

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62621 File No. SR-FINRA-2010-034)

July 30, 2010

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change to Adopt FINRA Rule 4530 (Reporting Requirements) in the Consolidated FINRA Rulebook

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on July 30, 2010, Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. 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

FINRA is proposing to adopt NASD Rule 3070 (Reporting Requirements) as FINRA Rule 4530 (Reporting Requirements) in the consolidated FINRA rulebook, subject to certain amendments, and to delete paragraphs (a) through (d) of Incorporated NYSE Rule 351 (Reporting Requirements) and Incorporated NYSE Rules 351.10 and 351.13. The proposed rule change also would add a supplementary material section to proposed FINRA Rule 4530.

The text of the proposed rule change is available on FINRA’s Web site at <http://www.finra.org>, on the Commission’s Web site at <http://www.sec.gov>, at the principal office of FINRA, and at the Commission’s Public Reference Room.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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

In its filing with the Commission, FINRA 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 these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

As part of the process of developing a new consolidated rulebook (“Consolidated FINRA Rulebook”),³ FINRA is proposing to adopt NASD Rule 3070 as FINRA Rule 4530 in the Consolidated FINRA Rulebook, subject to certain amendments as described below. The proposed rule change also would delete paragraphs (a) through (d) of Incorporated NYSE Rule 351⁴ and NYSE Rules 351.10 and 351.13 from the Transitional Rulebook.⁵ Further, the

³ The current FINRA rulebook consists of (1) FINRA Rules; (2) NASD Rules; and (3) rules incorporated from NYSE (“Incorporated NYSE Rules”) (together, the NASD Rules and Incorporated NYSE Rules are referred to as the “Transitional Rulebook”). While the NASD Rules generally apply to all FINRA members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (“Dual Members”). The FINRA Rules apply to all FINRA members, unless such rules have a more limited application by their terms. For more information about the rulebook consolidation process, see Information Notice, March 12, 2008 (Rulebook Consolidation Process).

⁴ For convenience, the Incorporated NYSE Rules are referred to as the NYSE Rules.

⁵ NYSE Rule 351(e) and NYSE Rule Interpretation 351(e)/01 (Reports of Investigation) govern trade investigation reporting requirements. NYSE Rules 351(f), 351.11 and 351.12 govern the annual attestation requirement of the research analyst conflict of interest rules. These provisions will be addressed as part of the supervision rules and research analyst conflict of interest rules, respectively. See Regulatory Notice 08-24 (May 2008) (Proposed Consolidated FINRA Rules Governing Supervision and

proposed rule change would add a supplementary material section to proposed FINRA Rule 4530 as detailed below.

Background

NASD Rule 3070 and NYSE Rule 351 require members to report to FINRA certain specified events (e.g., regulatory actions) and quarterly statistical and summary information regarding written customer complaints. FINRA uses the reported information for regulatory purposes. Among other things, the information assists FINRA to identify and investigate firms, offices and associated persons that may pose a regulatory risk.

Proposal

FINRA proposes replacing NASD Rule 3070 and NYSE Rule 351 with a single rule, proposed FINRA Rule 4530, in the Consolidated FINRA Rulebook. FINRA Rule 4530 is based in large part on NASD Rule 3070, taking into account certain requirements under NYSE Rule 351. The proposed rule also includes a supplementary material section that contains certain clarifications and definitions as well as codifications of existing staff guidance. More specifically, FINRA is proposing the following changes.

a. Reporting Deadline (Proposed FINRA Rule 4530(a))

FINRA Rule 4530(a) consolidates the requirement (currently in NASD Rules 3070(a)(1), (a)(9) and (b)) that a firm report an event after the firm “knows or should have known” of the existence of the event. Consistent with the requirements of NYSE Rule 351, FINRA Rule 4530(a) also extends the time period for reporting any of the events specified in paragraph (a) of the proposed rule to no later than 30 calendar days after the firm knows or should have known of the existence of the event (rather than the 10 business days currently provided under NASD Rule

Supervisory Controls) and Regulatory Notice 08-55 (October 2008) (FINRA Requests Comment on Proposed Research Registration and Conflict of Interest Rules).

