

(11) Each Fund will achieve commodities exposure through investment in a Subsidiary, and such investment may not exceed 25% of a Fund's total assets, as measured at the end of every quarter of a Fund's taxable year.

(12) Each Fund may invest up to an aggregate amount of 15% of its net assets in illiquid assets (calculated at the time of investment), including Rule 144A securities deemed illiquid by the Adviser, consistent with Commission guidance.

(13) A minimum of 100,000 Shares for each Fund will be outstanding at the commencement of trading on the Exchange.

The Exchange represents that all statements and representations made in the filing regarding (a) the description of the portfolio, (b) limitations on portfolio holdings or reference assets, or (c) the applicability of Exchange rules and surveillance procedures constitute continued listing requirements for listing the Shares on the Exchange. In addition, the issuer has represented to the Exchange that it will advise the Exchange of any failure by the Funds to comply with the continued listing requirements, and, pursuant to its obligations under Section 19(g)(1) of the Act, the Exchange will monitor for compliance with the continued listing requirements.<sup>39</sup> If a Fund is not in compliance with the applicable listing requirements, the Exchange will commence delisting procedures under NYSE Arca Equities Rule 5.5(m). This approval order is based on all of the Exchange's representations, including those set forth above, in the Notice, and in Amendment Nos. 1, 2, 3, and 4 to the proposed rule change. The Commission notes that the Funds and the Shares must comply with the requirements of NYSE Arca Equities Rule 8.600, including those set forth in this proposed rule change, to be listed and traded on the Exchange on an initial and continuing basis.

For the foregoing reasons, the Commission finds that the proposed rule change, as modified by Amendment

<sup>39</sup> The Commission notes that certain other proposals for the listing and trading of managed fund shares include a representation that the exchange will "surveil" for compliance with the continued listing requirements. *See, e.g.*, Amendment No. 2 to SR-BATS-2016-04, available at: <http://www.sec.gov/comments/sr-bats-2016-04/bats201604-2.pdf>. In the context of this representation, it is the Commission's view that "monitor" and "surveil" both mean ongoing oversight of the Fund's compliance with the continued listing requirements. Therefore, the Commission does not view "monitor" as a more or less stringent obligation than "surveil" with respect to the continued listing requirements.

Nos. 1, 2, 3, and 4 thereto, is consistent with Section 6(b)(5) of the Act<sup>40</sup> and Section 11A(a)(1)(C)(iii) of the Act<sup>41</sup> and the rules and regulations thereunder applicable to a national securities exchange.

#### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>42</sup> that the proposed rule change (SR-NYSEArca-2015-107), as modified by Amendment Nos. 1, 2, 3, and 4 thereto, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>43</sup>

**Robert W. Errett,**  
*Deputy Secretary.*

[FR Doc. 2016-07511 Filed 4-1-16; 8:45 am]

**BILLING CODE 8011-01-P**

### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-77465; File No. SR-FINRA-2015-056]

#### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Instituting Proceedings To Determine Whether to Approve or Disapprove Proposed Rule Change To Adopt FINRA Rule 2030 and FINRA Rule 4580 to Establish "Pay-To-Play" and Related Rules

March 29, 2016.

#### I. Introduction

On December 16, 2015, Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act," "Exchange Act" or "SEA")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to adopt FINRA Rules 2030 (Engaging in Distribution and Solicitation Activities with Government Entities) and 4580 (Books and Records Requirements for Government Distribution and Solicitation Activities) to establish "pay-to-play"<sup>3</sup> and related rules that would regulate the activities of member

firms that engage in distribution or solicitation activities for compensation with government entities on behalf of investment advisers.

The proposed rule change was published for comment in the **Federal Register** on December 30, 2015.<sup>4</sup> The Commission received ten comment letters, from nine different commenters, in response to the proposed rule change.<sup>5</sup> On February 8, 2016, FINRA extended the time period in which the Commission must approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change to March 29, 2016.<sup>6</sup> On March 28, 2016, FINRA filed a letter with the Commission stating that it has considered the comments received by the Commission, and that FINRA is not intending to make changes to the proposed rule text in response to the comments.<sup>7</sup> The Commission is publishing this order to institute proceedings pursuant to Exchange Act Section 19(b)(2)(B)<sup>8</sup> to determine whether to approve or disapprove the proposed rule change.

Institution of proceedings does not indicate that the Commission has

<sup>4</sup> See Exchange Act Rel. No. 76767 (Dec. 24, 2015), 80 FR 81650 (Dec. 30, 2015) (File No. SR-FINRA-2015-056) ("Notice").

<sup>5</sup> See Letters from David Keating, President, Center for Competitive Politics ("CCP"), dated Jan. 20, 2016 ("CCP Letter"); Clifford Kirsch and Michael Koffler, Sutherland Asbill & Brennan LLP, for the Committee of Annuity Insurers ("CAI"), dated Jan. 20, 2016 ("CAI Letter No. 1"); Clifford Kirsch and Michael Koffler, Sutherland Asbill & Brennan LLP, for the CAI, dated Feb. 5, 2016 ("CAI Letter No. 2"); David T. Bellaire, Executive Vice President and General Counsel, Financial Services Institute ("FSI"), dated Jan. 20, 2016 ("FSI Letter"); Tamara K. Salmon, Assistant General Counsel, Investment Company Institute ("ICI"), dated Jan. 20, 2016 ("ICI Letter"); Patrick J. Moran, Esq., dated Dec. 29, 2015 ("Moran Letter"); Gary A. Sanders, Counsel and Vice President, National Association of Insurance and Financial Advisors ("NAIFA"), dated Jan. 20, 2016 ("NAIFA Letter"); Judith M. Shaw, President, North American Securities Administrators Association, Inc. ("NASAA"), dated Jan. 20, 2016 ("NASAA Letter"); Hugh D. Berkson, President, Public Investors Arbitration Bar Association ("PIABA"), dated Jan. 20, 2016 ("PIABA Letter"); and H. Christopher Bartolomucci and Brian J. Field, Bancroft PLLC, for the New York Republican State Committee and the Tennessee Republican Party ("State Parties"), dated Jan. 20, 2016 ("State Parties Letter").

<sup>6</sup> See Letter from Victoria Crane, Associate General Counsel, FINRA, to Lourdes Gonzalez, Assistant Director, Sales Practices, Division of Trading and Markets, Securities and Exchange Commission, dated Feb. 8, 2016.

<sup>7</sup> See Letter from Victoria Crane, Associate General Counsel, FINRA, to Brent J. Fields, Secretary, Securities and Exchange Commission, dated Mar. 28, 2016 ("FINRA Response Letter"). The FINRA Letter is available on FINRA's Web site at <http://www.finra.org>, at the principal office of FINRA, and at the Commission's Public Reference Room.

<sup>8</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>40</sup> 15 U.S.C. 78f(b)(5).

<sup>41</sup> 15 U.S.C. 78k-1(a)(1)(C)(iii).

<sup>42</sup> 15 U.S.C. 78s(b)(2).

<sup>43</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> "Pay-to-play" practices typically involve a person making cash or in-kind political contributions (or soliciting or coordinating others to make such contributions) to help finance the election campaigns of state or local officials or bond ballot initiatives as a quid pro quo for the receipt of government contracts.

reached any conclusions with respect to the proposed rule change, nor does it mean that the Commission will ultimately disapprove the proposed rule change. Rather, as discussed below, the Commission seeks additional input on the proposed rule change and issues presented by the proposal.

