

VIA ELECTRONIC MAIL

March 20, 2014

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: Regulatory Notice 13-42: Comprehensive Automated Risk Data System

Dear Ms. Asquith:

On December 23, 2013, the Financial Industry Regulatory Authority (FINRA) published a request for comment on a concept proposal to develop a new Comprehensive Automated Risk Data System (CARDS), a rule-based program that would allow FINRA to automatically collect information from clearing firms on accounts, trading activity, and security identification.¹ CARDS would collect specific retail customer information from clearing and self-clearing firms on a regular schedule. Introducing firms would be required to transmit the specific information to their clearing firms which would then provide this data to FINRA on a daily or weekly basis. FINRA has stated in the proposal that the purpose of CARDS is to identify risks, assist FINRA in assessing business conduct patterns and trends in the industry, assist firms with their compliance and supervisory programs, and reduce the number of information requests firms currently receive from FINRA.²

The Financial Services Institute³ (FSI) appreciates the opportunity to comment on this important proposal. FSI and its members support efforts by regulators to improve oversight, increase the efficiency of the examination process, and enhance investor protection. FINRA asserts that CARDS is capable of achieving these goals while supporting a more effective examination program. These goals are laudable, and under ideal conditions would be a promising and effective additional tool for regulators to enhance supervision capabilities and improve market efficiency and integrity. As proposed, however, CARDS presents significant challenges due to its ambitious scope and massive scale. These challenges include data standardization, data complexity, data translation, system infrastructure, and the incredible financial costs required to develop, implement and maintain CARDS. In addition, the collection and centralized warehousing of vast quantities of data raises substantial concerns with regard to data security, privacy, and potential liability in the event of a security breach. FSI and its members believe some of these issues may be mitigated

¹ Regulatory Notice 13-42, Comprehensive Automated Risk Data System, available at <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p413652.pdf>.

² *Id.* at 7.

³ The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has 100 Broker-Dealer member firms that have more than 138,000 affiliated registered representatives serving more than 14 million American households. FSI also has more than 37,000 Financial Advisor members.

with alternative approaches; however, we are concerned the development and implementation of CARDS is simply not feasible while preserving widespread investor access to the services of independent broker-dealers and financial advisors. Therefore, FSI cannot support the creation and implementation of CARDS as currently proposed.

Background on FSI Members

The independent broker-dealer (IBD) community has been an important and active part of the lives of American investors for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD firms also share a number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; primarily engage in the sale of packaged products, such as mutual funds and variable insurance products; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered investment adviser firms or such firms owned by their registered representatives. Due to their unique business model, IBDs 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 financial goals and objectives.

In the U.S., approximately 201,000 independent financial advisers – or approximately 64 percent of all practicing registered representatives – operate in the IBD channel.⁴ These financial advisers are self-employed independent contractors, rather than employees of the IBD firms. These financial advisers 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. Clients of independent financial advisers are typically “main street America” – it is, in fact, almost part of the “charter” of the independent channel. The core market of advisers affiliated with IBDs is comprised of clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisers are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other centers of influence.⁵ Independent financial advisers get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisers have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisers. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is committed to preserving the valuable role that IBDs and independent advisers play in helping Americans plan for and achieve their financial goals. FSI's primary goal is to ensure our members operate in a regulatory environment that is fair and balanced. FSI's advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

⁴ Cerulli Associates at <http://www.cerulli.com/>.

⁵ These “centers of influence” may include lawyers, accountants, human resources managers, or other trusted advisers.

Comments

FSI appreciates the opportunity to submit comments on FINRA's CARDS Proposal. We support FINRA's goal of enhancing its ability to supervise and analyze market trends. In addition, efforts that increase the efficiency of the examination process by reducing the number of piecemeal information requests will reduce the resource burden placed on firms. However, as currently proposed, CARDS presents several significant challenges which are described in the following comments:

