

## VIA ELECTRONIC MAIL

May 19, 2016

Robert W. Errett  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: **Regulatory Notice 16-14: Changing National Adjudicatory Council Composition, Member Terms, and Election Procedures**

Dear Mr. Errett:

On April 28, 2016, the Financial Industry Regulatory Authority (FINRA) published its request for public comment on proposed amendments to the National Adjudicatory Council's (NAC) composition, member terms, and election procedures (Proposed Amendments).<sup>1</sup> The Proposed Amendments are in response to recent changes made to the composition of FINRA's Board of Governors, requiring the number of non-industry governors to outnumber the industry governors. FINRA's stated goal of the Proposed Amendments is to better align the NAC's composition with that of the Board of Governors.

The Financial Services Institute<sup>2</sup> (FSI) appreciates the opportunity to comment on this important proposal. FSI commends FINRA for suggesting changes to the NAC but has some concerns about both the shifting of the council's composition and extending member terms. We elaborate on our viewpoints in our comments below.

### **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. 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

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<sup>1</sup> Regulatory Notice 16-14, Changing National Adjudicatory Council Composition, Member Terms, and Election Procedures (Apr. 28, 2016).

<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.

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**

The NAC serves an important and crucial role in the disciplinary process by presiding over disciplinary matters that are either appealed directly to the NAC or are called for review by NAC members. Additionally the NAC helps determine statutory disqualifications, oversees membership proceedings, considers the appeals of members seeking exemptive relief, and retains the authority to review decisions proposed in other proceedings. Usually two NAC members are charged with responsibility for each disciplinary matter. They provide guidelines and edits for FINRA decisions. Draft decisions are then presented to the entire council through periodic meetings, where all NAC members provide their perspective, make edits, and vote on final decisions. These important responsibilities require all NAC members to have a sophisticated understanding of the industry and its various intricacies.

In 2007 FINRA, amended its By-Laws, changing the composition of its Board of Governors to require that non-industry members outnumber industry members.<sup>3</sup> The Proposed Amendments are intended to better align the composition of the NAC with the changes made to FINRA's Board. While FSI understands and appreciates FINRA trying to unify the composition of various board, council, and committee compositions, FSI has some reservations about the Proposed Amendments.

#### **I. FSI requests clarification of the benefits of the proposed change.**

FSI understands that FINRA is trying to better align the composition of the NAC with the composition of FINRA's Board of Governors. However, it is unclear from the proposal whether the current composition of the NAC has resulted in issues that would be remedied by altering its composition. The proposal states that adding more non-industry members helps to emphasize the "importance of the unique, balanced perspectives that are valued in NAC deliberations and aid in its ability to address issues in a neutral fashion."<sup>4</sup> FSI believes that keeping the composition equal between industry and non-industry members, better attains a more balanced perspective. An alteration of that balance does not appear to create any additional neutrality.

Many of the issues that come before the NAC are nuanced, requiring the input of an individual with extensive industry knowledge and experience in order to effectively assess the issue at hand. FSI is concerned that increasing the number of non-industry members may result in

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<sup>3</sup> Industry members are anyone "who: (1) is or has served in the prior year as an officer, director (other than as an independent director), employee or controlling person of a broker or dealer, or (2) has a consulting or employment relationship with or provides professional services to a self-regulatory organization registered under the Act, or has had any such relationship or provided any such services at any time within the prior year." *FINRA Article I Definitions*, available at [http://finra.complinet.com/en/display/display\\_main.html?rbid=2403&element\\_id=4599](http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4599). Non-Industry members are individuals "who otherwise has no material business relationship with a broker or dealer or a self-regulatory organization registered." *Id.*

<sup>4</sup> Regulatory Notice 16-14, Changing National Adjudicatory Council Composition, Member Terms, and Election Procedures, 13 (Apr. 28, 2016).

diminishing this important expertise on the council. FSI therefore asserts that the composition of the NAC is currently effective and maintains the neutrality sought after through the proposed change.

**II. FSI supports the change to member term length but requests that this proposal be reviewed after its implementation.**

In addition to altering the composition of the council, the proposal also increases NAC members' terms from three years to four years. FSI understands the benefits of extending term lengths. It takes NAC members time to become familiar with the financial industry, the workings of FINRA and its members, and their role on the NAC. An extended term of four years will allow NAC members to spend more time serving after they become well-versed in the industry and their duties as they relate to the industry.

Despite this benefit, FSI believes the current term of three years allows for a rolling board which ensures that a variety of views and individuals are able to serve and provide valuable input. Extending the term to four years may result in an insufficient varied viewpoint over time. While it seems that extending terms would allow for "greater utilization of the unique skills and expertise of each member," the reality is that it could unintentionally create stagnation among the NAC. In other words, the cohesion FINRA hopes to gain could actually result in monotony and lack of interest. Because the NAC is ideally "composed of members with a diversity of expertise, experiences and perspectives that fosters making fair decisions and, where necessary, imposing appropriately remedial sanctions,"<sup>5</sup> we believe that FINRA should amend its proposal to include a provision dictating when FINRA should reevaluate the effectiveness of the proposed longer four year term. Ideally, FINRA could reevaluate the effectiveness after three tranches of members serve for four years. FSI believes that this will provide sufficient time to conduct an evaluation and ensure that the stated goals of this proposal are being achieved.

**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" and a stylized "Bellaire".

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

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<sup>5</sup> *Id.* at 12.