3070(b)). The proposed 30-calendar-day reporting deadline also is consistent with the reporting deadline for disclosing information on the Forms BD (Uniform Application for Broker-Dealer Registration), U4 (Uniform Application for Securities Industry Registration or Transfer) and U5 (Uniform Termination Notice for Securities Industry Registration) (collectively referred to as the “Uniform Forms”).

b. External Findings (Proposed FINRA Rule 4530(a)(1)(A))

NASD Rule 3070(a)(1) requires that a firm report whenever the firm or an associated person of the firm has been found to have violated any provision of any securities law or regulation, “any” rule or standard of conduct of “any” governmental agency, self-regulatory organization (“SRO”), or financial business or professional organization, or engaged in conduct that is inconsistent with just and equitable principles of trade. This provision requires firms to report findings of violations by an external body.

FINRA Rule 4530(a)(1)(A) generally retains the requirement under NASD Rule 3070(a)(1), though it limits the scope of reportable findings of violation by an external body to violations of any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body, SRO or business or professional organization. FINRA believes that limiting the scope of the rule to violations of any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body, SRO or business or professional organization will make it more effective and relevant to FINRA’s program, as well as enhance firms’ ability to more accurately report such information. For similar reasons, FINRA has eliminated the requirement that firms report any and all findings that amount to violations of just and equitable principles of trade. However, for instance, firms

would continue to report a finding of violation of an SRO's just and equitable principles of trade rule, such as FINRA Rule 2010.

c. Civil Litigation or Arbitration; Other Claims for Damages
(Proposed FINRA Rule 4530(a)(1)(G))

FINRA Rule 4530(a)(1)(G) merges for simplification the reporting provisions, currently in NASD Rules 3070(a)(7) and (a)(8) and NYSE Rules 351(a)(7) and (a)(8), pertaining to (1) any securities- or commodities-related civil litigation or arbitration; and (2) any claim for damages by a customer or broker-dealer, disposed of by judgment, award or settlement for certain monetary thresholds. In addition, the proposed rule extends the provision relating to civil litigation or arbitration matters to include the reporting of any "insurance" civil litigation or arbitration that is "financial related." Further, the proposed rule clarifies that firms are required to report any claim for damages by a customer or broker-dealer that is "financial" or "transactional" in nature. FINRA believes that transactional claims by customers, including contractual disputes, are relevant to its programs since they may reveal misconduct, such as an impermissible customer loan.

d. Statutory Disqualifications (Proposed FINRA Rule 4530(a)(1)(H))

Consistent with NYSE Rule 351(a)(9), FINRA Rule 4530(a)(1)(H) requires a firm to report whenever the firm itself is subject to a "statutory disqualification" and clarifies that a firm is required to report whenever an associated person of the firm is subject to a "statutory disqualification." The proposed rule also replaces the requirement in NASD Rule 3070(a)(9) and NYSE Rule 351(a)(9) to report whenever a firm or an associated person of the firm "is associated in any business or financial activity" with a person subject to a "statutory disqualification" with a requirement to report whenever the firm or an associated person of the firm "is involved in the sale of any financial instrument, the provision of any investment advice

or the financing of any such activities” with a person subject to a “statutory disqualification.”

FINRA believes that this change provides greater clarity as to the scope of the provision.

e. Internal Disciplinary Actions Against Associated Persons
(Proposed FINRA Rule 4530(a)(2))

Similar to NASD Rule 3070(a)(10) and NYSE Rule 351(a)(10), FINRA Rule 4530(a)(2) continues to require a firm to report certain disciplinary actions taken by the firm against its associated persons. However, the proposed rule clarifies that any such disciplinary action involving the withholding of compensation or of any other remuneration (not just commissions) in excess of \$2,500 is a reportable event.

f. Internal Conclusions (Proposed FINRA Rules 4530(b) and 4530.01)

NYSE Rule 351(a)(1) requires that a firm report whenever it or its associated persons have violated any provision of any securities law or regulation, “any” agreement with or rule or standard of conduct of “any” governmental agency, SRO, or business or professional organization, or engaged in conduct that is inconsistent with just and equitable principles of trade or detrimental to the interests or welfare of the NYSE. This provision requires firms to report their internal conclusions of the enumerated violative conduct.