- **CARDS Raises Significant Issues Regarding Data Security, Data Privacy, and Potential Liability in the Event of a Security Breach:** As proposed, CARDS will collect the following information: 1) account information to be used for sales practice reviews including suitability, commissions, markup/down, account types, customer investment profiles, and representative and branch CRD numbers; 2) account activity information related to suitability, anti-money laundering (AML), fraud detection, purchase and sales dates, margins, and account balances; and 3) security identification information such as CUSIP. The sensitivity of this information cannot be overstated, particularly when considering the data and security breaches that have recently occurred to major retailers⁶ and government agencies.⁷ The magnitude and scope of CARDS' data collection make it an attractive target for hackers and other online criminals intent on accessing and misusing this information. As a result, firms and the investing public have raised legitimate and serious privacy and data security concerns with respect to the data collection envisioned by FINRA through CARDS.⁸ In addition, due to FINRA's status as a non-governmental self-regulatory organization (SRO), firms and advisors have significant concerns with respect to accountability, legal liability, and reputational harm in the event of a data security breach. Firms and advisors take very seriously their duties to safeguard the personal information of their clients. In the event of a breach, however, investors will likely place blame on advisors and firms if FINRA fails to keep safe their personal and financial information. We expand on these comments below:
 - *Exclusion of Personally Identifiable Information (PII) Does Not Alleviate All Concerns:* While FSI is encouraged by FINRA's announcement that PII will be excluded from CARDS data,⁹ FSI remains concerned with the data security issues introduced by CARDS. The data collection process must include significant controls and systems to ensure that CARDS is secure, and must provide a robust and transparent description with respect to the methods FINRA plans to utilize to protect client and firm data. This may include data encryption methods and separate systems for storing client data that, if combined, may increase the risk to clients. For example, suitability data on clients often includes certain data elements, such as age, that may increase the risk to clients' data security when combined with other data that CARDS collects. Furthermore, while FINRA will not seek PII from CARDS data, the data will still be consolidated at the clearing firm level. While FINRA may not have

⁶ See Mark Hosenball, "Target vendor says hackers breached data link used for billing," Reuters (Feb. 6, 2014), available at <http://www.reuters.com/article/2014/02/06/us-target-breach-vendor-idUSBREA1523E20140206>.

⁷ See Rory Carroll, "Snowden used simple technology to mine NSA computer networks," The Guardian (Feb. 9, 2014), available at <http://www.theguardian.com/world/2014/feb/09/edward-snowden-used-simple-technology-nsa>.

⁸ See, e.g., Letter from Paul Meehl to Marcia Asquith, (Jan. 3, 2014), available at <http://www.finra.org/Industry/Regulation/Notices/Comments/P424802>; Letter from Sweney Cartwright & Co. to Marcia Asquith (Jan. 24, 2014), available at <http://www.finra.org/Industry/Regulation/Notices/Comments/P439084>.

⁹ Update Regarding Regulatory Notice 13-442, available at <http://www.finra.org/Industry/Regulation/Notices/2013/P451243>.

the PII, the data security concerns with consolidated financial data still remain but have been shifted from FINRA to the clearing firms.

- *FINRA and Clearing Firms Should Be Subject to SSAE-16 Auditing Standards Regarding Data Privacy and Data Security Controls:* Like many companies that operate data centers and are responsible for safeguarding sensitive consumer information, FINRA should become subject to Statements on Standards for Attestation Engagements No. 16 (SSAE-16). Firms subjected to SSAE-16 are audited “to report on controls at organizations that provide services to user entities when those controls are likely to be relevant to user entities’ internal control over financial reporting.”¹⁰ With respect to data security and privacy, FINRA would attest to the controls and systems in place to protect data security and privacy. During an examination, FINRA’s external auditor would audit to these standards and provide a report of its findings. By attesting and auditing to these standards, FINRA will be more accountable to its members and their clients with respect to the effectiveness of their systems and can identify areas of improvement. It would also hold FINRA to the same standards as other data centers in the private sector that are often required by contract to be subject to SSAE-16. However, if FINRA does utilize this approach, it must also provide firms with the ability to opt out of the CARDS submission process in the event that FINRA becomes SSAE-16 deficient. These standards should also apply to clearing firms should CARDS collect data as proposed in the concept release.
- *Clarify Legal Liability with Respect to Data Security and State Privacy Laws:* Firms may find themselves subject to state and federal civil regulatory liability in the event of a breach of FINRA’s CARDS data. Firms may also be sued by clients for damages in the event that FINRA’s controls or the clearing firms’ controls are inadequate to prevent a breach and the data is misused. It is not clear which parties would be found liable in this instance, and FINRA should clarify that it alone would be liable in the event that its systems are compromised and individual clients have their data stolen or misused. Current litigation between retailers and banks with regard to financial liability in the wake of security breach highlights this concern.¹¹ This may require coordination with regulators or federal legislation due to FINRA’s position as a non-governmental regulator and the various state laws covering data security.¹² An additional concern for firms is state consumer data privacy laws. Individual state legislatures have proposed or passed laws that place a variety of restrictions and requirements on firms with respect to the collection and transmission of client data.¹³ Firms have concerns that they will either violate state data privacy laws or incur significant legal fees in order to fully understand and comply with the variety of state requirements that impact their ability to transmit client data as required by CARDS. However, it is important to note that even if a breach occurred and FINRA was fully liable, FINRA would be unable to compensate firms for the reputational harm firms would suffer as a result.

