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September 6, 2022

Via Email Only @ rule-comments@sec.gov

Vanessa Countryman
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: SR-FINRA-2022-021 – Proposed Rule Change to Adopt Supplementary Material .18 (Remote Inspections Pilot Program) under FINRA Rule 3110 (Supervision)

Dear Ms. Countryman:

I write on behalf of the Public Investors Advocate Bar Association ("PIABA"), an international bar association comprised of attorneys who represent investors in disputes with the securities industry. Since its formation in 1990, PIABA has promoted the interests of the public investor in all forums where securities and commodities disputes are heard, while also advocating for public education regarding investment fraud and industry misconduct. Our members and their clients have a strong interest in rules promulgated by the Financial Industry Regulatory Authority ("FINRA") relating to both investor protection and disclosure.

Pursuant to Rule of Practice 192(a) of the Securities and Exchange Commission ("SEC" or "Commission"), PIABA submits this comment to the SEC concerning FINRA's above-captioned recent filing, a proposed rule change to amend FINRA Rule 3110 (Supervision). FINRA proposes adopting new Supplementary Material section .18 (Remote Inspections Pilot Program) to Rule 3110 (Supervision). The proposed amendment would create a new voluntary, three-year remote inspection pilot program. The program would allow member firms to fulfill their obligation under Rule 3110(c) (Internal Inspections) by conducting inspections of some or all branch offices and locations remotely, without an on-site visit to such office or location, subject to specified terms.

For the same reasons that PIABA urged the Commission to reject the amendments proposed by SR-FINRA-2022-019 (proposed rule change to adopt new Supplementary Material .19 for residential supervisory locations), PIABA urges the Commission to reject remote inspections and the proposed pilot program in this SR-FINRA-2022-21.

The Exigencies of the Pandemic Should Not Lead to Weakening of Supervisory Structures

Beginning many years ago, SEC staff and FINRA interpreted FINRA rules to require member firms to conduct on-site inspections of branch offices and unregistered offices (i.e., non-branch locations) in accordance with the periodic schedule described under Rule 3110(c)(1).[2] In its proposal to create the pilot program, FINRA states that over the years, widespread advancements in technology and communications in the financial industry have significantly changed the way in which members and their associated persons conduct their business and communicate.[1] The proposal argues that this includes the practices that formed the original bases for an on-site inspection requirement:

> The COVID-19 pandemic has accelerated the use of a wide variety of compliance and workplace technology as many government and private employers, including member firms, were driven to adopt a broad remote work environment by quickly moving their employees out of their usual office setting to an alternative worksite such as a private residence. Insights obtained from member firms and other industry representatives, through various pandemic-related initiatives and other industry outreach, have led FINRA to carefully consider whether some processes and rules, including the manner in which a firm may satisfy its Rule 3110(c) obligations, should be modernized. Technological improvements and developments in regulatory compliance have provided more tools than before to create more effective and efficient compliance programs. To that end, FINRA believes that regulatory models should evolve to benefit from the availability and use of effective technology tools.[2]

To address the operational challenges in conducting on-site inspections during the pandemic, FINRA adopted temporary Rule 3110.17, effective since November 2020, to provide member firms the option to conduct inspections of their branch offices and non-branch locations remotely, subject to specified terms therein. FINRA seems to believe that now is the time to assess making what has been a temporary and necessary program to deal with the extraordinary exigencies of quarantines and health and safety concerns over the past two years of the global pandemic, into an accepted norm.

This is not acceptable. The proposed amendment, much like the recently proposed amendment to Rule 3110.19, to allow a home office to be considered residential supervisory location and creating rules and procedures for the supervision of same (SR-FINRA-2022-019), runs counter to FINRA's stated objective of investor protection. While it is understood that FINRA is attempting to change with the increased use of virtual technology, allowing more permanent home offices and remote supervision leaves considerable opportunity for brokers and their Member Firms to skirt the rules and harm investors.

As the SEC considers FINRA's proposal for the pilot program, we ask that the Commission staff consider numerous past enforcement cases from both FINRA and the SEC relating to inadequate supervision of remote offices. One such case is *In the Matter of Royal Alliance Associates, Inc*., Release No. 38174, 63 SEC Docket No. 1606 (Jan. 15, 1997). In this case, the SEC took issue with Royal Alliance's practice of performing announced audits on "small dispersed offices" beyond the "direct aegis of the firm":

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[1] SR-FINRA-2022-021, page 6 of 96. Full text of SR-FINRA-2022-021 accessed here: https://www.finra.org/rules-guidance/rule-filings/sr-finra-2022-021.
[2] *Id.*

> …Royal Alliance operates 1,500 offices with 2,700 registered representatives. Some 49 of these are one-person Offices. Here, Royal Alliance's failure to scrutinize adequately the securities-related business of its registered representatives, which were conducted beyond the direct aegis of the firm, was a certain recipe for trouble. Further, Royal Alliance's practice of conducting a pre-announced compliance examination only once a year was inadequate to satisfy its supervisory obligations.
> * * *
> Nevertheless, such arrangements necessarily entail greater supervisory challenges and the Commission requires firms organized in such a fashion, and individual supervisors at those firms, to meet the same high standards of supervision as at more traditionally organized firms.