## II. Description of the Proposed Rule Change<sup>9</sup>

As described more fully in the Notice, FINRA is proposing a pay-to-play rule, Rule 2030,<sup>10</sup> that FINRA states is modeled on the Commission's Rule 206(4)–5 under the Investment Advisers Act of 1940 (“Advisers Act”), which addresses pay-to-play practices by investment advisers (the “SEC Pay-to-Play Rule”).<sup>11</sup> The SEC Pay-to-Play Rule, among other things, prohibits an investment adviser and its covered associates from providing or agreeing to provide, directly or indirectly, payment to any person to solicit a government entity for investment advisory services on behalf of the investment adviser unless the person is a “regulated person.”<sup>12</sup> A “regulated person,” as defined in the SEC Pay-to-Play Rule, includes a FINRA member firm, provided that: (a) FINRA rules prohibit member firms from engaging in distribution or solicitation activities if political contributions have been made; and (b) the SEC finds, by order, that such rules impose substantially equivalent or more stringent restrictions on member firms than the SEC Pay-to-Play Rule imposes on investment advisers and that such rules are consistent with the objectives of the SEC Pay-to-Play Rule.<sup>13</sup> Therefore, based on this regulatory framework, FINRA is proposing its own pay-to-play rule to enable its member firms to continue to

engage in distribution and solicitation activities for compensation with government entities on behalf of investment advisers, while at the same time deterring its member firms from engaging in pay-to-play practices.<sup>14</sup> FINRA also believes that its proposed rule would establish a comprehensive regime to regulate the activities of its member firms that engage in distribution or solicitation activities with government entities on behalf of investment advisers and would impose substantially equivalent restrictions on FINRA member firms engaging in distribution or solicitation activities to those the SEC Pay-to-Play Rule imposes on investment advisers.<sup>15</sup>

Furthermore, FINRA is proposing Rule 4580, which would impose recordkeeping requirements on FINRA member firms in connection with its pay-to-play rule that would allow examination of member firms' books and records for compliance with the pay-to-play rule.<sup>16</sup> FINRA believes that its proposed Rule 4580 is consistent with similar recordkeeping requirements imposed on investment advisers in connection with the SEC Pay-to-Play Rule.<sup>17</sup>

The following is an overview of some of the key provisions in FINRA's proposed rules.

### A. Proposed Rule 2030(a): Limitation on Distribution and Solicitation Activities

Proposed Rule 2030(a) would prohibit a covered member from engaging in distribution or solicitation activities for compensation with a government entity on behalf of an investment adviser that provides or is seeking to provide investment advisory services to such government entity within two years after a contribution to an official of the government entity is made by the covered member or a covered associate, including a person who becomes a covered associate within two years after the contribution is made.<sup>18</sup> FINRA states that the terms and scope of the prohibitions in proposed Rule 2030(a) are modeled on the SEC Pay-to-Play Rule.<sup>19</sup>

FINRA explains that proposed Rule 2030(a) would not ban or limit the amount of political contributions a covered member or its covered associates could make.<sup>20</sup> Rather, FINRA

states that, consistent with the SEC Pay-to-Play Rule, the proposed rule would impose a two-year “time out” on engaging in distribution or solicitation activities for compensation with a government entity on behalf of an investment adviser after the covered member or its covered associates make a contribution to an official of the government entity.<sup>21</sup> According to FINRA, the two-year time out period is intended to discourage covered members from participating in pay-to-play practices by requiring a cooling-off period during which the effects of a political contribution on the selection process can be expected to dissipate.<sup>22</sup>

### 1. Distribution Activities

FINRA states that, based on the definition of “regulated person” in the SEC Pay-to-Play Rule, it is required to adopt a rule that prohibits its member firms from engaging in distribution activities (as well as solicitation activities) with government entities if political contributions have been made.<sup>23</sup> FINRA also notes that certain language in the SEC Pay-to-Play Rule Adopting Release further supports the inclusion of distribution activities by broker-dealers in a FINRA pay-to-play rule.<sup>24</sup>

However, FINRA also explains that, based on the definition of a “covered investment pool” in proposed Rule 2030(g)(3),<sup>25</sup> the proposed rule would not apply to distribution activities related to registered investment companies that are not investment options of a government entity's plan or program.<sup>26</sup> Therefore, the proposed rule would apply to distribution activities involving unregistered pooled

<sup>21</sup> See *id.*

<sup>22</sup> *Id.*

<sup>23</sup> See *id.* at 81660–61 (explaining that FINRA believes its proposed rule must apply to member firms engaging in distribution activities and that FINRA did not revise the proposed rule to remove references to the term distribution as requested by comments received in response to *Regulatory Notice 14–50*).

<sup>24</sup> See *id.* at 81660–61 (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41040 n. 298 where, according to FINRA, the Commission “clarif[ied] under what circumstances distribution payments would violate the SEC's Pay-to-Play Rule”).

<sup>25</sup> See *id.* at 81654, n. 46 (proposed Rule 2030(g)(3) defines a “covered investment pool” to mean: “(A) Any investment company registered under the Investment Company Act that is an investment option of a plan or program of a government entity, or (B) Any company that would be an investment company under Section 3(a) of the Investment Company Act but for the exclusion provided from that definition by either Section 3(c)(1), 3(c)(7) or 3(c)(11) of that Act”).

<sup>26</sup> See Notice, 80 FR at 81661, nn. 105–106 (explaining that the proposed rule would not apply to distribution activities relating to all registered pooled investment vehicles).

<sup>9</sup> The proposed rule change, as described in this Item II, is excerpted, in part, from the Notice, which was substantially prepared by FINRA. See *supra* note 4.

<sup>10</sup> See Notice, 80 FR at 81650–51 (citing Advisers Act Release No. 3043 (July 1, 2010), 75 FR 41018 (July 14, 2010) (Political Contributions by Certain Investment Advisers) (“SEC Pay-to-Play Rule Adopting Release”).

<sup>11</sup> FINRA also published the proposed rule change in *Regulatory Notice 14–50* (Nov. 2014) (“*Regulatory Notice 14–50*”) and sought comment on the proposal. FINRA states that commenters were generally supportive of the proposed rule change, but also expressed some concerns. As such, FINRA revised the proposed rule change as published in *Regulatory Notice 14–50* in response to those comments. As described more fully in the Notice, FINRA believes that the revisions it made more closely align FINRA's proposed rule with the SEC Pay-to-Play Rule and help reduce cost and compliance burden concerns raised by commenters. See Notice, 80 FR at 81651, n. 16.

<sup>12</sup> See Notice, 80 FR at 81650, 81656. See also SEC Pay-to-Play Rule 206(4)–5(a)(2)(i)(A).

<sup>13</sup> See Notice, 80 FR at 81650, n. 6 (citing SEC Pay-to-Play Rule 206(4)–5(f)(9)).

<sup>14</sup> See Notice, 80 FR at 81651, 81656.

<sup>15</sup> See *id.* at 81651, 81656.

<sup>16</sup> See *id.* at 81651, 81655–56.

<sup>17</sup> See *id.* at 81655, n. 60 (citing Advisers Act Rule 204–2(a)(18) and (h)(1)).

<sup>18</sup> See Notice, 80 FR at 81651.

<sup>19</sup> See *id.* (citing SEC Pay-to-Play Rule 206(4)–5(a)(1)).

<sup>20</sup> See Notice, 80 FR at 81651.

investment vehicles such as hedge funds, private equity funds, venture capital funds, and collective investment trusts, and registered pooled investment vehicles such as mutual funds, but only if those registered pools are an investment option of a participant-directed plan or program of a government entity.<sup>27</sup> FINRA also notes that, consistent with the SEC Pay-to-Play Rule, to the extent mutual fund distribution fees are paid by the fund pursuant to a 12b-1 plan, such payments would not be prohibited under the proposed rule as they would not constitute payments by the fund's investment adviser.<sup>28</sup> However, if the adviser pays for the fund's distribution out of its "legitimate profits," the proposed rule would generally be implicated.<sup>29</sup>

## 2. Solicitation Activities

FINRA also states that, consistent with the SEC Pay-to-Play Rule, proposed Rule 2030(g)(1) defines the term "solicit" to mean: "(A) With respect to investment advisory services, to communicate, directly or indirectly, for the purpose of obtaining or retaining a client for, or referring a client to, an investment adviser; and (B) With respect to a contribution or payment, to communicate, directly or indirectly, for the purpose of obtaining or arranging a contribution or payment."<sup>30</sup> FINRA also notes that, although the determination of whether a particular communication would be a solicitation would depend on the facts and circumstances relating to such communication, as a general proposition FINRA believes that any communication made under circumstances reasonably calculated to obtain or retain an advisory client would be considered a solicitation unless the circumstances otherwise indicate that the communication does not have the purpose of obtaining or retaining an advisory client.<sup>31</sup>