FINRA Rule 4530(b) generally incorporates the requirement under NYSE Rule 351(a)(1) and provides that a firm is required to report to FINRA no later than 30 calendar days after the firm has concluded, or reasonably should have concluded, *on its own* that an associated person of the firm or the firm itself has engaged in violative conduct.⁶ However, the proposed rule limits

⁶ Proposed FINRA Rule 4530(b) was originally proposed as FINRA Rule 4530(a)(3) in Regulatory Notice 08-71 (discussed in Item II.C. of this filing). As discussed above, proposed FINRA Rule 4530(a) requires a firm to report an event after the firm “knows or should have known” of the existence of the event. To clarify the standard applicable to a firm’s internal conclusion of violation, FINRA is proposing to re-designate paragraph (a)(3) as paragraph (b) of FINRA Rule 4530 and require a firm to report where it has

the scope of reportable violative conduct to violations of any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or SRO.

Additionally, FINRA Rule 4530.01 excludes from the reporting requirement an isolated violation by the firm or an associated person of the firm that can be reasonably viewed as a ministerial violation of the applicable rules that did not result in customer harm and was remedied promptly upon discovery. Thus, for example, if a firm discovers a few corporate accounts that, due to a ministerial lapse, do not have a record identifying the person(s) authorized to transact business on behalf of the accounts and upon discovering the problem promptly updates the accounts with the required information, it would not be considered a reportable event for purposes of proposed FINRA Rule 4530(b). Conversely, if there is a wholesale failure by a firm to maintain such information, it would be considered a reportable event for purposes of the proposed rule.

Further, if a firm disciplines an associated person in the manner described in FINRA Rule 4530(a)(2), FINRA Rule 4530.01 requires the firm to report the event under paragraph (a)(2), rather than paragraph (b) of the proposed rule.

g. Domestic and Foreign Actions and Actions By a Regulatory Body
(Proposed FINRA Rules 4530(a)(1)(A), (C), (D), (F) and 4530.04)

Currently, both NASD Rule 3070 and NYSE Rule 351 make frequent reference to, for example, “any” regulatory or self-regulatory body, without denoting that it includes both domestic and foreign regulators. FINRA Rules 4530(a)(1)(A), (C), (D) and (F) clarify that they apply to both domestic and foreign actions and that they apply to actions by a “regulatory body.”

concluded or reasonably should have concluded that the firm or an associated person has engaged in the enumerated violative conduct.

FINRA Rule 4530.04 defines the term “regulatory body” as governmental regulatory bodies and authorized non-governmental regulatory bodies, such as the Financial Services Authority.

h. Reporting Obligation (Proposed FINRA Rule 4530(e))

NASD Rule 3070(d) provides that compliance with NASD Rule 3070 does not relieve a firm or an associated person from certain other obligations, such as the requirement to disclose information on the Uniform Forms, as applicable.

FINRA Rule 4530(e) continues the requirement of NASD Rule 3070(d). The proposed rule also clarifies that a firm has an obligation to report the specified events (FINRA Rules 4530(a) and (b)) and quarterly statistical and summary information regarding written customer complaints (FINRA Rule 4530(d)), regardless of whether such information is reported or disclosed pursuant to any other rule or requirement, including the requirements of the Forms BD or U4. However, the proposed rule provides that a firm is not required to report an event otherwise required to be reported under FINRA Rules 4530(a) or (b) if the firm discloses the event on the Form U5, consistent with the requirements of that form. While information disclosed on the Forms BD and U4 are not subject to this exception at this time, FINRA will work toward the goal of eliminating duplicative reporting of information disclosed on those forms.

i. Elimination of the Exemption for Dual Members Subject to Another SRO’s Rule

NASD Rule 3070(e) provides an exemption for firms subject to substantially similar reporting requirements of another SRO. This provision is intended to exempt Dual Members subject to the reporting requirements of NYSE Rule 351. The proposed rule change eliminates this exemption since FINRA proposes creating a single rule and deleting the applicable reporting

requirements of NYSE Rule 351 (as noted below). Accordingly, all FINRA members will be subject to FINRA Rule 4530.