The SEC continued to recognize this problem in another matter, *In the Matter of 1st Discount Brokerage, Inc.,* Release No. 66212A, Admin. Proc. File No. 3-14710 (Jan. 23, 2012). Therein, the SEC opined that firms that have an independent broker model require greater supervision than that of a traditional wire house brokerage firm. The lack of unannounced audits for a far-away broker with no one looking over their shoulder was wholly deficient. The firm's failure to adequately supervise the broker's conduct resulted in enabling the broker to conduct a nearly $9 million Ponzi scheme.

Other regulatory actions involving brokers "selling away" or running Ponzi schemes from residential or remote (often one-broker) offices are too plentiful to count. For a few examples: *In re Lawrence John Fawcett, Jr.*, FINRA No. 2017056329801 (operating from home); *see also Hailey v. Westpark Capital, Inc*., FINRA Arb No. 20-00320 (detailing the lack of sufficient supervision of Fawcett's home office); *In re Jerry Irvin Chancy*, FINRA No. 2014043629801 (operating from home), *In re Mark Lewton Hopkins*, FINRA No. 2018060968101 (operating from an office on a golf course owned by the broker); *In re Malcolm Segal*, FINRA No. 2014041990901 (home office); *In re Robert Van Zandt*, FINRA No. 2011027577001; *In re Nevin Gillette*, FINRA No. 2006007067401; *In re Charles Caleb Fackrell*, FINRA No. 2014043705201; *In re Thomas H. Laws*, FINRA No. 2019061095601; *In re Brian Royster*, FINRA No. 2017052882601; *In re Michael James Blake*, FINRA No. 2010021710501; *In re Murray Todd Petersen*, FINRA No. 2019064432901; *In the Matter of Rebecca Engle*, SEC Admin. Release 34-75127 (June 9, 2015); *In the Matter of Brian Schuster*, SEC Admin. Release 34-75128 (June 9, 2015); *In the Matter of Larry Dearman Sr.*, SEC Release No. 75292 (June 24, 2015); *In the Matter of Levi D. Lindemann*, SEC Release No. 77696 (Apr. 22, 2016); and *In the Matter of Securities America Advisors, Inc*., SEC Release No. 94995 (May 26, 2022) (regarding a failure to supervise Hector May, who ran a $8 million Ponzi scheme).

This partial history of enforcement cases indicates member firms have been and remain unable or unwilling to effectively supervise remote offices. While the pandemic brought technological advancements, the same cannot be assumed for broker-dealer supervisory and compliance cultures.

Similarly, remote inspections simply cannot uncover nefarious conduct by brokers who keep records in paper form and meet with clients in-person, notwithstanding rules or guidance to the contrary.

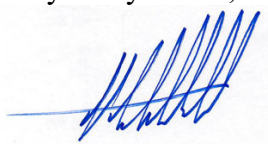
Likewise, a review of all electronic communications that are made through the member firm's electronic data systems would only be sufficient if the rules governing how firms are required to adequately review these emails are strengthened. Often, firms only review a small *sampling* of electronic correspondence. Our members have seen numerous cases where a broker engaged in secretly selling unauthorized investments *was openly discussing* the unlawful conduct through their firm-approved email address, but the

firm did not detect it for years (or ever) because the firm did not have adequate systems in place to monitor and catch the emails.

Any provision that weakens the rules as it relates to inspections of home or remote offices is unacceptable and will lead to more harmed investors. These proposed rules would provide additional opportunities for a broker to engage in fraudulent conduct without a supervisor or auditor adequately supervising the broker's conduct. If anything, FINRA should require firms to develop and implement more unannounced, *in-person* inspections as remote offices and virtual technology becomes more prevalent. Additionally, regardless of whether the pilot program is implemented or not, the Commission should demand that FINRA require firms to review more than just a sampling of electronic correspondence.

PIABA thanks the Commission and FINRA for the opportunity to comment on this proposal.

Very Truly Yours,



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