### B. Proposed Rule 2030(b): Prohibition on Soliciting and Coordinating Contributions

Proposed Rule 2030(b) would also prohibit a covered member or covered associate from coordinating or soliciting any person or political action committee (PAC) to make any: (1) Contribution to

an official of a government entity in respect of which the covered member is engaging in, or seeking to engage in, distribution or solicitation activities on behalf of an investment adviser; or (2) payment to a political party of a state or locality of a government entity with which the covered member is engaging in, or seeking to engage in, distribution or solicitation activities on behalf of an investment adviser.<sup>32</sup> FINRA states that this provision is modeled on a similar provision in the SEC Pay-to-Play Rule<sup>33</sup> and is intended to prevent covered members or covered associates from circumventing the proposed rule's prohibition on direct contributions to certain elected officials such as by "bundling" a large number of small employee contributions to influence an election, or making contributions (or payments) indirectly through a state or local political party.<sup>34</sup>

### C. Proposed Rule 2030(c): Exceptions

FINRA's proposed pay-to-play rule contains three exceptions from the proposed rule's prohibitions: (1) *De minimis* contributions, (2) new covered associates, and (3) certain returned contributions.<sup>35</sup> FINRA states that these exceptions are modeled on similar exceptions in the SEC Pay-to-Play Rule.<sup>36</sup>

#### 1. De Minimis Contribution Exception

Proposed Rule 2030(c)(1) would except from the rule's restrictions contributions made by a covered associate who is a natural person to government entity officials for whom the covered associate was entitled to vote at the time of the contributions, provided the contributions do not exceed \$350 in the aggregate to any one official per election.<sup>37</sup> However, if the covered associate was not entitled to vote for the official at the time of the contribution, the contribution must not exceed \$150 in the aggregate per election.<sup>38</sup> FINRA states that, consistent with the SEC Pay-to-Play Rule, under this exception, primary and general elections would be considered separate elections.<sup>39</sup> FINRA also explains that this exception is based on the theory that such contributions are typically made without the intent or ability to

influence the selection process of the investment adviser.<sup>40</sup>

#### 2. Exception for Certain New Covered Associates

The proposed rule would attribute to a covered member contributions made by a person within two years (or, in some cases, six months) of becoming a covered associate. However, proposed Rule 2030(c)(2) would provide an exception from the proposed rule's restrictions for covered members if a natural person made a contribution more than six months prior to becoming a covered associate of the covered member unless the covered associate engages in, or seeks to engage in, distribution or solicitation activities with a government entity on behalf of the covered member.<sup>41</sup> FINRA states that this exception is consistent with the SEC Pay-to-Play Rule<sup>42</sup> and is intended to balance the need for covered members to be able to make hiring decisions against the need to protect against individuals marketing to prospective employers their connections to, or influence over, government entities the employer might be seeking as clients.<sup>43</sup> FINRA also provides, with respect to the "look back" provisions in the proposed rules generally, the following illustrations of how the "look back" provisions work: if, for example, the contributions were made more than two years (or six months for new covered associates) prior to the employee becoming a covered associate, the time out has run.<sup>44</sup> According to FINRA, however, if the contribution was made less than two years (or six months, as applicable) from the time the person becomes a covered associate, the proposed rule would prohibit the covered member that hires or promotes the contributing covered associate from receiving compensation for engaging in distribution or solicitation activities on behalf of an investment adviser from the hiring or promotion date until the applicable period has run.<sup>45</sup> FINRA also states that the "look back" provisions are designed to prevent covered members from circumventing the rule by influencing the selection process by hiring persons who have made political contributions.<sup>46</sup>

<sup>27</sup> See *id.* at 81661. See also *id.* at 81651, n. 17 and 81654, n. 46.

<sup>28</sup> See *id.* at 81661.

<sup>29</sup> See *id.* (noting, among other things, that "for private funds, third parties are often compensated by the investment adviser or its affiliated general partner").

<sup>30</sup> See *id.* at 81651, n. 18. See also *id.* at 81653, n. 40.

<sup>31</sup> See *id.*

<sup>32</sup> See *id.* at 81654. See also *id.* at 81662.

<sup>33</sup> See *id.* at 81654 (citing SEC Pay-to-Play Rule 206(4)-5(a)(2)).

<sup>34</sup> See Notice, 80 FR at 81654.

<sup>35</sup> See *id.*

<sup>36</sup> See *id.* (citing SEC Pay-to-Play Rule 206(4)-5(b)).

<sup>37</sup> See Notice, 80 FR at 81655.

<sup>38</sup> See *id.*

<sup>39</sup> See *id.* (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41034).

<sup>40</sup> See Notice, 80 FR at 81655.

<sup>41</sup> See *id.*

<sup>42</sup> See *id.* (citing SEC Pay-to-Play Rule 206(4)-5(b)(2)).

<sup>43</sup> See Notice, 80 FR at 81655.

<sup>44</sup> See *id.*

<sup>45</sup> See *id.*

<sup>46</sup> See *id.* at 81653, 81655.

### 3. Exception for Certain Returned Contributions

Proposed Rule 2030(c)(3) would provide an exception from the proposed rule's restrictions for covered members if the restriction is due to a contribution made by a covered associate and: (1) The covered member discovered the contribution within four months of it being made; (2) the contribution was less than \$350; and (3) the contribution is returned within 60 days of the discovery of the contribution by the covered member.<sup>47</sup> FINRA explains that, consistent with the SEC Pay-to-Play Rule, this exception would allow a covered member to cure the consequences of an inadvertent political contribution.<sup>48</sup> The proposed rule would also provide that covered members with 150 or fewer registered representatives would be able to rely on this exception no more than two times per calendar year, while covered members with more than 150 registered representatives would be permitted to rely on this exception no more than three times per calendar year.<sup>49</sup> Furthermore, a covered member would not be able to rely on an exception more than once with respect to contributions by the same covered associate regardless of the time period, which is consistent with similar provisions in the SEC Pay-to-Play Rule.<sup>50</sup>

### D. Proposed Rule 2030(d): Prohibitions as Applied to Covered Investment Pools

Proposed Rule 2030(d)(1) provides that a covered member that engages in distribution or solicitation activities with a government entity on behalf of a covered investment pool<sup>51</sup> in which a government entity invests or is solicited to invest shall be treated as though the covered member was engaging in or seeking to engage in distribution or solicitation activities with the government entity on behalf of the investment adviser to the covered

investment pool directly.<sup>52</sup> Proposed Rule 2030(d)(2) provides that an investment adviser to a covered investment pool in which a government entity invests or is solicited to invest shall be treated as though that investment adviser were providing or seeking to provide investment advisory services directly to the government entity.<sup>53</sup> FINRA states that proposed Rule 2030(d) is modeled on a similar prohibition in the SEC Pay-to-Play Rule and would apply the prohibitions of the proposed rule to situations in which an investment adviser manages assets of a government entity through a hedge fund or other type of pooled investment vehicle.<sup>54</sup> Therefore, according to FINRA, the provision would extend the protection of the proposed rule to public pension plans that access the services of investment advisers through hedge funds and other types of pooled investment vehicles sponsored or advised by investment advisers as a funding vehicle or investment option in a government-sponsored plan, such as a 529 plan.<sup>55</sup>

### E. Proposed Rule 2030(e): Prohibition on Indirect Contributions or Solicitations

Proposed Rule 2030(e) provides that it shall be a violation of Rule 2030 for any covered member or any of its covered associates to do anything indirectly that, if done directly, would result in a violation of the rule.<sup>56</sup> FINRA states that this provision is consistent with a similar provision in the SEC Pay-to-Play Rule<sup>57</sup> and would prevent a covered member or its covered associates from funneling payments through third parties, including, for example, consultants, attorneys, family members, friends or companies affiliated with the covered member as a means to

circumvent the proposed rule.<sup>58</sup> FINRA also notes that, consistent with guidance provided by the SEC in connection with SEC Pay-to-Play Rule 206(4)–5(d), proposed Rule 2030(e) would require a showing of intent to circumvent the rule in order for such persons to trigger the two-year “time out.”<sup>59</sup>

### F. Proposed Rule 2030(f): Exemptions

Proposed Rule 2030(f) includes an exemptive provision for covered members, modeled on the exemptive provision in the SEC Pay-to-Play Rule, that would allow covered members to apply to FINRA for an exemption from the proposed rule's two-year time out.<sup>60</sup> As proposed, FINRA states that this provision would allow FINRA to exempt covered members, either conditionally or unconditionally, from the proposed rule's time out requirement where the covered member discovers contributions that would trigger the compensation ban after they have been made, and when imposition of the prohibition would be unnecessary to achieve the rule's intended purpose.<sup>61</sup> In determining whether to grant an exemption, FINRA would take into account varying facts and circumstances, outlined in the proposed rule, that each application presents (*e.g.*, the timing and amount of the contribution, the nature of the election, and the contributor's apparent intent or motive in making the contribution).<sup>62</sup> FINRA notes that this provision would provide covered members with an additional avenue by which to seek to cure the consequences of an inadvertent violation by the covered member or its covered associates that falls outside the limits of one of the proposed rule's exceptions.<sup>63</sup>

### G. Proposed Rule 2030(g): Definitions

The following is an overview of some of the key definitions in FINRA's proposed rules.

