



39 Broadway, Suite 3300, New York, New York 10006-3019

Via email: pubcom@finra.org

May 14, 2015

RE: Regulatory Notice 15-10: Comments on the Effectiveness and Efficiency of FINRA Membership Application Rules

Integrated Management Solutions USA LLC (“IMS”) is pleased to comment on Regulatory Notice 15-10 (“RN 15-10”) seeking comment on the Effectiveness and Efficiency of FINRA Membership Application Rules (“MAP Rules”)¹. RN 15-10 is part of FINRA’s general retrospective rule review process and is specifically intended to elicit users’ experience with these specific rules. It comes on the heels of FINRA’s proposal to improve the membership application process (RN 13-29; RN 10-01).

IMS is one of the largest providers of financial accounting and compliance consulting services to the financial services industry, providing such services to about 100 FINRA members, among others types of financial services firms.² We counsel clients daily on the scope of permissible broker-dealer activities under various FINRA and SEC rules. At any one time, we have several NMAs, CMAs or Materiality Consultations (“MatCons”) pending before FINRA on behalf of clients under the MAP Rules. In addition, we are constantly involved with the panoply

¹ The MAP Rules encompass New Member Applications (“NMAs”), Continuing Member Applications (“CMAs”) and Materiality Consultations (“MatCons”).

² The statements in this comment letter incorporate the views of IMS, not those of our clients.

of other FINRA rules, SEC Rules, etc. as they apply to FINRA members on a regular basis. We believe that our regular, daily experience with FINRA's MAP Rules and how they are applied by FINRA itself, as well as the other rules affecting FINRA members every day, enables us to assess whether the MAP Rules are meeting their intended goals as well their impact on FINRA members from both a regulatory and business perspective. Many of our comments apply to all three types of reviews under the MAP Rules.

Overall Concern

We are pleased to note that FINRA is now seeking input from stakeholders in the membership process as well as seeking comment on the existence of “duplicative, inconsistent or ineffective regulatory obligations.” In that spirit, we are submitting these comments in the hope that a more effective membership process will result. However, we note that RN 15–10 describes a two-step review process: an assessment phase and an implementation phase. Our concern is that this process will take far longer than it should. There are practical answers to practical problems within the MAP Rules well known to FINRA, the SEC and the industry. With very little effort, these can be implemented almost immediately.

Principles-Based Regulation

A few years ago senior management at FINRA and the SEC began talking about principles-based regulation, with a strong emphasis on risk management. Regrettably, this policy message has not yet been understood, much less implemented, in the FINRA trenches. What we see in the membership review process is still an inexplicable inflexibility and failure to recognize business realities in terms of time frames, capital and reputations at risk and the quality of the people seeking to run or expand a FINRA-member firm. A risk-based assessment should also recognize that there is no benefit to applying arcane capitalization rules to a broker-dealer

that will never hold customer securities or cash or whose capitalization is therefore of little relevance to the investing public or other broker-dealers. There still remains too much of a checklist mentality which, although ostensibly seductive, remains inefficient and often conveys a misleading impression of what is actually occurring at a particular firm. We welcome this review process as it specifically requests suggestions to update what is required to determine membership status.

If principles-based regulation is to be put into effect, FINRA's rules should demonstrate sophisticated analysis based on economic realities, risk and financial and functional distinctions. Paying lip service to addressing risk management concerns in the rule-making process has not, overall, in our view, resulted in more practical or efficient rules. We believe the financial services industry would be better served if FINRA were willing to reconsider and reassess where proven risks lie in the MAP process. Any regulation should always respect what its purpose is and never be a "solution" to a non-existent problem.

One Size Does Not Fit All with Respect to Risk Management

Based on risk assessment not only to the investing public but also to other broker-dealers, and market integrity, we suggest that FINRA focus on three (3) main categories of business risk in implementing its MAP rules: (1) carrying and clearing firms; (2) broker-dealers that make markets or otherwise have supporting roles in the financial services industry; and (3) broker-dealers that do not carry, clear or maintain customer accounts or even handle customer funds or securities (collectively, "Non-Custodial Brokers"). This latter category has three subgroups: (1) retail firms; (2) firms focusing on institutional business; and (3) firms that service both retail and institutional customers. Maximum risk lies with carrying and clearing firms, a rather small subdivision of the FINRA-registered broker-dealer population. The sad litany of issues that arise

from the business activities of retail firms clearly justifies enhanced regulatory scrutiny, but, again, there are fewer of those broker-dealer firms in existence these days and most of those are large firms. Institutional customers have multiple avenues of self-help options available to them, including, but not limited to, reputational and legal solutions, as well as those that the regulators can bring to bear.