j. Filing of Related Documents with FINRA (Proposed FINRA Rule 4530(f))

NASD Rule 3070(f) requires a firm to file copies of certain criminal and civil complaints and arbitration claims with FINRA, including copies of (1) any complaint in which the firm is named as a defendant or respondent in any securities- or commodities-related private civil litigation; and (2) any securities- or commodities-related arbitration claim filed against the firm in any forum other than FINRA Dispute Resolution. Consistent with FINRA Rule 4530(a)(1)(G) discussed above, FINRA Rule 4530(f) extends the filing requirement to copies of any “insurance” civil litigation or arbitration that is “financial related.”

k. Additional Supplementary Material (Proposed FINRA Rules 4530.02, .03, .05, .06, .07 and .08)

In addition to the supplementary material discussed above (FINRA Rules 4530.01 and .04), FINRA proposes adding the following supplementary material:

- FINRA Rule 4530.02 clarifies the distinction between a firm’s internal conclusion of violative conduct and a finding of violative conduct by an external body, such as a court, domestic or foreign regulatory body, SRO or business or professional organization;
- FINRA Rule 4530.03 defines the term “found” as used in FINRA Rule 4530(a)(1)(A) generally consistent with the definition of the term in the Uniform Forms, and clarifies that the term also includes any formal finding (regardless of whether the finding will be appealed), but that it does not include a minor rule violation involving a fine of \$2,500 or less;

- FINRA Rule 4530.05 clarifies that for purposes of FINRA Rules 4530(a) and (b), firms should not report a single event under more than one paragraph or subparagraph, but that they may be required to report related events under more than one paragraph or subparagraph.
- FINRA Rule 4530.06 clarifies that when calculating the monetary thresholds for reporting civil litigations, arbitrations or claims for damages for purposes of FINRA Rule 4530(a)(1)(G), firms must include any attorneys fees and interest in the total amount. The proposed rule also codifies existing staff guidance regarding the calculation of the monetary thresholds when the parties are subject to “joint and several” liability (i.e., if the parties are subject to “joint and several” liability, each party is separately liable for the aggregate amount);⁷
- FINRA Rule 4530.07 clarifies that for purposes of FINRA Rules 4530(a), (b) and (d), firms should report an event relating to a former associated person if the event occurred while the individual was associated with the member; and
- FINRA Rule 4530.08 codifies existing staff guidance regarding a firm’s obligation to report quarterly statistical and summary information with respect to written customer complaints alleging theft or misappropriation of funds or securities, or forgery.⁸

1. Provisions Transferring With Non-Substantive Changes (Proposed FINRA Rules 4530(a)(1)(B), (a)(1)(E), (d) and (g))

⁷ See Notice to Members 96-85 (December 1996) (Customer Complaint Reporting Rule Update).

⁸ See Notice to Members 96-85.

FINRA proposes to transfer into FINRA Rule 4530 with non-substantive changes the provisions of NASD Rules 3070(a)(2), (a)(5), (c) and (g).

m. NYSE Provisions Proposed for Deletion

FINRA proposes to delete paragraphs (a) through (d) of NYSE Rule 351 and NYSE Rules 351.10 and 351.13 relating to the reporting of specified events and quarterly statistical and summary information regarding written customer complaints as these provisions are substantially similar to proposed FINRA Rule 4530, otherwise incorporated as described above, rendered obsolete by the approach reflected in the proposed rule, or addressed by other rules.

FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 90 days following Commission approval. The implementation date will be no later than 240 days following Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁹ which 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. FINRA believes that the proposed rule change will further the purposes of the Act by enhancing FINRA's ability to detect and investigate violative conduct.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

⁹ 15 U.S.C. 78q-3(b)(6).