¹⁰ American Institute of Certified Public Accountants, Attestation Standards § 801; available at <http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AT-00801.pdf>.

¹¹ See *Putnam Bank v Target Corp.*, Case Number 14-cv-00121, (D.Minn 2014), available at <http://www.aba.com/Tools/Function/Legal/Public/edocketdocs/Putnam%20Bank%20v.%20Target%20Corp.%20-%20Class%20Action%20Complaint.pdf>.

¹² See, e.g., Massachusetts Data Security Regulations, 201 CMR 17.00.

¹³ See, e.g., California AB 370 (signed into law September 27, 2013); Cal. Bus. & Prof. Code §§ 22575-22579.

- **Future Collection of Direct Business Data Will Involve Significant Challenges:** FSI and its members are concerned that by appointing clearing firms as the data conduits at the outset of this initiative, later developments and phases will rely upon clearing firms as well. FINRA should be aware that requiring direct business information to be submitted through clearing firms will create an unprecedented disruption to firms who have built businesses that do not rely upon clearing firms' brokerage platforms for every transaction. While several FSI member firms are self-clearing, most conduct transactions on a fully disclosed basis with a clearing firm. In this arrangement, FSI members act as the introducing broker-dealer, which "introduces" client accounts and transactions to a clearing firm that is a Depository Trust & Clearing Corporation (DTCC) member for purposes of clearance, settlement, and custody.¹⁴ These transactions will take place through the clearing firm's brokerage platform after the broker-dealer and financial advisor conduct the required pre-trade suitability, Know Your Customer (KYC), AML, and other compliance reviews. Upon entering the transaction via the clearing firm's brokerage platform, an automated processing system captures and transmits the order, books transactions in the customer account, and settles the transaction. The clearing firm also makes payments to the broker-dealer, maintains consolidated position information, and generates statements and tax forms for the client.

In addition to utilizing a clearing firm's brokerage platform for trading, many firms and advisors directly process transactions with product providers, typically mutual fund companies, variable annuity providers, or alternative investment sponsors. For many IBD firms, this non-brokerage represents a very significant part of their business model. Commonly referred to as "direct business," transactions often are conducted through the so-called "check and app" process. Upon following the pre-transaction suitability requirements of Rule 2111, a client completes and signs an application and provides a check to his or her financial advisor. The financial advisor forwards these materials to the broker-dealer home office or Office of Supervisory Jurisdiction (OSJ) to conduct principal review, KYC, and AML processes before forwarding these materials to the product provider. Upon reviewing the application, the product provider makes the investment, sends the commissions to the broker-dealer, and generates statements, tax reports, and other documents which it sends directly to the client. This transaction data does not flow through clearing firms' brokerage platforms, and therefore will not be collected in CARDS. Although introducing broker-dealers do retain the required books and records for these transactions, including documentation with respect to suitability, KYC, and AML, none of this information flows through the clearing firm platform. As a result, CARDS will not be capable of assessing all the information on retail customer accounts and activity conducted on a direct basis.

This shortcoming introduces significant challenges for FINRA. By not collecting direct business data, FINRA will be excluding a large percentage of the sales practice information that occurs in the securities industry that will be necessary for FINRA to have a complete picture of a specific firm or specific client. This may cause additional and unnecessary information requests as FINRA analyzes CARDS data. Furthermore, if FINRA requires direct business data to be provided to clearing firms as part of CARDS, firms may experience significant costs and challenges if forced to submit direct business data directly to FINRA or to clearing firms. Finally, clients who neither desire nor authorized the

¹⁴ See Henry Minnerop, *Clearing Arrangements*, 58 Bus. Law. 917 (May 2003).

sharing of their data with the clearing firm will have sensitive private data about their accounts and trading history shared with these entities. It is important to note that one of the major benefits of direct business is that it reduces the costs to firms and advisors and is therefore essential to providing financial services for middle and lower income clients. To the extent FINRA would seek to require firms to collect, standardize, and submit direct data, this would significantly impact the cost-effectiveness of direct business and ultimately investors' access to affordable financial advice.