#### 1. Contributions

Proposed Rule 2030(g)(1) defines “contribution” to mean any gift, subscription, loan, advance, deposit of money, or anything of value made for the purpose of influencing the election for a federal, state or local office, and includes any payments for debts incurred in such an election or

<sup>47</sup> See *id.* at 81655.

<sup>48</sup> See *id.*

<sup>49</sup> See *id.* FINRA notes that these limitations are consistent with similar provisions in the SEC Pay-to-Play Rule 206(4)–5(b)(3), although the SEC Pay-to-Play Rule includes different allowances for larger and smaller investment advisers based on the number of employees they report on Form ADV. See *id.* at 81655, n. 59.

<sup>50</sup> See Notice, 80 FR at 81655.

<sup>51</sup> See *id.* at 81654, n. 46 (proposed Rule 2030(g)(3) defines a “covered investment pool” to mean: “(A) Any investment company registered under the Investment Company Act that is an investment option of a plan or program of a government entity, or (B) Any company that would be an investment company under Section 3(a) of the Investment Company Act but for the exclusion provided from that definition by either Section 3(c)(1), 3(c)(7) or 3(c)(11) of that Act”).

<sup>52</sup> See Notice, 80 FR at 81654, n. 47 (FINRA notes that, consistent with the SEC Pay-to-Play Rule, under the proposed rule, if a government entity is an investor in a covered investment pool at the time a contribution triggering a two-year time out is made, the covered member must forgo any compensation related to the assets invested or committed by the government entity in the covered investment pool) (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41047).

<sup>53</sup> See Notice, 80 FR at 81654, n. 48 (FINRA states that it added proposed Rule 2030(d)(2) in response to comments on *Regulatory Notice* 14–50 to clarify, for purposes of the proposed rule, the relationship between an investment adviser to a covered investment pool and a government entity that invests in the covered investment pool).

<sup>54</sup> See *id.* at 81654 (citing SEC Pay-to-Play Rule 206(4)–5(c)).

<sup>55</sup> See Notice, 80 FR at 81654 (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41044, which discusses the applicability of the SEC Pay-to-Play Rule to covered investment pools).

<sup>56</sup> See Notice, 80 FR at 81654.

<sup>57</sup> See *id.* (citing SEC Pay-to-Play Rule 206(4)–5(d)).

<sup>58</sup> See Notice, 80 FR at 81654 (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41044, which discusses direct and indirect contributions or solicitations).

<sup>59</sup> See Notice, 80 FR at 81654.

<sup>60</sup> See *id.* at 81654–55.

<sup>61</sup> See *id.* at 81655.

<sup>62</sup> See *id.*

<sup>63</sup> See *id.*

transition or inaugural expenses incurred by a successful candidate for state or local office.<sup>64</sup> FINRA states that this definition is consistent with the SEC Pay-to-Play Rule.<sup>65</sup> FINRA also states that it would not consider a donation of time by an individual to be a contribution, provided the covered member has not solicited the individual's efforts and the covered member's resources, such as office space and telephones, are not used.<sup>66</sup> FINRA further states that it would not consider a charitable donation made by a covered member to an organization that qualifies for an exemption from federal taxation under the Internal Revenue Code, or its equivalent in a foreign jurisdiction, at the request of an official of a government entity to be a contribution for purposes of the proposed rule.<sup>67</sup>

## 2. Covered Associates

Proposed Rule 2030(g)(2) defines the term "covered associates" to mean: "(A) Any general partner, managing member or executive officer of a covered member, or other individual with a similar status or function; (B) Any associated person of a covered member who engages in distribution or solicitation activities with a government entity for such covered member; (C) Any associated person of a covered member who supervises, directly or indirectly, the government entity distribution or solicitation activities of a person in subparagraph (B) above; and (D) Any political action committee controlled by a covered member or a covered associate."<sup>68</sup> FINRA states that, as also noted in the SEC Pay-to-Play Rule Adopting Release, contributions made to influence the selection process are typically made not by the firm itself, but by officers and employees of the firm who have a direct economic stake in the business relationship with the government client.<sup>69</sup> For example, contributions by an "executive officer of a covered member" (as defined in proposed Rule 2030(g)(5)) would trigger the two-year time out.<sup>70</sup> FINRA also notes that whether a person is an executive officer would depend on his or her function or activities and not his or her title.<sup>71</sup> In addition, FINRA states that a covered associate would include a PAC controlled by the covered

member or any of its covered associates, as a PAC is often used to make political contributions.<sup>72</sup> FINRA explains that it would consider a "covered member" (as defined in proposed Rule 2030(g)(4)) or its covered associates to have "control" over a PAC if the covered member or covered associate has the ability to direct or cause the direction of governance or operations of the PAC.<sup>73</sup>

## 3. Official of a Government Entity

FINRA explains that an "official" (as defined in proposed Rule 2030(g)(8)) of a "government entity" (as defined in proposed Rule 2030(g)(7))—both of which FINRA states are consistent with the SEC Pay-to-Play Rule definitions—would include an incumbent, candidate or successful candidate for elective office of a government entity if the office is directly or indirectly responsible for, or can influence the outcome of, the hiring of an investment adviser or has authority to appoint any person who is directly or indirectly responsible for, or can influence the outcome of, the hiring of an investment adviser.<sup>74</sup> FINRA also explains that government entities would include all state and local governments, their agencies and instrumentalities, and all public pension plans and other collective government funds, including participant-directed plans such as 403(b), 457, and 529 plans.<sup>75</sup>

FINRA further states that the two-year time out would be triggered by contributions, not only to elected officials who have legal authority to hire the adviser, but also to elected officials (such as persons with appointment authority) who can influence the hiring of the adviser.<sup>76</sup> FINRA notes that it is the scope of authority of the particular office of an official, not the influence actually exercised by the individual that would determine whether the individual has influence over the awarding of an investment advisory contract under the definition.<sup>77</sup>

## H. Proposed Rule 4580: Recordkeeping Requirements

Proposed Rule 4580 would require covered members that engage in distribution or solicitation activities with a government entity on behalf of any investment adviser that provides or is seeking to provide investment advisory services to such government entity to maintain books and records

that would allow FINRA to examine for compliance with its pay-to-play rule.<sup>78</sup> FINRA states that this provision is consistent with similar recordkeeping requirements imposed on investment advisers in connection with the SEC Pay-to-Play Rule.<sup>79</sup> The proposed rule would also require covered members to maintain a list or other record of certain specific information.<sup>80</sup> FINRA states that the proposed rule would, among other things, require that the direct and indirect contributions or payments made by the covered member or any of its covered associates be listed in chronological order and indicate the name and title of each contributor and each recipient of the contribution or payment, as well as the amount and date of each contribution or payment, and whether the contribution was the subject of the exception for returned contributions in proposed Rule 2030.<sup>81</sup>

## III. Summary of Comments

As noted above, the Commission received ten comment letters, from nine different commenters, on the proposed rule change.<sup>82</sup> Six commenters generally expressed support for FINRA's proposal.<sup>83</sup> However, five of those commenters, while generally expressing support for the goals of the proposal, also raised certain concerns regarding various aspects of the proposal as drafted and recommended amendments to the proposal.<sup>84</sup> The other three commenters did not support the proposed rule as drafted based largely on concerns involving the First Amendment to the U.S. Constitution.<sup>85</sup> These comments are summarized below.<sup>86</sup> On March 28, 2016, FINRA filed a letter with the Commission stating that it has considered the comments received by the Commission, and that FINRA is not intending to make

<sup>78</sup> See Notice, 80 FR at 81655.