In November 2008, FINRA published Regulatory Notice 08-71 soliciting comment on a proposal relating to the FINRA reporting requirements. FINRA received 21 comment letters in response to the Notice,¹⁰ which are discussed below.¹¹ A copy of the Notice is attached as Exhibit 2a. A list of the comment letters received in response to the Notice is attached as Exhibit 2b. Copies of the comment letters received in response to the Notice are attached as Exhibit 2c.¹²

1. Reporting Deadline (Proposed FINRA Rule 4530(a))

As discussed above, the proposed rule requires that a firm report an event after the firm “knows or should have known” of the existence of the event. One commenter argues that the

¹⁰ See Letter from Puplava Securities, Inc., dated December 4, 2008 (“Puplava”); letter from Committee of Annuity Insurers, dated December 29, 2008 (“CAI”); letter from Cutter & Company, Inc., dated December 29, 2008 (“Cutter”); letter from Farmers Financial Solutions, LLC, dated December 29, 2008 (“Farmers”); letter from National Association of Independent Broker-Dealers, Inc., dated December 29, 2008 (“NAIBD”); letter from GBS Financial Corp., dated December 30, 2008 (“GBS”); letter from Goodwin Browning & Luna Securities, dated December 30, 2008 (“Goodwin”); letter from OmniCap, LLC, dated December 30, 2008 (“OmniCap”); letter from Pointe Capital, Inc., dated December 30, 2008 (“Pointe”); letter from R.F. Lafferty & Co., Inc., dated December 30, 2008 (“Lafferty”); letter from Wachovia Securities, LLC, dated December 30, 2008 (“Wachovia”); letter from Financial Telesis, Inc., dated January 5, 2009 (“Telesis”); letter from Askar Corp., dated January 6, 2009 (“Askar”); letter from Investment Company Institute, dated January 15, 2009 (“ICI”); letter from Northwestern Mutual Investment Services, LLC, dated January 15, 2009 (“Northwestern”); letter from Charles Schwab & Co., Inc., dated January 16, 2009 (“Schwab”); letter from Financial Services Institute, Inc., dated January 16, 2009 (“FSI”); letter from National Society of Compliance Professionals, Inc., dated January 16, 2009 (“NSCP”); letter from PFS Investments, Inc., dated January 16, 2009 (“PFS”); letter from the Securities Industry and Financial Markets Association, dated January 16, 2009 (“SIFMA”); and letter from State Farm VP Management Corp., dated January 16, 2009 (“State Farm”).

¹¹ Askar, GBS, Goodwin, Lafferty, OmniCap, Pointe and Telesis support NAIBD’s comments. Northwestern submitted its own comments, but it also supports FSI’s comments.

¹² The Commission notes that these documents are attached to the filing, not to this notice.

“should have known” standard is too demanding.¹³ The purpose of the “should have known” standard is to ensure that members do not intentionally avoid becoming aware of a reportable event.¹⁴ FINRA does not believe that this standard, which has been a part of NASD Rule 3070 since its adoption, is too demanding.

2. External Findings (Proposed FINRA Rule 4530(a)(1)(A))

Several commenters argue that the proposed rule, including the requirement to report external findings relating to “insurance” matters, is too expansive and unduly burdensome.¹⁵ As noted above, the proposed rule actually limits the scope of current reportable external findings and requires firms to report external findings related to the financial services industry (*i.e.*, securities, insurance, commodities, financial or investment related). Additionally, the requirement to report matters related to the financial services industry, such as “insurance” and “commodities” matters, is consistent with other provisions of the current rules. This information assists FINRA in identifying and investigating firms, offices and associated persons that may pose a regulatory risk. Some of these commenters are also concerned that the proposed rule may reach the activities of affiliates.¹⁶ Similar to NASD Rule 3070, the proposed rule is limited to findings against a firm or an associated person of the firm.

Some commenters believe that the proposed term “business or professional organization” is overly broad and vague compared to the current term “financial business or professional organization.”¹⁷ The proposed rule requires firms to report a business or professional

¹³ NSCP.

¹⁴ See also Securities Exchange Act Release No. 35956 (July 11, 1995), 60 FR 36838 (July 18, 1995) (Notice of File No. SR-NASD-95-16).

¹⁵ FSI, NAIBD, Northwestern, NSCP and State Farm.

¹⁶ FSI, Northwestern and NSCP.