- **As Proposed, CARDS Will Have Significant Challenges With Respect to Data Standardization, Data Quality, and Data Translation:** FINRA will experience significant challenges in standardizing data collected through CARDS and ensuring data quality. FINRA itself attempted to collect information on variable annuities using a standard request and template since 2011,¹⁵ and has likely experienced first-hand the difficulties involved with data standardization with respect to just one type of product. The differences in data format, pipeline, and translation methods create serious challenges to collect and analyze this information, particularly as new products frequently enter the market. These challenges also exist in normalizing data amongst a variety of clearing firms. They will compound should FINRA also attempt to collect data related to all direct business. The lack of standardization across carriers within each group of product providers will be an immense issue that will take enormous resources to address. FINRA would need to spend significant resources to create new systems and teams of employees responsible for obtaining the raw data, standardizing it, and then translating it to develop consolidated account information for customers and firms. If FINRA determines that data normalization is required for certain data fields, FSI has concerns that this process will require significant resources and will reduce the usefulness of CARDS data for the purposes of FINRA's analysis. For instance, FINRA states that it will use the data to "better analyze customer dealing information on an individual firm basis, compare one firm's customer dealing activity against its peers', and understand industry-wide patterns and trends."¹⁶ To the extent this data is required to be normalized, it may eliminate the utility of the analytics as normalized data may not include important context necessary to understand the customer dealings or the patterns and trends identified.

Firms and industry vendors have made numerous unsuccessful attempts to create common data standards and forms to reduce the costs involved with having non-standard product forms and data fields with respect to different investment products. In fact, one FSI member spent over a million dollars attempting to create a common new account form to streamline the back office process and was forced to abandon the project due to the cost and complexity involved. The enormous costs of creating this process will likely be passed on to firms and advisors. If FINRA begins to require new standardized CARDS data fields, the costs will be significant for firms and advisors to change their systems, repaper their accounts, and enter the new information in their systems. Firms have recent experience with the costs involved with adding only a few new data fields to their systems due to the changes made by FINRA's new suitability rule, FINRA Rule 2111. Many firms experienced costs running into the millions of dollars to comply with the new requirements.

¹⁵ See Remarks by Richard G. Ketchum (June 28, 2011); available at <http://www.finra.org/Newsroom/Speeches/Ketchum/P123832>.

¹⁶ Regulatory Notice 13-42 at 4.

- **FINRA is Also Engaged in Other Large-Scale Data and Technology Initiatives:** In addition to proposing the development of CARDS, FINRA is currently in the process of developing another large-scale data and technology project through the Consolidated Audit Trail (CAT) and has encountered serious delays and challenges. The CAT involves FINRA and 18 national securities associations jointly developing a plan to create, implement, and maintain a database of every order, cancellation, modification, and trade execution for all exchange-listed equities and equity options across all U.S. markets. The CAT will track orders through their lifecycle and identify broker-dealers handling each order to provide FINRA and the SEC with the ability to monitor overall market structure as well as for investigating insider trading and market-manipulation. In addition to providing more powerful tools for regulators, the CAT may also be a benefit to the industry by reducing the quantity of data that firms and exchanges produce for regulators during examinations and other regulatory requests. The development of the CAT represents an enormously challenging technology and data project that has already required FINRA to request two temporary exemptions from the SEC filing deadline specified in Section 613(a)(1) of the Securities Exchange Act.¹⁷ The rule required FINRA and the exchanges to submit “a national market system plan to govern the creation, implementation, and maintenance of a consolidated audit trail and central repository (CAT NMS Plan).” This has required additional time to select the CAT plan processor and to provide bidders with the evaluation and approval process by which FINRA and the exchanges will “review and evaluate bids, narrow down the list of bids, use those bids in formulating the CAT NMS Plan, and, ultimately, select the CAT plan processor.”¹⁸ The challenges faced by FINRA in developing the CAT are notable because they have occurred during the initial planning phases. It is logical to assume that the development, implementation, and maintenance of the CAT will introduce additional costs for broker-dealers, particularly for firms who will be required to make changes to their systems in order to comply with the new regulatory and system requirements involved with CAT implementation. In addition to CAT, FINRA is currently engaged in other resource intensive initiatives, including the OTC Reporting Facility Platform migration¹⁹ and the implementation of additional data elements for Electronic Blue Sheets under the SEC’s Large Trader Reporting Rule.²⁰ Adding CARDS as another on-going technology and data project presents several significant issues for FINRA and member firms and may introduce inefficiencies and unnecessary duplication. It will also put a substantial resource burden on member firms to prepare for two separate regulatory programs that each introduce significant burdens in terms of financial and employee resources. FSI requests that FINRA reconcile these challenges in the following ways:
 - *Identify Areas of Overlap between CARDS and CAT:* Although there are distinctions between the goals and processes of each system, there are potential areas of overlap. FINRA should identify and eliminate these overlaps for members as the development of CARDS and CAT continues. FINRA should also provide firm

¹⁷ See Order Granting a Temporary Exemption Pursuant to Section 36(a)(1) of the Securities Exchange Act of 1934 from the Filing Deadline Specified in Rule 613(a)(1) of the Exchange Act, Release No. 34-71018 (December 6, 2013); see also Order Granting a Temporary Exemption Pursuant to Section 36(a)(1) of the Securities Exchange Act of 1934 from the Filing Deadline Specified in Rule 613(a)(1) of the Exchange Act, Release No. 34-69060 (March 7, 2013).