A critical factor affecting these risk categories is the size of the particular firm. Yet the MAP Rules hardly take size into consideration. Even though FINRA's fees for the MAP process are segregated into tiers based on size, beyond that initial recognition that size matters, the MAP Rules make no further substantive recognition of this distinction. A one or two person shop engaged in private placements solely with institutional customers is reviewed under the MAP Rules in almost the same manner as a carrying and clearing firm. As part of the RN 15-10 mandate, size should be a major determinant of the scope of the MAP review process.

We propose a much simpler, unified regulatory approach to the non-custodial or advisory activities of broker-dealers. The receipt of transaction-based compensation should not automatically require registration as a broker-dealer.³ Instead, the analytic focus should be on risk and risk management. In our view, the MAP Rules should focus on the quality of the people at a firm and the money funding them. Currently, there are no overriding regulatory principles under the MAP Rules regulating the risks of clearing and carrying firms as opposed to all other types of broker-dealer firms. If FINRA is truly committed to assessing and improving its MAP processes, we suggest that the most stringent review process apply solely to carrying and

³ We recognize that it is the Securities and Exchange Commission that has mandated the registration and regulation of persons that receive transaction-based compensation even for those that do not do so in the traditional, active sense. Thus, there are many enterprises that have registered as broker-dealers even though, for example, all they do is maintain a computerized platform for transaction executions and do not necessarily execute transactions themselves.

clearing firms. Another set of rules should deal with those firms whose customers are exclusively retail and a third set of risk-based rules should focus on institutional business. Firms whose business model combines all three of these business activities pose the most risk and, quite correctly, should be more heavily reviewed during the MAP process, as they are now in the examination process post-approval. This retrospective rule review process should be an opportunity to address the needs of, and burdens on, small- and medium-sized firms. Instead, FINRA blithely continues to promulgate rules, including the MAP Rules, as if all prospective members and members are equally affected by the same issues in the same way. Moreover, many of the MAP Rules address very narrow issues promulgated in response to perceived issues, but this “band-aid” approach is about as effective as the efforts of that little Dutch boy to stop a flood by sticking his finger in a break in the dike. What is needed are principles-based rules that incorporate risk and business realities.

Instead, the industry is faced with continuous attempts by FINRA to segment and carve out minuscule exemptions to existing rules, while simultaneously creating burdensome, artificial and overly technical distinctions. For example, under the mandate of the Dodd-Frank and JOBS Acts, there has been a fair amount of regulatory rule-making with respect to private placement type activities. Recently, the industry has been presented with proposals for funding portals, crowdfunding, limited corporate finance brokers, the SEC’s M&A exemption letter and changes to the solicitation rules governing private placements.⁴ Not only will these proposals result in the “Balkanization” of the private placement regulatory scheme, which we have commented on

⁴ Proposed amendments to Regulation A, known as Regulation A-plus, are also part of this liberalizing regulatory trend, allow issuers more flexibility as an available exemption from the SEC’s registration requirements for securities offerings.

previously,⁵ but, far more damagingly, also create artificial distinctions that are hard to parse out in the real world. These definitional subcategories ostensibly exempting certain business activities are difficult to implement, and the significant regulatory burden FINRA has proposed is hardly worth anybody's efforts to use these new forms. What these private placement proposals have done, in fact, is generate lots of business for lawyers who are hired to review and assess whether their particular clients' business model can fall within one of these exemptions. If FINRA had a simpler, straightforward set of principles-based rules that apply to firms focusing solely on private placements with institutional firms, and, perhaps, high net worth individuals, based on risk assessment, these proposals would be unnecessary.