¹⁷ NAIBD, NSCP and Wachovia.

organization's findings of violations relating to securities, insurance, commodities, financial or investment-related matters. For instance, a finding of violation of the Code of Professional Conduct of the American Institute of Certified Public Accountants is an example of the type of finding by a business or professional organization that is reportable under the proposed rule.

3. Civil Litigation or Arbitration; Other Claims for Damages (Proposed FINRA Rule 4530(a)(1)(G))

As originally proposed in Regulatory Notice 08-71, the rule required members to report any insurance-related civil litigation or arbitration. The purpose of this proposed change was to make the provision consistent with other provisions of NASD Rule 3070 and NYSE Rule 351 that require the reporting of regulatory matters relating to insurance. Several commenters argued that the proposed requirement will result in voluminous reporting regarding insurance matters completely unrelated to securities activities (e.g., auto and health).¹⁸ In response, FINRA has revised the proposed rule to require the reporting of any "insurance" civil litigation or arbitration that is "financial related." One of these commenters also argued that the requirement to report "any other claim for damages" by a customer or broker-dealer is too expansive since it may require the reporting of a wide array of matters (e.g., family grievances).¹⁹ In response to this comment, FINRA has revised the proposed rule to require the reporting of any claim for damages by a customer or broker-dealer that is "financial" or "transactional" in nature.

One commenter asks that FINRA clarify that matters reportable under the proposed rule continue to be subject to the current dollar thresholds for reporting (\$15,000 for associated

¹⁸ CAI, Cutter, Farmers, FSI, NSCP, Schwab and State Farm.

¹⁹ Cutter.

persons; \$25,000 for firms).²⁰ In response to this comment, FINRA has revised the proposed rule to clarify this point.

Several commenters suggest that the current dollar thresholds for reporting are too low and outdated.²¹ FINRA believes that the current dollar thresholds continue to be consistent with the purposes of the rule. In addition, the \$15,000 reporting threshold for an associated person is consistent with the Forms U4 and U5 current reporting thresholds.

4. Statutory Disqualifications (Proposed FINRA Rule 4530(a)(1)(H))

As noted above, the proposed rule replaces the current requirement to report whenever a firm or an associated person of the firm “is associated in any business or financial activity” with a person subject to a “statutory disqualification” with a requirement to report whenever the firm or an associated person of the firm “is involved in the sale of any financial instrument, the provision of any investment advice or the financing of any such activities” with a person subject to a “statutory disqualification.” Two commenters ask whether the term “investment advice” in the proposed rule refers to advisory activities and suggest that the inclusion of such activities broadens the scope of NASD Rule 3070(a)(9) and NYSE Rule 351(a)(9).²² FINRA notes that advisory activities are covered under the current rules (i.e., considered a “financial activity”) and will continue to be covered under the proposed rule. One of these commenters also requests that FINRA Rule 4530(a)(1)(H) include the phrase “knows or should have known,” which is currently in NASD Rule 3070(a)(9).²³ As discussed above, FINRA is proposing to consolidate

²⁰ State Farm.

²¹ CAI, FSI and NSCP.

²² Cutter and NAIBD.

²³ NAIBD.

in a single paragraph, FINRA Rule 4530(a), the various references to the “knows or should have known” standard.

5. Internal Disciplinary Actions Against Associated Persons (Proposed FINRA Rule 4530(a)(2))

Several commenters suggest that the current \$2,500 threshold for reporting internal disciplinary actions is too low and outdated.²⁴ FINRA believes that the current dollar threshold continues to be consistent with the purposes of the rule.

6. Internal Conclusions (Proposed FINRA Rules 4530(b) and 4530.01)

Several commenters believe that the proposed provisions are unnecessary, unduly burdensome, overly broad and costly.²⁵ These commenters also argue that the provisions are vague and too subjective and that certain terms, such as “the member has concluded,” “isolated” and “ministerial,” need further clarification. For instance, one commenter asks whether internal conclusions that are equivalent to minor rule violations will have to be reported.²⁶ One commenter recommends that the proposal exclude either a “ministerial” or “non-material” violation.²⁷ One commenter suggests that the requirement be limited to those matters that result in “material customer harm.”²⁸ Another commenter recommends that the requirement be limited to matters that result in “customer harm.”²⁹ Some of these commenters also suggest that if FINRA opts to retain the proposed requirement, it adopt the reporting standard set forth in NYSE Information Memorandum 06-11, which provides that if a firm determines not to impose

²⁴ CAI, FSI and NSCP.