¹⁸ *Id.*

¹⁹ See Revised Migration Date for New OTC Reporting Facility Technology Platform (Jan. 21, 2014); available at <http://www.finra.org/Industry/Compliance/MarketTransparency/ORF/Notices/P434983>.

²⁰ See Regulatory Notice 13-16, Electronic Blue Sheet Submissions (April 2013); available at <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p244048.pdf>.

guidance on implementing and complying with both CAT and CARDS, particularly for aspects of the rules that present challenges with overlapping data and coverage. Firms should not be required to create duplicative systems and processes for FINRA to collect the same data.

- *Provide Clarification with Respect to Rulemaking:* Based upon FINRA's description of the data collection through CARDS, the concept proposal appears to create new rules or requirements with respect to books and records. Firms are currently not required to maintain books and records in an electronic format, and some may maintain this information through imaging systems. For the purpose of CARDS, however, FINRA appears to significantly alter the books and records rules to require that this information be maintained in a database or electronic format that can be queried and submitted to FINRA for collection and analysis. Small firms that do not have the resources to build or purchase these sophisticated technology systems may be severely impacted by these changes. Even if such an investment was feasible, the cost of performing the necessary data entry to populate such a database would be prohibitive.
 - *Provide Extended Compliance Periods for Each System:* In addition to providing sufficient compliance and implementation periods for each system, FINRA should also provide staggered compliance periods that provide feasible and flexible deadlines for each of these new systems. Because of the complexity and challenges involved with CARDS, FINRA should give firms at least five years to develop systems and achieve compliance.
- **CARDS is Not Business Neutral and Will Introduce Costs that May Cause Advisors to Move Toward Alternative Business Models:** A serious unintended consequence of CARDS is that FINRA, in attempting to increase the robustness of its supervisory capabilities, will actually drive more business to alternative, less regulated business models. In doing so, CARDS will also have a detrimental impact on certain business models, particularly IBDs and independent financial advisors. The IBD model is very well suited to servicing investors with a wide range of investable assets. As a result, the IBD model is particularly important in delivering financial products, services, and advice to middle market clientele. One of the central reasons the IBD model works well in providing affordable advice is because firms are able to control their costs. FSI believes that the costs of implementing CARDS will fall very heavily on IBD firms and their advisors, which raises concerns that CARDS will have a disparate impact on these firms. For example, some smaller firms may use hard copy files or imaging systems rather than databases for maintaining certain required records. To the extent firms are required to expend significant resources to create new technology systems that transmit their data in a standardized format to clearing firms or directly to FINRA, this will severely impact their ability to provide cost effective services to clients most in need of affordable advice and services. Many financial advisors who have been running their businesses in a particular way to service their clients will be forced to carry at least some of the burden of the immense increased costs of CARDS, which will impact their small businesses and their abilities to service a wide range of clients. Advisors may be forced to purchase new software or services which will increase their overheads and may require them to abandon smaller accounts or leave the broker-dealer model altogether. In sum, as the costs required by CARDS are felt by firms and their financial advisors, they may find that they are struggling to remain profitable, and, therefore, may find different business models more attractive. Many advisors find current regulatory requirements to be expensive and

burdensome, and CARDS may be responsible for creating the additional burdens that drive them to change their businesses and broker-dealer affiliation. The end result will be fewer IBD firms and financial advisors to service investors in need of affordable financial advice and services.

- **CARDS Could Degrade Firms' Ability to Conduct Robust Suitability Analyses:** FSI members are concerned that CARDS will require firms' suitability data be transmitted in a standardized format in order to allow FINRA to more easily analyze the data. FSI has serious concerns about the potential harm to investors that would occur if suitability information and reviews are forced to become standardized. Currently, many firms use software tools that allow the firm to customize their suitability analyses to their particular business model and clientele. In addition to their robust software capabilities, firms also train financial advisors to collect suitability information from their clients and assess their clients' needs and goals, not just through data collection, but through building relationships and asking important questions. As such, firms and their financial advisors use both quantitative and qualitative methods to assess their clients' financial picture and determine suitability. For instance, a client's suitability profile may indicate they have a net worth within a certain dollar range and a low risk tolerance, but through interviewing the client and determining their financial needs, the financial advisor may understand the client also has expenses not reflected in a the suitability analysis data fields, such as medical expenses. In this situation, it may look on paper that a certain investment is unsuitable, but through additional context and information, the firm would understand that the seemingly unsuitable sale is intended to fulfill a need not reflected on the suitability form and is actually quite suitable given the entire picture of the client's situation. FINRA should be very cautious to insure that the standardization of data does not have the unintended consequence of reducing the ability of firms to make these types of robust and informed suitability determinations.

