

MEMO# 23593

June 30, 2009

Institute Comment Letter on Proposed FINRA Rules Recommends That FINRA Withdraw Recent Notice on ETF Suitability

[23593]

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TO: EXCHANGE-TRADED FUNDS (ETF) COMMITTEE No. 4-09 RE: INSTITUTE COMMENT
LETTER ON PROPOSED FINRA RULES RECOMMENDS THAT FINRA WITHDRAW RECENT
NOTICE ON ETF SUITABILITY

As you may know, 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. [\[1\]](#) The proposed suitability rule, Rule 2111, would be accompanied, in part, by proposed Supplementary Material .02, which would address the components of members’ suitability obligations. The comment letter we filed with FINRA on the proposal raises an issue that may be of interest to ETF sponsors.

In particular, in addition to supporting the rules’ adoption, the Institute’s letter recommends that FINRA address our concerns with a recent Regulatory Notice it published relating to recommendations involving “non-traditional ETS.” [\[2\]](#) FINRA’s Notice states, in relevant part, that certain inverse and leveraged exchange-traded funds “are unsuitable for retail investors who plan to hold them for longer than one trading session.” As such, according to the Institute’s letter, FINRA’s position appears to replace the ability of members to make suitability determinations involving these products with the value judgment of a Government-registered association. To ensure that such determinations lie with the member and not FINRA, the Institute’s letter recommends that FINRA amend Supplementary Material .02 to clarify this issue. It also recommends that FINRA withdraw

its recent Regulatory 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 \(in .pdf format\)](#)

endnotes

[\[1\]](#) See FINRA Notice to Members 09-25 (May 2009).

[\[2\]](#) 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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