We note with great interest FINRA's streamlined MAP Rules applicable to funding portals. Our position is that FINRA's MAP process for firms with, say, 10 or fewer Associated Persons with a limited business model requiring limited net capital (the proverbial "nickel BDs") should follow registration rules somewhat similar to those applicable to funding portals; generally, in our experience, the business activities of such firms are private placements, advisory services and referrals. Paramount is applying the speed of the funding portal approval process to such nickel BDs. The business, customer and industry risks are minimal, while the FINRA MAP Rules are needlessly burdensome. Other types of firms that could benefit from a quick approval process under the MAP Rules are third-party marketers acting on behalf of funds, firms that specialize in the sale of research only or firms contracting for transaction-based

⁵ IMS Letter on RN 14-09, Limited Corporate Finance Brokers (April 28, 2014) on file on the FINRA website at <http://www.finra.org/sites/default/files/NoticeComment/p496881.pdf>.

compensation for what is essentially the sale of trading platform or algorithmic trading services when the applicant itself does not execute securities transaction directly.⁶

MAP Rules that Work

Many of FINRA's MAP Rules and standards should be preserved, but they should be based on economic and risk-driven criteria, not a one-size-fits-all approach. Fidelity bonds have proven useful. Continuing education requirements should remain in place. Of course, people dealing in other people's money should be licensed, but as discussed further below, the confusing subcategories of licenses should be simplified.

MAP Culture

The MAP Rules themselves are designed to regulate application processes. Implicit in these processes is the notion that the goal of the processes should be Approvals, not dis-Approvals. Over the past few years, the FINRA member community has shrunk due to various factors. Among these is the cumbersomeness of the process of becoming a FINRA member since registration as an Investment Adviser is far easier and speedier. Changing the culture at FINRA such that its review will occur in a more positive manner will change the playing field so that people will actually enjoy FINRA membership and not be cynical about it.

MAP Rules that Don't Work

Licensing

FINRA's licensing requirements are valuable, but needlessly complex. We have spent countless hours explaining to prospective applicants the differences, benefits and burdens among the Series 7, 22, 62, 79 and 82 licenses. NASD Rules 1031 and 1032 are torturous to read and

⁶ We are aware that FINRA is currently seeking comment on whether registration of Associated Persons involved in the design, development or significant modification of algorithmic trading strategies is needed; Regulatory Notice 15-06.

somewhat contradictory; the exam instructions for each of these series licenses are worse than the rules themselves.

We remain baffled why anyone has to be registered with any firm to take the Series 7 (or any other) license. If someone wants to determine if functioning as a broker-dealer is a viable career choice for them, they should be permitted to take the exam. The license itself can be made dormant until the person affiliates with a FINRA member firm. This would also create the benefit of having licensed individuals available for hire by firms without protracted, and expensive, apprenticeship periods. Additionally, if someone leaves the industry voluntarily, why can't they meet their CE requirements and continue to maintain their licenses? Generally, such individuals have left the broker-dealer industry to work in the business world or other segments of the financial services industry. Their knowledge and training benefit their new employer. If that individual is also willing to take CE refresher courses, he or she remains just as qualified, from everyone's perspective, as if he or she is still working at a broker-dealer.⁷ This would also significantly reduce the need for requests for exam waivers and appeals of adverse decisions.

Leases

Currently, we spend endless hours reviewing ridiculously long leases to determine whether the lease allows a sublease to an affiliated entity or whether a small broker-dealer operating from someone's apartment can actually do so if the premises lease prohibits commercial activity.⁸ If it doesn't, then FINRA requires landlord consent and the Applicant

⁷ Actually, a person who leaves a broker-dealer to be employed in an ancillary activity such as being associated with a so-called buy-side organization, or practicing noble professions such as law or accounting, or being employed as regulators, brings invaluable experience when he or she rejoins the FINRA community. There is little sense to have them requalify by examination when they possess experience that is extremely valuable to the financial services community.

⁸ This is required under the MAP Rules even if no customers ever enter the premises of said apartment. We have never understood what purpose is served by forcing a person whose business is conducted primarily on the telephone and by e-mail to obtain a separate office facility just to satisfy an archaic NASD requirement.

spends a lot of time, and, often, counsel fees, negotiating and/or obtaining such consent. When a member or prospective member has 10 or fewer Associated Persons, what difference does a lease make? Often, the Associated Persons at many smaller firms with limited business models are rarely found in their offices anyway. They are traveling to identify deals and connect the parties. Their primary means of conducting business, and storing records, are electronic: computers, e-mails, cell phones, etc. A physical space apparently satisfies FINRA, but if there is no customer physical contact expected at that space, it is simply a wasteful, non-critical business expense. These days, there are many reputable options for obtaining meeting space. Anyone can walk into a business center and lease space for meetings for however long needed.