Furthermore, a significant portion of FSI members that do utilize clearing platforms maintain separate proprietary suitability systems and do not submit this information to their clearing firms. Firms do this for a variety of reasons. FINRA's books and records rules do not require standardized means of capturing and recording suitability data, and firms have been able to use this flexibility to create very sophisticated methods for analyzing portfolio risk for individual clients and across client segments. Firms often use these proprietary systems to create quantitative risk scores for clients and advisors and run algorithms for assessing portfolio risk against a client's new account form. Non-standardized suitability data and system requirements allow for enhanced investor protection and robust processes that leverage new and emerging techniques and technology.

- **FINRA Must Conduct a Thorough Cost-Benefit Analysis of Each Feature and Element of CARDS:** FSI and its members have been encouraged by FINRA's adoption of economic impact assessment and cost-benefit analysis with regard to rulemaking.²¹ Because of the magnitude and scope of CARDS, a number of significant issues arise that offer an appropriate opportunity to conduct thorough cost-benefit analysis. FINRA should investigate the resource drain on itself and broker-dealer firms from the number of on-

²¹ See Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking (September 2013); available at <http://www.finra.org/web/groups/industry/documents/industry/p346389.pdf>.

going large-scale data and technology initiatives it is currently undertaking. The analysis should directly consider the data security risks involved with CARDS and also cover potential alternative approaches that may alter some features of the concept proposal yet still provide FINRA with the ability to conduct analysis and improve examination efficiency. FINRA should also investigate whether its proposed data collection through clearing firms will insure CARDS provides a complete and accurate dataset to perform its data analysis, and whether this drawback justifies the expense of developing CARDS as proposed.

At this stage in the process, FINRA has not provided firms with sufficient specifics with regard to the type of data CARDS will collect, what format and fields this data will consist of, and how FINRA intends to normalize non-standardized data to conduct their analyses. Without these specifics, firms cannot adequately estimate the full costs or benefits of CARDS. As FINRA continues to advance this proposal and request more information from firms with respect to the costs involved in implementing CARDS, firms will need additional specifics from FINRA in order to accurately respond. For example, requests for information with respect to the costs on data standardization will require FINRA to provide the specific data fields and formats it intends to collect through CARDS. If FINRA requests information with respect to the costs of collecting direct business data, FINRA must provide a detailed description of which data fields and which products it requires, and in which format. In addition, FINRA should analyze to what extent their exclusion of PII will undermine many of the proposed goals of CARDS, if at all. While FSI highlights some of the elements to consider, this is not an exhaustive list and FSI encourages FINRA to analyze as many elements as possible in order to conduct a thorough and accurate cost-benefit analysis.

- **FINRA Must Proactively Eliminate Duplicative or Unnecessary Requirements Made Obsolete by CARDS:** Because the costs of CARDS will be enormous and will be incurred by clearing firms, broker-dealer firms, individual financial advisors, and ultimately investors, FINRA should proactively identify existing rules and requirements that become unnecessary as a result of CARDS and that can be immediately streamlined or eliminated. FINRA should work to eliminate these requirements before firms must incur the costs associated with CARDS to ensure firms do not incur duplicative costs. This is particularly essential for smaller firms with limited resources that could be put out of business by incurring enormous implementation costs while still complying with duplicative requirements. FSI urges the cost benefit analysis conducted on CARDS to identify these potential areas of overlapping regulation as well as ways in which CARDS data could be provided to firms to benefit their supervision and compliance efforts. FSI has identified some of the potential overlap or duplication of requirements that could be analyzed through a cost-benefit analysis: 1) streamlined examinations; 2) elimination or streamlining of other trade data collection requirements; 3) exception requests; and 4) reduced data requests, such as the Risk Control Assessment Questionnaire currently being utilized by FINRA. To the extent FINRA is able to eliminate other regulatory burdens as a result of CARDS and is able to provide the data to benefit firms' supervision and compliance efforts, this will ease the cost burden of implementing CARDS.
 - *FINRA Should Provide Firms with Data and Analytics to Assist Firms with Surveillance:* FSI suggests that FINRA provide data and analytics to firms that will assist them to conduct surveillance and to detect trends and red flags. This would include normalized client and trade data as well as benchmarking reports. For CARDS to be truly effective, it must leverage its data collection and analytics to enhance firms' surveillance and compliance program. Because many small firms do not have

the scaling ability and technology budget of FINRA and larger firms, CARDS as an initiative can also become an industry tool and surveillance platform in addition to a FINRA-only system.

