three partnerships); *Dep't of Enforcement v. Friedman*, Complaint No. 2005000835801, 2010 FINRA Discip. LEXIS 10, at *19 (FINRA NAC July 26, 2010), *aff'd*, Exchange Act Release No. 64486, 2011 SEC LEXIS 1699 (May 13, 2011) (explaining that "[Rule 3280] applies to both purchases and sales of securities"); *see also* NASD *Notice to Members 75-34* (April 1975) (stating that the rule concerning private securities applies to all securities transactions by an associated person "whether on behalf of themselves or on behalf of customers and others"). The most common "buying away" transactions are personal investments in private placements.

5 FINRA Rule 3210 requires that an associated person must obtain the prior written consent of his or her employer when opening an account, as specified by the rule, at another member or other financial institution. The other member must, upon written request by the employer member, transmit duplicate copies of confirmation and statements, or the transactional data, with respect to an account subject to Rule 3210. The requirements of Rule 3210 do not apply to transactions in unit investment trusts, municipal fund securities, Section 529 plans and variable contracts or redeemable securities of companies registered under the Investment Company Act or to accounts that are limited to transactions in such securities, or to Monthly Investment Plan type accounts.

6 This language comes from Rule 3280 and was favored for, among other reasons, consistency purposes over the language in Rule 3270—the notice must be "in such form as specified by the member."

7 Under Rule 3270, a registered person may use a single notice for the proposed outside activity. Rule 3280 requires an associated person to provide prior written notice to the member for each proposed securities transaction, unless an exception applies. *See In re Klaus Langheinrich*, Exchange Act Release No. 34107, 1994 SEC LEXIS 3623, at *6 (May 25, 1994) (explaining that Rule 3280 "requires that an associated person must give *specific prior notice of each transaction* if the associated person will receive selling compensation. A single notice will suffice only in the case of a series of related transactions in which no selling compensation has been or

will be received"). In addition, a single notice and approval of IA services for asset-based or performance-based fee is permitted. *See Notice to Members 96-33* (May 1996) ("The Board of Governors … has interpreted [Rule 3280] to require prior notice of the investment advisory services that will be provided by the RR/IA for an asset-based or performance-based fee, rather than prior notice of each trade effected by an RR/IA for a particular customer…. Members are reminded, however, that if an RR/IA receives transaction-based compensation, a member's prior approval of each trade is required.").

8 *See supra* note 3.

9 Figures as of mid-February 2025. This figure could be both overinclusive and underinclusive. For instance, the number of NRFs may overestimate the number of non-registered associated persons as FINRA rules do not require reporting the termination of an NRF's association with a member. Conversely, there may be other non-registered associated persons who are neither fingerprinted nor listed on Form BD who may not be captured in this figure (*e.g.*, certain individuals in compliance and legal departments, certain individuals who perform back-office functions).

10 Further discussion of comment letters received as part of the retrospective review follows below.

11 Question 13 ("Other Business") in Form U4 requires providing various details about outside activities, including whether it is an investment-related activity. While the question does not perfectly align with the activities reportable under Rule 3270, answers may be indicative of the prevalence and range of outside activities. However, the information provided is not structured, and it is difficult to assess the share of reported outside activity that is investment related. The Proposal does not impact reporting on Form U4.

12 In addition to limiting the scope to investment-related activities, the Proposal provides several exclusions, discussed above.

13 Based on information from Form U4, question 6 ("Will *applicant* maintain registration with *firm(s)* under common ownership and control with the *filing firm*?").

14 Based on information from Form BD, Schedule D.

15 Most non-broker-dealer activity of affiliates is overseen by other regulatory entities.

16 Registered persons that work for multiple members tend to hold operations professional (series 99) and financial and operations principal (series 27) registrations, particularly among those that are registered with more than five members.

17 These percentages might overestimate the actual proportion. *See supra* note 9.

18 A number of members responding to the Retrospective Review and the Prior Proposal commented that Rule 3270 was overinclusive to the point of being burdensome and that it took the focus off of activities that were more relevant from a risk perspective.

19 Based on information from Form U4, question 3.B. ("Will *applicant* maintain registration with an investment adviser that is not *affiliated* with the *filing firm*?"), figure as of September 2024.

20 *See Regulatory Notice 18-08* (February 2018).

21 *Id.*

22 *See* letter from Paul J. Tolley, senior vice president and chief compliance officer of

Commonwealth Financial Network, dated April 27, 2018.

23 *See* letter from Joseph P. Borg, president of North American Securities Administrators Association (NASAA), dated April 27, 2018. *See also* letters from Seth Miller, general counsel, senior vice president and chief risk officer, Cambridge Investment Research, dated April 27, 2018 ("Presently, regulatory oversight of investment advisory activity does not appear to be as robust and recurrent as in the broker-dealer space, which could create the potential for investor harm if activities and transactions member firms have been supervising are no longer being monitored and supervised."); Andrew Stoltmann, president of the Public Investors Arbitration Bar Association (PIABA), dated April 27, 2018 (asserting that its "members have seen, all too often, registered representatives establishing small IA firms and using outside business activities in order to avoid member supervision, in order to engage in activities that harm investors"); David T. Bellaire, executive vice president and general counsel, Financial Services Institute, dated April 27, 2018 (FSI Letter) (stating that the proposed rule raises investor protection concerns).

24 *See* letter from Robert J. McCarthy, director of Regulatory Policy, Wells Fargo Advisors, dated April 27, 2018.

25 *See* FSI Letter, *supra* note 23.

26 *Id.*

27 *See, e.g.*, letters from Paige W. Pierce, dated April 24, 2018; Ken Norensberg, dated April 26, 2018; Michelle Oroschakoff, managing director, chief legal officer, LPL Financial LLC, dated April 27, 2018; Heath Goldstein, chief compliance officer, 1st Financial Investment, Inc., dated April 2, 2018.

28 *See, e.g.*, letters from John M. Simon, president, Pacific Capital Associates, dated April 18, 2018; Kevin Zambrowicz, managing director and associate general counsel, Securities Industry and Financial Markets Association (SIFMA), dated June 29, 2017 (SIFMA Comment Letter) ("Under Rule 206(4)-7, each IA that is registered or required to be registered under the Advisers Act must establish an internal compliance program that addresses the IA's performance of its fiduciary and substantive obligations under the Investment Advisers Act of 1940. . . .").

29 *See* letter from Lisa D. Crossley, executive director, National Society of Compliance Professionals (NSCP), dated April 27, 2018 (NSCP Comment Letter).

30 *Id. See also* letters from Neal E. Nakagiri, president, CEO, CCO, NPB Financial Group, dated April 27, 2018; Myra P. Nicholson, general counsel, International Assets Advisory (IAA), dated June 22, 2017; Stephen Kohn, CEO/president, Stephen A. Kohn & Associates, dated April 3, 2018.

31 Letter from John Peter Purcell, CEO, Purshe Kaplan Sterling Investments, dated April 25, 2018.

32 NSCP Comment Letter, *supra* note 29. *See also* SIFMA Comment Letter, *supra* note 28.

33 *See* letter from Amber Eduvigen, dated May 15, 2018. *See also* letters from Dale A. Pope, president and CEO, MerCap Securities, LLC, MerCap Advisors, Inc., dated August 8, 2024 ("Many BDs don't want to give this oversight up because it is a big revenue generator. These firms charge a supervision fee as high as 5% of the fee income."); Peter T. Palion, president, Master Plan Advisory, Inc., dated April 26, 2018.