

MEMO# 23591

June 29, 2009

Institute Files Comment Letter on FINRA's Proposed Revisions to the NASD's Suitability and "Know Your Customer" Rules

[23591]

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TO: TRANSFER AGENT ADVISORY COMMITTEE No. 47-09
BROKER/DEALER ADVISORY COMMITTEE No. 36-09
COMPLIANCE MEMBERS No. 33-09 RE: INSTITUTE FILES COMMENT LETTER ON FINRA'S
PROPOSED REVISIONS TO THE NASD'S SUITABILITY AND "KNOW YOUR CUSTOMER" RULES

As we previously informed you, [\[1\]](#) in May FINRA published for comment two new rules that would consolidate the rules of the NASD and NYSE relating to suitability and "know your customer," respectively. The Institute has filed the attached letter in response to FINRA's request for comment. The Institute's letter recommends that the proposed suitability rule, FINRA Rule 2211, retain an exception in the NASD rule that relieves members from having to obtain suitability information when recommending transactions if the transactions are limited to money market funds. As noted in the Institute's letter, this exception has been part of the NASD's suitability rule since it was originally adopted almost twenty years ago. Notwithstanding this, it is omitted from FINRA's proposed new rule without comment or explanation. As such, it cannot be determined whether its omission was deliberate or unintended. If deliberate, the letter notes that the Notice should have discussed its elimination, including the costs and benefits associated with such elimination.

The Institute's letter also comments on proposed Supplementary Material .02 to proposed Rule 2211, which would address the three components of members' suitability obligations.

[2] The letter notes that a recent FINRA Regulatory Notice [3] states that certain inverse and leveraged exchange-traded funds “are unsuitable for retail investors who plan to hold them for longer than one trading session.” The Institute’s letter notes that such a definitive statement usurps a member’s ability to determine the suitability of its recommendations. To address this concern, the letter recommends that Supplementary Material .02 be revised to reaffirm that such determinations lie with the member and not FINRA. The letter additionally recommends that FINRA withdraw its recent Notice and, if necessary, instead issue a notice that both recognizes the responsibility of the member to make suitability determinations and provides meaningful guidance relating to recommendations involving non-traditional ETFs.

Tamara K. Salmon
Senior Associate Counsel

[Attachment](#)

endnotes

[1] See Institute [Memorandum](#) to Transfer Agent Advisory Committee No. 36-09, Broker/Dealer Advisory Committee No. 25-09, and Compliance Members No. 26-09 [No. 23476], dated May 21, 2009.

[2] These three suitability obligations are reasonably-basis suitability, customer-specific suitability, and quantitative suitability.

[3] See Non-Traditional ETF: FINRA Reminds Firms of Sale Practice Obligations Relating to Leveraged and Inverse Exchange-Traded Funds, FINRA Regulatory Notice 09-31 (June 2009).

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