PFS INVESTMENTS INC.
Member FINRA®

September 1, 2010

VIA Electronic Mail to rule-comments@sec.gov

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

RE: SR-FINRA-2010-034

Dear Ms. Murphy:

Introduction

This letter is submitted on behalf of PFSI Investments, Inc. ("PFSI"). PFSI recognizes the challenges and the importance of establishing a consolidated FINRA rulebook; however, PFSI has two concerns with the proposal. First, the process surrounding the proposal raises concerns regarding transparency and fundamental fairness. Second, the scope of proposed FINRA Rule 4530 goes well beyond mere consolidation, and substantially expands the current reporting requirements contained in NASD Rule 3070 and NYSE Rule 351. While the consolidation process presents an opportunity to improve upon the existing rules, proposed Rule 4530 places an unnecessary burden on member firms without any clear benefit to consumers or the market.

Discussion

When FINRA originally proposed Rule 4530 various commentators, including industry organizations representing a significant number of member firms, noted that while the proposed rule incorporated NYSE Rule 351 it failed to include the interpretive guidance contained in NYSE Information Memo 06-11. To address this apparent oversight, the commentators requested that Information Memo 06-11 be incorporated into the proposal. Surprisingly, FINRA rejected its member's suggestion with no explanation beyond stating, "FINRA believes that the standard set forth in Information Memorandum 06-11 is too narrow."[1]

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[1] SR-FINRA-2010-034 - p. 17

PFSI contends that a departure from the existing rules as significant as Rule 4530 should be supported by a detailed explanation that considers the costs of the proposal and not just the presumed benefits.[2] Anything less deprives member firms of a fair opportunity to assess the basis for the proposal and limits a firm's ability to offer meaningful commentary. Likewise, the absence of a demonstrated need for the proposed rule and the lack of an in-depth refutation of the members' concerns deprive the Commission of sufficient information to evaluate whether the changes will advance the goals of customer protection and market integrity without unnecessarily burdening members or creating harmful unintended consequences.[3] Ultimately, the absence of a detailed justification for the proposal undermines the perceived fairness of the rulemaking process.

With respect to the specific deficiencies of proposed Rule 4530, other commentators more than adequately have identified its various problematic components and PFSI will not reiterate those issues chapter and verse. However, PFSI would like to emphasize that the requirement under paragraph (b) of the proposed rule to report instances in which a firm has concluded or reasonably should have concluded that a violation has occurred places a firm in a precarious situation in which inherently subjective assessments will be susceptible to second guessing. For instance, whether certain conduct rises to the level of a violation often turns on unsettled interpretations of law and disputed interpretations of fact, including the significance of documentary evidence and the credibility of witnesses. Basing reporting requirements on such a subjective analysis will create uncertainty for firms and is likely to lead to inequitable enforcement decisions. Interestingly, FINRA has eliminated an element of subjectivity from the reporting of <u>external</u> findings by removing the requirement to report "any and all" findings that amount to violations of just and equitable principles of trade. This makes sense because in most instances an external body that issues a finding is unlikely to enunciate whether particular conduct violates just and equitable principals of trade; thus leaving the firm to guess whether FINRA would conclude so. In contrast, the requirements of Rule 4530(b) inject a new element of subjectivity that will hinder a firm's ability to report accurately.

Furthermore, since Rule 4530 requires reporting within 30 days of the date on which the firm "reasonably should have concluded" that a violation occurred, firms will be imperiled by the threat of enforcement actions based on the timing of the conclusion, as well as the conclusion itself. For example, a firm might take 60 days to reach a conclusion and report the findings, only to have FINRA decide later that the conclusion should have been reached sooner and the reporting is late.

In comparison, NASD Rule 3070 requires reporting based on clear and objective standards, such as whether an external entity has found a violation or whether a firm has imposed discipline in excess of clearly defined thresholds. Likewise, NYSE Rule 351 and Information Memo 06-11 provide clear guidance regarding reportable conduct. For example, NYSE members must report conduct that results in discipline at or above

[2] Even as to the presumed benefits, beyond several generic statements, the rule filing does not explain how it is an improvement over the present regulatory scheme.

[3] PFSI notes that in Notice 08-71, in which Rule 4530 was initially announced, FINRA provided no discussion or clear notice that it affirmatively had decided to abandon the guidance contained in NYSE IM 06-11.

clearly defined levels, recidivist or ongoing violative conduct, as well as violative conduct by the firm that is systemic or has a widespread impact on the firm, customers or industry.[4] Importantly, "isolated or individual exceptions to otherwise effective and regulatory compliant operations" do not require reporting.[5] The existing rules also require reporting of written customers complaints and prompt amendments to Forms U4 and U5.

Notwithstanding the extensive scope of the existing rules, FINRA seeks a significant expansion of the reporting requirements with little explanation beyond boilerplate statements that appear in most rule filings. In fact, neither Notice 08-71 nor SR-FINRA-2010-034 include a single example of a case in which the existing rules have deprived FINRA of information or hampered its ability to carry out its regulatory mandate.

Conclusion

Given the broad scope of the existing reporting requirements and the proposal's failure to demonstrate the need for or the benefit of the expanded reporting requirements, PFSI respectfully requests that the SEC reject SR-FINRA-2010-034 and require FINRA to provide a detailed analysis to support its claim that the proposed rule will advance the goals of customer protection and market integrity without placing an undue burden on member firms. At a minimum, the SEC should require FINRA to amend the proposal to incorporate fully the interpretive guidance contained in NYSE Information Memo 06-11.

Thank you for your consideration of these comments.

Sincerely yours,

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[4] NYSE Information Memo 06-11
[5] Id.