Answers to Specific Questions:

In addition to the overall concerns outlined previously, FSI welcomes the opportunity to provide responses to the specific questions FINRA included in the request for comment. However, it should be noted that the concept proposal did not contain sufficient specific information about the various aspects of CARDS in order to respond to these requests in detail:

- **Request 1– Alternative methods for achieving FINRA’s goals as articulated in the request for comment:** As proposed, CARDS faces severe challenges that will not only impact the effectiveness of the analysis and collection of data, but will impose serious costs in terms of personnel and information technology infrastructure. These costs and challenges must be viewed in concert with FINRA’s previous data project initiative with respect to variable annuities. The challenges and overall effectiveness of collecting and analyzing data with respect to variable annuities will only be magnified by expanding the universe of information through CARDS. FINRA must assess whether the status-quo, with respect to the collection and analysis of information provided during examinations, can provide the same level of market trend analysis and enhanced examination efficiency. FINRA has been collecting information from firms through piecemeal information requests during examinations for many years, yet it is not clear whether FINRA has attempted to conduct trend and market analysis on this data in the way it envisions with CARDS. Without a precedent to rely upon, firms are skeptical that CARDS’ development challenges and attendant risks with respect to data security and privacy are indeed a net benefit. FINRA already collects a significant amount of information through data feeds, including INSITE and OATS. FINRA should investigate alternatives that would allow it to achieve CARDS’ goals through those systems. In addition, FINRA should release additional information on the effectiveness of the pilot programs it has conducted with respect to this concept proposal, and expand the pilot program to collect additional data and information to inform the development of CARDS. Several additional pilot programs will be necessary to adequately understand the full impacts, particularly if FINRA plans to expand the collection to direct business information.
- **Request 2 – Primary sources of economic impact – cost and benefits:** The concept release does not contain enough specific information about CARDS in order for firms to adequately predict the potential economic impact. In general, FSI expects the economic impacts of CARDS to be unprecedented, particularly if FINRA continues to expand the scope of data collection as suggested in the Regulatory Notice’s discussion of future phases for the initiative. The primary source of economic impact will be increased costs placed on clearing firms. These costs will be passed onto firms, financial advisors, and clients and are likely to be significant. FINRA may determine that the data collected solely through clearing firms gives an incomplete picture of retail account activity, which may require an expansion of CARDS. If this occurs, firms and advisors are likely to see an additional increase in costs if system changes are required for compliance. Another concern is the potential benefits of CARDS. While FSI and members welcome the

exclusion of PII, by not collecting this information FINRA reduces the proposed benefits of the system significantly if the purpose of CARDS is to identify sales practice issues at a client level or across firms at a household level. In addition, if FINRA determines that it will not collect direct business data, it will be excluding a great deal of information with respect to client and firm transactions which will limit its ability to have the necessary full context for its analysis and may result in many false positives. If FINRA does expand into direct business, the costs will be enormous and potentially detrimental to the ability of firms to continue to provide cost-effective financial services to those investors most in need of them. Because clearing firms do not collect this information currently, firms would either have to 1) increase the amount of information they submit to clearing firms, which has a significant costs, or 2) submit the information directly to FINRA in a common data format which will significantly impact the business operations of firms, and may put some small firms out of business. With respect to data normalization, this process will require significant resources and will reduce the usefulness of the information that CARDS collects. FINRA must determine whether the increase in costs is justified in light of the reduction in proposed benefits that these processes introduce.