<sup>79</sup> See *id.* (citing Advisers Act Rule 204-2(a)(18) and (h)(1)).

<sup>80</sup> See Notice, 80 FR at 81655-56.

<sup>81</sup> See *id.*

<sup>82</sup> See *supra* note 5. CAI submitted two separate comment letters. See CAI Letter No. 1 and CAI Letter No. 2.

<sup>83</sup> See CAI Letter No. 1; CAI Letter No. 2; FSI Letter; ICI Letter; NAIFA Letter; NASAA Letter; and PIABA Letter.

<sup>84</sup> See CAI Letter No. 1; CAI Letter No. 2; FSI Letter; NAIFA Letter; NASAA Letter; and PIABA Letter. ICI did not raise additional concerns, but states that it is satisfied with FINRA's revisions and responses to the proposal as drafted in *Regulatory Notice* 14-50. See ICI Letter.

<sup>85</sup> See CCP Letter; Moran Letter; and State Parties Letter.

<sup>86</sup> For further detail, the comments that the Commission received on the Notice are available on the Commission's Web site at <http://www.sec.gov/comments/sr-finra-2015-056/finra2015056.shtml>.

<sup>64</sup> See *id.* at 81652.

<sup>65</sup> See *id.*

<sup>66</sup> See *id.* (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41030).

<sup>67</sup> See Notice, 80 FR at 81652.

<sup>68</sup> *Id.* at 81653, n. 37.

<sup>69</sup> See *id.* (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41031).

<sup>70</sup> See Notice, 80 FR at 81653.

<sup>71</sup> See *id.*

<sup>72</sup> See *id.*

<sup>73</sup> See *id.*

<sup>74</sup> See *id.* at 81652.

<sup>75</sup> See *id.*

<sup>76</sup> See *id.*

<sup>77</sup> See *id.* (citing SEC Pay-to-Play Rule Adopting Release, 75 FR 41018, 41029 (discussing the terms "official" and "government entity")).

changes to the proposed rule text in response to the comments.<sup>87</sup>

#### A. First Amendment Comments

As noted above, three commenters oppose the proposed rule as drafted based on First Amendment concerns.<sup>88</sup> One commenter simply noted that he thinks FINRA may have some First Amendment issues and suggested that FINRA consider raising the amount and restricted political donations limitations to Congressional committee members that might influence government decision-making in the relevant area.<sup>89</sup>

Another commenter urged the Commission to reject FINRA's proposal because, according to that commenter, it impermissibly restricts core political speech in violation of the First Amendment.<sup>90</sup> As more fully explained in the commenter's letter, this commenter makes the following general arguments in support of its position: (1) That FINRA's proposal is not narrowly tailored to achieve a compelling government interest and thus cannot survive First Amendment scrutiny and (2) that the Commission should examine FINRA's proposal on its own merits and should not take comfort from the opinion of the United States Court of Appeals for the DC Circuit in *Blount v. SEC*, 61 F.3d 938 (D.C. Cir. 1995), which upheld MSRB's Rule G-37 against a First Amendment challenge.<sup>91</sup> More specifically, this commenter also makes the following arguments regarding FINRA's proposal, including that: (i) The proposed contributions limits are too low to allow citizens to exercise their constitutional right to participate in the political process; (ii) the rule discriminates between contributions to a candidate for whom an individual is entitled to vote and other candidates and cannot be squared with the Supreme Court's decision in *McCutcheon v. FEC*, 134 S. Ct. 1434 (2014); (iii) FINRA did not consider less restrictive alternatives; (iv) the "look-back" provisions are overbroad and insufficiently tailored to support the governmental interest claimed to be served by these rules; (v) the rules are preempted, with respect to federal elections, by the Federal Election Campaign Act; (vi) the rules are impermissibly vague and overbroad; and (vii) the rules are overbroad as applied to independent broker-dealers

and their registered representatives who operate as independent contractors because they are not tailored to the manner in which services are provided by financial advisors in the independent broker-dealer model.<sup>92</sup>

Similarly, another commenter opposes FINRA's proposed rule, stating that the proposal is unlawful and unconstitutional.<sup>93</sup> This commenter makes the following general arguments in support of its position. First, the commenter claims that the proposal is unlawful as it is *ultra vires* because Congress did not empower entities like FINRA—nor agencies like the SEC—to regulate federal political contributions and the proposal is a direct effort to deter member firms and their employees from engaging in conduct that is protected by the First Amendment and permitted by federal statute.<sup>94</sup> As more fully explained in the commenter's letter, this commenter makes the following claims in support of its argument, including that: (i) Campaign finance regulation has long been the exclusive province of Congress and the Federal Election Commission; (ii) Congress' comprehensive regime of political contribution limits forecloses FINRA's effort to regulate the same conduct; and (iii) even assuming Congress' contribution limits regime does not preclude FINRA from enacting its own rules, the proposal exceeds FINRA's authority to issue rules "designed to prevent fraudulent and manipulative acts and practices[.]"<sup>95</sup> Second, the commenter also claims that the proposal violates the First Amendment.<sup>96</sup> In support of this argument, the commenter states that FINRA cannot show that the proposal's restrictions are necessary to further a sufficiently important interest, and do so in a sufficient tailored manner.<sup>97</sup> As more fully explained in the commenter's letter, this commenter makes the following claims in support of its argument, including that: (i) The proposal severely burdens First Amendment rights and, therefore, FINRA bears an exceedingly high burden in establishing the constitutionality of the proposal; (ii) FINRA openly acknowledges that its proposal is a broad prophylactic measure that deters constitutionally protected conduct even when the

government has no legitimate interest in doing so; (iii) the *Blount* opinion overlooked the disparate impact that a restriction like the FINRA proposal has on candidates; and (iv) the *Blount* opinion also did not discuss the constitutionality of anything comparable to the FINRA proposal's prohibition on coordinating or soliciting contributions "to a political party of a State or locality where the investment adviser is providing or seeking to provide investment advisory services to a government entity."<sup>98</sup>

Although not expressly opposing the proposed rules on First Amendment grounds, two other commenters also raise First Amendment comments.<sup>99</sup> One of these commenters submits that Rule 2030 is not closely drawn in terms of the conduct it prohibits, the persons who are subject to its restrictions, and the circumstances in which it is triggered.<sup>100</sup> This commenter claims that the proposed rule's ambiguity may contravene one of the "key animating principles of the Commission in crafting the [SEC Pay-to-Play Rule]" which, according to the commenter, was to ensure its rule was narrowly tailored to serve a compelling governmental interest, namely, the elimination of pay-to-play practices by investment advisers by preventing fraudulent acts and practices in the market for the provision of investment advisory services to government entities.<sup>101</sup> Another commenter states that the proposed rules may "inadvertently capture activity that does not present the risk of *quid pro quo* corruption," and this commenter believes that FINRA must "define the contours of its proposal as clearly and distinctly as possible to avoid an unnecessary limitation on one's First Amendment rights, especially in the area of political speech."<sup>102</sup>

#### B. Variable Annuity-Related Comments

Two commenters raised concerns regarding the application of the proposed rules to variable annuities.<sup>103</sup>

<sup>87</sup> See *id.*

<sup>88</sup> See CAI Letter No. 1 and FSI Letter.

<sup>89</sup> See CAI Letter No. 1 (arguing that "[f]ailing to meet this objective of the [SEC Pay-to-Play Rule] would appear to be fatal to Rule 2030 inasmuch as the [SEC Pay-to-Play Rule] requires the Commission to find, by order, that Rule 2030 meets the objectives of the [SEC Pay-to-Play Rule]").