Written Supervisory Procedures (“WSP”) Checklist

Anyone who has ever had to fill out the WSP checklist complains about what a useless document it is. We find it difficult to explain to clients why they have to pay for us to fill in a WSP checklist (and clients have asked and then complained), which contains 74 screens (slightly shorter than the Form NMA), each screen generally requiring 6 to 8 responses (which are usually the word “no”). If someone were to try to draft a set of WSPs based on the WSP checklist, the resulting set of WSPs would contain glaring omissions. If people at a functioning broker-dealer would try to use it, they would obtain no regulatory guidance; perusing the Table of Contents in even an off-the-shelf set of WSPs would be more useful. We hope that the WSP checklist is of some use to FINRA MAP personnel, but we have yet to ascertain what that value is. If (and we believe it doubtful) FINRA derives some regulatory benefit from the continued requirement that the WSP checklist be attached to all NMAs and any CMA adding new business lines, there is a way to make its completion a less burdensome requirement. Since most firms only engage in specific, narrow types of business, such as private placements, no one should have to fill out

multiple sections of the WSP checklist that do not pertain to the business lines for which they are seeking approval with an endless sequence of “no.” Instead of completing all 74 screens, all applicants should fill out an initial section that applies to all types of firms. Then, instructions at the top of the WSP checklist should state, for example, if you are only applying to engage in private placements fill out screen numbers 15 to 20; if your business includes the sale of municipal securities, fill out screen numbers 32 to 40; for options, screen numbers 57 to 68; etc.

Membership Interview

During the review process, particularly after the initial comment letter from FINRA is received, it is typical for the FINRA examiner and the Applicant’s representative(s) to communicate with each other informally, either by phone or e-mail. As part of the initial review process, under NASD Rule 1013(a)(4), FINRA routinely requests additional documents and information from the Applicant’s representative(s). Our concern is with the raising of new issues at the membership interview without prior notice to the Applicant’s representative(s).

FINRA is a regulator and its MAP review process is more in the nature of an administrative review. Most membership applications are approved and once registered, most members do what is necessary and prudent to maintain their membership status and most importantly, earn a profit. When FINRA waits until the membership interview to present adversarial information and/or documents for the first time, that meeting can turn into an amateur Perry Mason scenario generating hostility on both sides. It may be melodramatic, but we strongly question whether it is effective or necessary.

We had a situation at the membership interview where FINRA presented information concerning a dispute that a principal of the Applicant had with the landlord for his personal residence involving a fairly small amount and with zero impact on the Applicant’s business.

Instead of asking for an explanation during the review process, FINRA waited until the membership interview. Once the issue was raised, the Applicant was able to provide information and documents that fully resolved FINRA's concerns. But all that could have been done far more quickly earlier in the review process, without the theatrics of introducing this issue at the membership interview.

We are baffled as to the benefit of dragging the review process out when issues are raised, for the first time, at the membership interview.⁹ This is a waste of the time and resources of all sides; after all, it is called a "membership" interview. It is also expensive, needlessly so. The membership interview should be a time for FINRA to meet the principals of a new or continuing member and resolve any loose ends, not raise new issues by ambush. We understand that, occasionally, membership applications are denied, but that should be based on the ongoing review and a determination that certain adverse facts cannot be overcome. In those few situations, the Applicant would know that it was attending a membership interview where FINRA would state the basis for its rejection. That procedure is already in place for when FINRA "...receives such [adverse] information or document after the membership interview or decides to base its decision on such information after the membership interview..."¹⁰ In those post-membership interview situations, FINRA "...shall promptly serve the information or document and an explanation thereof on the Applicant."¹¹

Where in the Rules is That?

During the MAP process, particularly with CMAs and MatCons, we have repeatedly encountered attempts at micro-management by FINRA Staff persons who often know little about

⁹ We understand that, in rare circumstances, the information and/or documents may not be available to FINRA prior to the membership interview.

¹⁰ NASD Rule 1013(b)(7).

¹¹ Id.

many of the specific nuances of various segments of the securities industry challenging industry veterans who clearly are experts. Even worse, sometimes we encounter FINRA personnel who think it's appropriate to create and enforce non-existent rules. For example, if a well-capitalized, 3-person firm, with a very well-established parent entity, wishes to sell private placements to institutional accounts, why does membership approval have to be delayed until one of the 3 Registered Representatives who already holds the Series 7 and 24 licenses gets his Series 79 license, while another individual who already holds the Series 7 and 79 licenses pass the exam for the Series 24 license? FINRA rules require that a Registered Representative who engages in certain business activities must have specified licenses. Nowhere do those rules require that the same person hold both the Series 24 and 79 licenses simultaneously for the firm to function. Particularly when the finances of the firm are not in question, what risk is posed to the public or the industry by a firm dealing only with institutional customers if a particular Registered Representative does not hold all the licenses initially as long as someone in the firm has the needed license? What is sad is that when we ask, "Which rule states that?" the examiner generally has no answer. This is a no-win situation for everyone. It is clearly inappropriate for the MAP Staff to attempt to enforce non-existent rules or policies that have not been vetted or publicized.