- **Request 3 – Other than system modifications, what other infrastructure changes would be necessary to implement CARDS:** The development of systems by the clearing firms or introducing firms would require capital investments in new technology systems. Additional staff would likely need to be hired by clearing and introducing firms to effectively operate and maintain these systems, and these additional employees would require training. Because the data from clearing firms would need to be standardized, firms would be required to translate the raw data received through their various pipelines for transmission. This is a costly manual process in many cases and FINRA would be placing this burden on the industry. Firms, however, require more information from FINRA in order to adequately calculate the full costs involved. As FINRA continues to advance the CARDS proposal, it must provide very specific information with respect to the data fields it will require firms to transmit, the data formats, and whether it plans to expand the collection to direct business.
- **Request 4 – Firm reliance upon third parties to fulfill reporting obligations:** FSI does not believe the current proposal provides enough information and specifics about CARDS' requirements to adequately address this request for comment at this time. However, to the extent firms would rely on third parties to fulfill their reporting obligations with regard to CARDS, FINRA should work to establish clear supervisory obligations for firms that enter into these types of agreements with third parties. FINRA should identify areas of overlap with existing reporting and examination requirements and eliminate those instances where CARDS would create a duplicative requirement so firms can potentially reduce their use of personnel and third parties to fulfill those requirements.
- **Request 5 – Suitability information maintained at clearing firms:** CARDS will create significant challenges due to the variety of systems and data standards that firms use to obtain and retain suitability information. As stated above, a significant portion of FSI members that utilize clearing platforms maintain separate proprietary suitability systems and do not submit this information to their clearing firms. The proprietary systems vary by firm, and the data they collect is not in a standardized format. Although a clearing firm's brokerage platform may possess the ability to enter basic suitability information, these data fields are often free

text fields that do not possess the robustness of internal proprietary systems for running queries and quantifying risk. This lack of inter-linkages present a challenge that FINRA would need to resolve in order to capture the sales practice information it desires for running analytics through CARDS.

- **Request 6 – Extent that CARDS data is collected and maintained for all types of products in automated format and/or stored at clearing and self-clearing firms or service bureaus:** As discussed above, firms utilize a variety of different methods for capturing and storing this information. Smaller firms in particular may not automate much of the process at all. Other firms may rely more heavily on the automated data collection process maintained through clearing firm systems.
- **Request 7 – Feasibility and economic impact of a 12-18 month cycle to expand books and records CARDS data:** Using the example set by changes to the data collected for suitability through FINRA Rule 2111, FSI believes that a 12-18 month cycle to expand the books and records collection to additional data is too aggressive. New systems can take several years to create and implement for all existing clients. FSI anticipates the economic impact of future expansions of CARDS data will be significant, and requests that FINRA indicate in future Regulatory Notices the types of data expansion it anticipates would be required by firms. To fully understand the impact of a 12-18 month cycle for books and records expansions, FSI requests that FINRA provide longer lead-times and additional information on future plans for the CARDS system.
- **Request 8 – Cost and benefits of longer or shorter schedules for data submission:** Because the data submission process will be automated, the scheduling of data submission is less important than which actual data is going to be submitted. Whether weekly or nightly, the central concern is the data fields that CARDS will require. Another related concern with respect to the data submission schedule is the opportunity to review the data quality prior to submission. Currently, when firms receive data requests from FINRA during examinations, they are provided an opportunity to ensure that the data is in fact correct prior to submission. With an automated process such as CARDS, however, firms will not have this opportunity unless afforded the time and means to review, change, or access this data. One possible avenue is to utilize longer submission schedules to provide firms sufficient time to review the data prior to submission.
- **Request 9 – Methods for first phase of CARDS to best achieve goal of focusing on business conduct of retail accounts:** FSI suggests that FINRA implement several additional pilot programs to further study the feasibility issues and challenges likely to be faced by CARDS. This pilot program would be the best method to test whether the additional information FINRA envisions capturing in later phases is feasible.
- **Request 10 – Distinguishing between retail and institutional accounts:** FSI members overwhelmingly service retail customer accounts; however, some may have a number of institutional clients. Firms may utilize data fields within their systems to designate between retail institutional accounts. Firms may also query based on account size, however this is an imprecise method. However, firms may have different definitions of institutional accounts. As FINRA makes progress on this issue, it must provide firms with a more specific definition of institutional versus retail accounts to allow firms to adequately respond.
- **Request 11 – Providing data with performance benchmarks:** FSI requests more information from FINRA on the type of data and performance benchmarks that

firms would be receiving if this proposal is implemented. In addition, FSI would request information regarding whether the performance benchmarks would be utilized as part of a voluntary self-assessment or later to impose more requirements on the data submission process.

Conclusion

In conclusion, we believe that CARDS' development and implementation is simply not feasible while preserving widespread investor access to the services of independent broker-dealers and financial advisors. Because of the variety of costs, risks, and other concerns involved, FSI cannot support the creation and implementation of CARDS as currently proposed.

We are committed to constructive engagement in the regulatory process and, therefore, welcome the opportunity to work with FINRA on this and other important regulatory efforts.

Thank you for your consideration of our 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" followed by "Bellaire".

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