<sup>90</sup> See CAI Letter No. 1 (stating that in adopting the SEC Pay-to-Play Rule, "the Commission demonstrated its sensitivity to, and careful consideration of, potential First Amendment concerns because of the Rule's potential impact on political contributions").

<sup>91</sup> See FSI Letter.

<sup>92</sup> See CAI Letter No. 1 and FSI Letter. See also CAI Letter No. 2 (reflecting CAI's suggested

<sup>87</sup> See FINRA Response Letter, *supra* note 7.

<sup>88</sup> See CCP Letter; Moran Letter; and State Parties Letter.

<sup>89</sup> See Moran Letter.

<sup>90</sup> See CCP Letter (also urging rejection of MSRB's proposed amendments to its pay-to-play rules, MSRB Rule G-37).

<sup>91</sup> See CCP Letter.

<sup>92</sup> See *id.*

<sup>93</sup> See State Parties Letter (attaching its opening and reply appellate briefs filed in the *Republican State Committee v. SEC*, No. 14-1194 on Dec. 22, 2014 and Feb. 4, 2015, respectively).

<sup>94</sup> See State Parties Letter.

<sup>95</sup> See *id.* (quoting 15 U.S.C. 78o-3(b)(6)).

<sup>96</sup> See State Parties Letter.

<sup>97</sup> See *id.*

Both of these commenters requested, as a threshold matter, that FINRA confirm that Rule 2030 would not apply to variable annuities.<sup>104</sup> In support of one of these commenter's request that the proposed rule should not apply to the sales of variable annuity contracts which are supported by a separate account that invests in mutual funds, the commenter argues that the nature of variable annuities and the way investment options are selected does not implicate the investment advisory solicitation activities contemplated by the SEC Pay-to-Play Rule.<sup>105</sup> This same commenter claims that the relationship between a variable annuity contract holder and the investment adviser to a mutual fund supporting the variable annuity does not rise to a level such that it should implicate a pay-to-play obligation.<sup>106</sup> Another one of these commenter's claims, in support of its argument that Rule 2030 should not apply to variable annuities, is that compliance with Rule 2030 would be impractical for broker-dealers selling variable annuities in the government market.<sup>107</sup> This commenter also argues, for example, that a covered member selling a variable annuity, particularly where the separate account is a registered as a unit investment trust, cannot fairly be seen to be engaging in solicitation activities on behalf of all of the investment advisers and sub-advisers that manage the covered investment pools available as investment options under the separate account and subaccounts.<sup>108</sup>

One of these commenters also requests that proposed Rule 2030 be modified to, among other things, clarify that the distribution of a two-tiered product such as a variable annuity is not solicitation activity for an investment adviser and sub-advisers managing the funds available as investment options.<sup>109</sup> Furthermore, this same commenter states that if FINRA or the Commission determines that broker-dealers selling variable annuities constitute solicitation activities for purposes of Rule 2030, that determination raises a host of interpretive questions that, in this commenter's view, will require further

revisions to the certain language in some of FINRA's proposed rules).

<sup>104</sup> See CAI Letter No. 1 and FSI Letter.

<sup>105</sup> See FSI Letter (claiming that applying the proposed rule to variable annuities will significantly increase the compliance burden and as such may limit the options our members make available to 403(b) and 457 plans).

<sup>106</sup> See FSI Letter.

<sup>107</sup> See CAI Letter No. 1.

<sup>108</sup> See *id.*

<sup>109</sup> See *id.*

guidance from FINRA or the Commission.<sup>110</sup>

### C. Comments Regarding the Scope of the Proposed Rule

Two commenters also expressed concern that proposed rule 2030(d) would, in their view, re-characterize "ordinary" or "customary" distribution activities for covered investment pools as the solicitation of clients on behalf of the investment adviser to the covered investment pools.<sup>111</sup> One of these commenters requests that such customary distribution activity by member firms for covered investment pools sold to government entities *not* be treated as solicitation activity for an investment adviser for purposes of Rule 2030 simply because an investment adviser provides advisory services to a covered investment pool that is available as an investment option.<sup>112</sup> As more fully explained in the commenter's letter, the commenter claims, for example, that proposed Rule 2030(d) would recast "traditional" broker-dealer activity (*i.e.*, the offer and sale of covered investment pool securities pursuant to a selling or placement agent agreement) into something it is not: The solicitation of investment advisory services on behalf of an investment adviser.<sup>113</sup> This commenter also claims that the decision in *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006) and the Commission staff's interpretive position under Advisers Act Rule 206(4)-3 make proposed Rule 2030(d) impractical, as it would put selling firms in a contradictory position under FINRA rules and Advisers Act rules.<sup>114</sup> This commenter states that a broker-dealer that offers and sells interests in a mutual fund or private fund cannot be characterized as soliciting on behalf of the investment adviser to a covered investment pool.<sup>115</sup>

Similarly, another commenter expressed concern with the apparent application of proposed Rule 2030(d) to traditional brokerage sales of mutual funds and variable annuities to participant-directed government-sponsored retirement plans.<sup>116</sup> As more fully explained in the commenter's letter, this commenter states that it continues to be concerned that the provisions in proposed Rule 2030(d) "go beyond that which is required under Rule 206(4)-5(a)(2)(i) and Rule 206(4)-

<sup>110</sup> See *id.*

<sup>111</sup> See CAI Letter No. 1 and FSI Letter.

<sup>112</sup> See CAI Letter No. 1.

<sup>113</sup> See *id.*

<sup>114</sup> See *id.*

<sup>115</sup> See *id.*

<sup>116</sup> See FSI Letter.

5(c) to the detriment of investors."<sup>117</sup> This same commenter also claims that mutual fund sales, as well as variable annuity sales, should be excluded, claiming that the proposed rules serve to redefine the sale of mutual funds as solicitation by a broker-dealer on behalf of an investment adviser and also conflicts with the realities of conventional mutual fund selling agreements.<sup>118</sup>

### D. Comments Regarding the Inclusion of Distribution Activity in the Proposed Rule

One commenter generally expressed concern that Rule 2030 is unnecessarily ambiguous regarding the term distribution activities in Rule 2030(a).<sup>119</sup> This commenter claims that it is unclear what distribution activities "with" a government entity would be prohibited, what compensation is covered by the proposed rule and who must pay it, and when a member firm might be deemed to be acting "on behalf of" an investment adviser.<sup>120</sup> For example, this commenter states that the ambiguity of Rule 2030 may result in its misapplication in a variety of contexts.

This commenter also claims that, while the SEC Pay-to-Play Rule requires regulated persons to be subject to rules that prohibit them from engaging in certain distribution activities if certain political contributions have been made, Rule 206(4)-5 does not mandate the use of the term "distribution" in describing the conduct prohibited by the proposed rule, and suggested revised rule text reflecting that assertion.<sup>121</sup>

The commenter believes that its suggested revisions would, among other things, eliminate the potential concern that a selling firm might violate Rule 2030 unknowingly due to being deemed to be acting on behalf of investment advisers or sub-advisers of underlying funds with which it has no relationship.<sup>122</sup>

### E. Comments Regarding Defined Terms Used in the Proposed Rules

Two commenters requested clarification of certain defined terms used in the proposed rules.<sup>123</sup> One commenter urged FINRA, or the Commission, to clarify the meaning of

<sup>117</sup> FSI Letter.

<sup>118</sup> See *id.*

<sup>119</sup> See CAI Letter No. 1.

<sup>120</sup> See *id.*

<sup>121</sup> See CAI Letter No. 1 and CAI Letter No. 2 (reflecting CAI's suggested revisions to certain language in some of FINRA's proposed rules).

<sup>122</sup> See CAI Letter No. 1 (claiming that the commenter's suggested revisions would not result in any inappropriate narrowing of the scope of Rule 2030).