Processing Time Frames

All who are subject to the MAP process complain about processing times. In fact, virtually the first question asked about NMAs and CMAs by established clients is, "how long do you think this will take?" They have all heard horror stories of reviews beyond the regulatory 180 day period, as have we. When a FINRA examiner asks that we "request" an extension, it triggers heated debate internally and sometimes, with client input and approval, we have refused;

amazingly, that has often triggered the instantaneous completion of the review within regulatory time mandates.

We acknowledge and appreciate that FINRA has implemented a fast-track review process. Much as FINRA did with the MatCon guidelines (the “Guidelines”),¹² it would be helpful if FINRA provided guidance with respect to which firms, under which circumstances, would qualify for fast-track review status and why. Regrettably, we are currently unable to counsel our clients as to whether they qualify for fast-track review and it often seems to remain an arbitrary decision. CMAs are particularly time sensitive and often dictated by impending business deals. Yet only rarely have we been able to persuade FINRA that certain CMAs are driven by business considerations. We represented a well-established firm in business for nearly 40 years with plenty of net capital and two miniscule, technical violations of trade reporting rules that sought to hire a particular investment banker with an established client base. By the time FINRA granted approval to add private placements and M&A advisory services as business lines, that investment banker had joined another broker-dealer; sadly, nearly 2 years later, that firm still has not found a comparable replacement. We welcome the institution of the MatCon process and the issuance of the Guidelines, but note, anecdotally, that most MatCons are denied. At our firm, we find we have better success with a MatCon if the request is a page or two long, accompanied by carefully selected attachments.

¹² <http://www.finra.org/industry/overview-materiality-consultation-process>.

Net Capital

Given the limited risk and scope of activities of Non-Custodial Brokers who, by definition, never handle customer securities or funds, the net capital rules serve no benefit either as a measure of fiscal integrity or as a meaningful barrier to entry into the brokerage business. Net capital requirements should be replaced with a significant fidelity or performance bond. Reliance on market-based insurance underwriting standards, with insurers having their money and reputations on the line, would provide more realistic investor protection. Such brokers, moreover, have no need for an annual audit report that no one reads other than the regulators. With no customer funds or securities at risk, the filing of periodic FOCUS Reports by advisory brokers is of marginal, if any, utility.¹³

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¹³ For the sake of full disclosure, we note that a significant portion of the income of our firm is derived from the financial and operational functions we perform for our clients. In spite of that, we unselfishly continue to endorse a construct that would reduce net capital and reporting requirements for many of them. We have previously commented publicly in support of a more simplified regimen. We understand that FINRA's ability to simplify these rules is limited by the existing rules of the Securities and Exchange Commission.

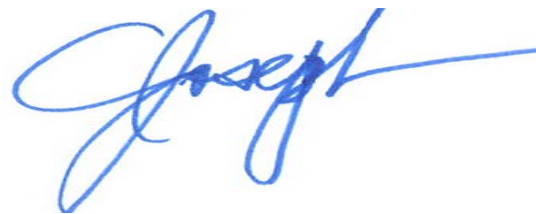
What the industry needs is a simplified, rational and uniform approach to the admission, expansion and regulation of broker-dealer activities. The key guidelines should be risk assessment and cost efficiency.

Thank you for the opportunity to comment on RN 15-10. Should you have any further questions, please feel free to call Howard Spindel at 212-897-1688 or Cassondra Joseph at 212-897-1687, or contact us by e-mail at hspindel@intman.com or cjoseph@intman.com, respectively.

Very truly yours,

A handwritten signature in black ink, appearing to be 'H Spindel', with a stylized, overlapping structure.

Howard Spindel
Senior Managing Director

A handwritten signature in blue ink, appearing to be 'Cassondra E. Joseph', with a long horizontal flourish extending to the right.

Cassondra E. Joseph
Managing Director