<sup>123</sup> See CAI Letter No. 1 and NAIFA Letter.

the term “instrumentality” as it is used in the definition of “government entity.”<sup>124</sup> This commenter claims that, without additional guidance, covered members will continue to struggle with whether a contribution to a given entity should be treated as a contribution to an instrumentality of a state or state agency, thus triggering the two-year time out.<sup>125</sup> This same commenter also asked for clarification as to whether each and every “contribution” (as defined in proposed Rule 2030(g)(1)) is, by definition, also a “payment” (as defined in proposed Rule 2030(g)(9)).<sup>126</sup>

Another commenter requests that FINRA clarify the definition of a “covered associate” and clarify and delineate the positions that would qualify someone as a covered “official.”<sup>127</sup> This commenter claims that, in response to the same definition of “covered associate” as used in the SEC Pay-to-Play Rule, many investment advisers and broker dealers have classified all of their representatives as covered associates regardless of whether they actually engage in the solicitation activity specified in the definition.<sup>128</sup> This commenter believes that additional clarification on when an associated person of a covered member would (or would not) qualify as a “covered associate” would ease compliance burdens, curtail overly broad limits on legitimate political activity, and increase the consistency of procedures amongst member firms who seek to comply with both the letter and the spirit of the proposed rule.<sup>129</sup> This same commenter requests additional details or guidance from the Commission with respect to this definition of “official” because, according to that commenter, that definition has caused, and will continue to spark confusion over exactly what offices subject the holder to be classified as an “official” given that the term is defined the same way in the SEC Pay-to-Play Rule.<sup>130</sup>

<sup>124</sup> See CAI Letter No. 1 (claiming that CAI’s members have struggled to understand the contours of this term in the context of the SEC Pay-to-Play Rule).

<sup>125</sup> See *id.*

<sup>126</sup> See CAI Letter No. 1 (discussing Notice, 80 FR at 81654, n. 41: “Consistent with the SEC Pay-to-Play Rule, FINRA is including the broader term “payments,” as opposed to “contributions,” to deter a cover member from circumventing the proposed rule’s prohibitions by coordinating indirect contributions to government officials by making payments to political parties”).

<sup>127</sup> See NAIFA Letter.

<sup>128</sup> See *id.*

<sup>129</sup> See *id.*

<sup>130</sup> See *id.*

#### F. Comments Regarding PAC Contributions That Trigger the Anti-Circumvention Provision of the Proposed Rule

This commenter also claims that statements made by FINRA in the Notice regarding the proposed rule’s anti-circumvention provision, proposed Rule 2030(e), combined with statements made in SEC staff guidance concerning whether contributions through PACs would violate the SEC Pay-to-Play Rule and section 208(d) of the Advisers Act, have the ability to chill contributions to PACs.<sup>131</sup> This commenter claims, for example, that prospective contributors who simply want to donate to a PAC have been hesitant to or restricted from doing so out of fear that they may be making an indirect contribution in violation of the SEC Pay-to-Play Rule.<sup>132</sup> Accordingly, this commenter requests further guidance from the Commission on the factors by which contributions to PACs would or would not trigger the anti-circumvention provision of the proposed rule.<sup>133</sup>

#### G. Comments Regarding the De Minimis Exception Under Proposed Rule 2030(c)

Several commenters raised concerns regarding the *de minimis* contribution exception under proposed Rule 2030(c)(1). One commenter requested that the \$350 and \$150 amounts “be raised substantially” in both SEC Pay-to-Play Rule and in proposed Rule 2030(c)(1), and further requested that the \$350 limitation on the proposed exception for returned contributions under proposed Rule 2030(c)(3), be eliminated in both the SEC Pay-to-Play Rule and in FINRA’s proposed rule.<sup>134</sup>

#### H. Comments Regarding the Grandfathering of Existing Accounts and Contracts

One commenter requested that FINRA clarify the application of the proposed rule to existing government entity accounts or contracts.<sup>135</sup> This commenter requests that, in the event that FINRA does not amend the application of its proposed rule to covered investment pools (as requested by this same commenter), FINRA apply the proposed rule only to accounts and variable contracts opened after the effective date.<sup>136</sup>

<sup>131</sup> See *id.*

<sup>132</sup> See *id.*

<sup>133</sup> See *id.*

<sup>134</sup> See CAI Letter No. 1.

<sup>135</sup> See FSI Letter.

<sup>136</sup> See *id.*

#### I. Comments Regarding Application of the Proposed Rules to the Independent Business Model

One commenter claims that its members will face difficulties in attempting to comply with the proposed rules, and that these difficulties stem, primarily, from a requirement for independent firms to implement a rule that is premised on the notion that solicitation of clients is performed pursuant to a centralized process controlled by the management of a registered investment adviser.<sup>137</sup> This same commenter claims that the lack of clarity as to the application of the SEC Pay-to-Play Rule to its members’ business model, and the scope of government officials that trigger the requirements, has led some firms to adopt aggressive compliance programs that prohibit political contributions.<sup>138</sup> Accordingly, this commenter claims that absent clarity concerning the application of the proposed rule to the brokerage services provided to 403(b) and 457 plans, its members will be faced with the choice of either adopting similarly aggressive policies or prohibiting sales to government-sponsored retirement plans.<sup>139</sup>

#### J. Comments Regarding Proposed Rule 4580: Books and Records Requirements

One commenter claims that it continues to believe that not all payments to political parties or PACs should have to be maintained under the books and records requirements of proposed Rule 4580.<sup>140</sup> Rather, this commenter believes that only payments to political parties or PACs where the covered member or a covered associate (i) directs the political party or PAC to make a contribution to an official of a government entity which the covered member is soliciting on behalf of an investment adviser or (ii) knows that the political party or PAC is going to make a contribution to an official of a government entity which the covered member is soliciting on behalf of an investment adviser, should have to be maintained.<sup>141</sup> This commenter states that, while it appreciates FINRA’s rationale for proposed Rule 4580, it believes the costs and burdens associated with the request far outweigh the benefits to FINRA in ensuring compliance with the rule and will lead

<sup>137</sup> See FSI Letter (claiming FSI believes that the SEC Pay-to-Play Rule has inadvertently captured non-corrupting activity and it fears that the proposed rule may do the same).

<sup>138</sup> See *id.*

<sup>139</sup> See *id.*

<sup>140</sup> See CAI Letter No. 1.

<sup>141</sup> See *id.*

to periodic “fishing expeditions” by FINRA examiners.<sup>142</sup>

#### *K. Comments Requesting More Stringent Requirements in the Proposed Rules*

Two commenters suggested including more stringent requirements in FINRA’s proposed rule.<sup>143</sup> First, both commenters request that FINRA expand the applicability of its proposed rules to include state-registered investment advisers.<sup>144</sup> More specifically, one of these commenters suggests that FINRA include state-registered investment advisers in its definition of “investment adviser” for the purposes of its proposed rule.<sup>145</sup> These commenters note, for example, that FINRA states in the Notice that relatively few state-registered investment advisers manage public pension plans.<sup>146</sup> However, one of these commenters believes that this alone does not justify permitting FINRA-member firms that do manage public pension plans, but happen to work with smaller investment advisers, to engage in pay-to-play activities with no repercussions.<sup>147</sup> One of these commenters also claims that state-registered investment advisers now include larger firms and, therefore, it is much more likely that state-registered investment advisers advise or manage public pension plans or similar funds.<sup>148</sup>

Second, these same two commenters request that FINRA include a mandatory disgorgement provision for violations of its proposed rule.<sup>149</sup> These commenters state that they are disappointed that FINRA removed the mandatory disgorgement provisions from the proposal as outlined in FINRA’s *Regulatory Notice* 14–50.<sup>150</sup> These commenters believe that a mandatory disgorgement provision would act as a significant deterrent to engaging in pay-to-play schemes, and it should remain in FINRA’s final rule.<sup>151</sup>

Finally, one of these commenters believes that the current two-year cooling-off period in the proposal should be at least four years.<sup>152</sup> This commenter believes that the two-year cooling-off period does not adequately reduce the incentive for FINRA member firms to make political contributions in order to obtain pay-to-play

advantages.<sup>153</sup> This commenter states FINRA should start with the most comprehensive rule, and that it would welcome the deterrent effect of a four-year cooling off period.<sup>154</sup>

#### **IV. Proceedings To Determine Whether To Approve or Disapprove SR–FINRA–2015–056 and Grounds for Disapproval Under Consideration**

The Commission is instituting proceedings pursuant to Exchange Act Section 19(b)(2)(B) to determine whether the proposed rule change should be approved or disapproved.<sup>155</sup> Institution of proceedings appears appropriate at this time in view of the legal and policy issues raised by the proposal. As noted above, institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, the Commission seeks and encourages interested persons to comment on the proposed rule change, including the comments received, and provide the Commission with additional comment to inform the Commission’s analysis as to whether to approve or disapprove the proposal.

Pursuant to Exchange Act Section 19(b)(2)(B),<sup>156</sup> the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of, and input from, commenters with regard to the proposed rule change’s consistency with Section 15A of the Exchange Act, and in particular Sections 15A(b)(6) and 15A(b)(9). Exchange Act Section 15A(b)(6)<sup>157</sup> requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. In addition, Exchange Act Section 15A(b)(9)<sup>158</sup> requires that FINRA rules not impose any unnecessary or inappropriate burden on competition.

<sup>142</sup> See *id.*

<sup>143</sup> See *id.*

<sup>144</sup> 15 U.S.C. 78s(b)(2). Exchange Act Section 19(b)(2)(B) provides that proceedings to determine whether to disapprove a proposed rule change must be concluded within 180 days of the date of publication of notice of the filing of the proposed rule change. The time for conclusion of the proceedings may be extended for up to an additional 60 days if the Commission finds good cause for such extension and publishes its reasons for so finding or if the self-regulatory organization consents to the extension.

<sup>145</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>146</sup> 15 U.S.C. 78o–3(b)(6).

<sup>147</sup> 15 U.S.C. 78o–3(b)(9).

#### **V. Request for Written Comments**

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues raised by the proposed rule change. In particular, the Commission invites the written views of interested persons on whether the proposed rule change is inconsistent with Sections 15A(b)(6) and 15A(b)(9), or any other provision, of the Exchange Act, or the rules and regulations thereunder.

Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b–4, any request for an opportunity to make an oral presentation.<sup>159</sup>

Interested persons are invited to submit written data, views, and arguments by April 25, 2016 concerning whether the proposed rule change should be approved or disapproved. Any person who wishes to file a rebuttal to any other person’s submission must file that rebuttal by May 19, 2016. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission’s Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR–FINRA–2015–056 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090.

All submissions should refer to File Number SR–FINRA–2015–056. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission’s Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule

<sup>159</sup> Exchange Act Section 19(b)(2), as amended by the Securities Acts Amendments of 1975, Pub. L. 94–29, 89 Stat. 97 (1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Acts Amendments of 1975, Report of the Senate Committee on Banking, Housing and Urban Affairs to Accompany S. 249, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

<sup>142</sup> See *id.*

<sup>143</sup> See NASAA Letter and PIABA Letter.

<sup>144</sup> See NASAA Letter and PIABA Letter.

<sup>145</sup> See NASAA Letter.

<sup>146</sup> See NASAA Letter and PIABA Letter.

<sup>147</sup> See PIABA Letter.

<sup>148</sup> See NASAA Letter.

<sup>149</sup> See NASAA Letter and PIABA Letter.

<sup>150</sup> See NASAA Letter and PIABA Letter.

<sup>151</sup> See NASAA Letter and PIABA Letter.

<sup>152</sup> See PIABA Letter.

change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change. The Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make publicly available.

All submissions should refer to File Number SR-FINRA-2015-056 and should be submitted on or before April 25, 2016. If comments are received, any rebuttal comments should be submitted by May 19, 2016.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>160</sup>

**Robert W. Errett,**  
*Deputy Secretary.*

[FR Doc. 2016-07513 Filed 4-1-16; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-77468; File No. SR-NYSE-2016-27]

### Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Adopting Requirements for the Collection and Transmission of Data Pursuant to Appendices B and C of the Regulation NMS Plan to Implement a Tick Size Pilot Program

March 29, 2016.

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (the "Act")<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that on March 25, 2016, New York Stock Exchange LLC ("NYSE" or the "Exchange") filed with the Securities and Exchange Commission (the "Commission") the proposed rule change as described in

Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to adopt requirements for the collection and transmission of data pursuant to Appendices B and C of the Regulation NMS Plan to Implement a Tick Size Pilot Program ("Plan"). The proposed rule change is available on the Exchange's Web site at [www.nyse.com](http://www.nyse.com), at the principal office of the Exchange, and at the Commission's Public Reference Room.

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

##### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

On August 25, 2014, NYSE Group, Inc., on behalf of the Exchange, NYSE MKT LLC, NYSE Arca, Inc., the Bats BZX Exchange, Inc. f/k/a BATS Exchange, Inc. ("BZX"), BATS BYX Exchange, Inc. f/k/a BATS Y-Exchange, Inc. ("BYX"), Bats EDGA Exchange, Inc., Bats EDGX Exchange, Inc., Chicago Stock Exchange, Inc., Financial Industry Regulatory Authority, Inc. ("FINRA"), NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, and the Nasdaq Stock Market LLC (collectively "Participants"), filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 11A of the Act<sup>4</sup> and Rule 608 of Regulation NMS thereunder,<sup>5</sup> the Plan to Implement a Tick Size Pilot Program ("Pilot").<sup>6</sup> The Participants filed the

Plan to comply with an order issued by the Commission on June 24, 2014.<sup>7</sup> The Plan<sup>8</sup> was published for comment in the **Federal Register** on November 7, 2014, and approved by the Commission, as modified, on May 6, 2015.<sup>9</sup>

The Plan is designed to allow the Commission, market participants, and the public to study and assess the impact of increment conventions on the liquidity and trading of the common stocks of small-capitalization companies. Each Participant is required to comply, and to enforce compliance by its member organizations, as applicable, with the provisions of the Plan. As is described more fully below, the proposed rules would require member organizations to comply with the applicable data collection requirements of the Plan.<sup>10</sup>

The Pilot will include stocks of companies with \$3 billion or less in market capitalization, an average daily trading volume of one million shares or less, and a volume weighted average price of at least \$2.00 for every trading day. The Pilot will consist of a control group of approximately 1400 Pilot Securities and three test groups with 400 Pilot Securities in each (selected by a stratified random sampling process).<sup>11</sup> During the pilot, Pilot Securities in the control group will be quoted at the current tick size increment of \$0.01 per share and will trade at the currently permitted increments. Pilot Securities in the first test group ("Test Group One") will be quoted in \$0.05 minimum increments but will continue to trade at any price increment that is currently permitted.<sup>12</sup> Pilot Securities in the second test group ("Test Group Two") will be quoted in \$0.05 minimum increments and will trade at \$0.05 minimum increments subject to a midpoint exception, a retail investor order exception, and a negotiated trade exception.<sup>13</sup> Pilot Securities in the third test group ("Test Group Three") will be subject to the same quoting and trading increments as Test Group Two and also will be subject to the "Trade-at"

<sup>7</sup> See Securities Exchange Act Release No. 72460 (June 24, 2014), 79 FR 36840 (June 30, 2014).

<sup>8</sup> Unless otherwise specified, capitalized terms used in this rule filing are based on the defined terms of the Plan.

<sup>9</sup> See Securities Exchange Act Release No. 74892 (May 6, 2015), 80 FR 27513 (May 13, 2015) ("Approval Order").

<sup>10</sup> The Exchange proposes to provide in the introduction paragraph to Rule 67 that the Rule shall be in effect during a pilot period to coincide with the pilot period for the Plan (including any extensions to the pilot period for the Plan).

<sup>11</sup> See Section V of the Plan for identification of Pilot Securities, including criteria for selection and grouping.

<sup>12</sup> See Section VI(B) of the Plan.

<sup>13</sup> See Section VI(C) of the Plan.

<sup>160</sup> 17 CFR 200.30-3(a)(12); 17 CFR 200.30-3(a)(57).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

<sup>4</sup> 15 U.S.C. 78k-1.

<sup>5</sup> 17 CFR 242.608.

<sup>6</sup> See Letter from Brendon J. Weiss, Vice President, Intercontinental Exchange, Inc., to Secretary, Commission, dated August 25, 2014.