²⁵ CAI, FSI, ICI, Northwestern, NSCP, PFS, Schwab, SIFMA and State Farm.

²⁶ Schwab.

²⁷ ICI.

²⁸ Northwestern.

²⁹ FSI.

discipline against an individual, the firm need only report any recidivist or ongoing violative conduct by the individual.³⁰ NYSE Information Memorandum 06-11 also provides that a firm need only report systemic firm failures involving numerous customers, multiple errors or significant dollar amounts, as well as violative conduct by the firm or its employees that has widespread or potential widespread impact to the firm, its customers or the industry.

FINRA believes that the standard set forth in Information Memorandum 06-11 is too narrow. However, in response to the comments, FINRA has provided an example in Item II.A. of this filing of the types of reportable and non-reportable matters.

One commenter suggests that the proposed requirement be limited to conclusions reached at a senior level.³¹ Another commenter requests that FINRA clarify that a settlement with a customer does not create the presumption that a reportable violation has occurred.³² Additionally, one commenter asks whether internal audit findings are deemed internal conclusions.³³ FINRA believes that a firm is free to determine the level of seniority required of an associated person in making a determination of a reportable internal conclusion; however, it will not be a defense to a failure to report such conduct that it was of a nature that did not merit consideration by a person of such seniority. With respect to settlements, it is not the fact that a firm has settled a matter that makes it a reportable event under FINRA Rule 4530(b), rather it is whether the firm has reached an internal conclusion or reasonably should have reached an internal conclusion that the firm or an associated person has engaged in the enumerated violative

³⁰ FSI, NSCP, PFS, Schwab and SIFMA.

³¹ CAI.

³² PFS.

³³ NSCP.

conduct.³⁴ Regarding internal audit findings, FINRA believes that the existence of such findings creates a strong presumption that the matter is reportable, but that any particular finding is eligible to be viewed by the firm as non-reportable (i.e., an isolated, ministerial violation that did not result in customer harm and was remedied promptly upon discovery).

Further, two commenters believe that matters subject to a firm's internal review process as required under other rules (e.g., FINRA Rule 3130 (Annual Certification of Compliance and Supervisory Processes)) should be excluded from the proposed requirement.³⁵ FINRA believes that firms have an obligation to meet each of their regulatory requirements (including the requirements of FINRA Rule 3130) and that the obligation to meet a regulatory requirement is not superseded based on compliance with other regulatory requirements.

Additionally, some commenters suggest that the proposed requirement may have a chilling effect on a firm's willingness to reach such conclusions or that reporting such information, which may lack qualified or total immunity, may result in defamation suits.³⁶ Without opining on the issues raised by these commenters, FINRA questions the collateral effects posited by the commenters given the use of the information for FINRA internal examination and enforcement purposes and that, in any event, FINRA believes that the goals of customer protection and market integrity necessitate the reporting of such conduct to FINRA.

7. Domestic and Foreign Actions and Actions By a Regulatory Body
(Proposed FINRA Rules 4530(a)(1)(A), (C), (D), (F) and 4530.04)

³⁴ Firms should note that certain settlements will have to be reported based on other reporting requirements (e.g., FINRA Rule 4530(a)(1)(G)).

³⁵ CAI and ICI.

³⁶ CAI, FSI and Schwab.

One commenter suggests that it may be too difficult to obtain information from foreign regulatory bodies.³⁷ In general, firms should report the information in their custody, possession, or control or to which they have knowledge and provide an explanation in the appropriate reporting system fields of the information that they were unable to obtain due to circumstances beyond their control. In addition, as noted above, firms cannot intentionally avoid becoming aware of a reportable event.

8. Quarterly Statistical and Summary Information Regarding Written Customer Complaints (Proposed FINRA Rule 4530(d))

One commenter argues that the requirement to report quarterly statistical and summary information regarding written customer complaints, including emails, is unduly burdensome and wants to know how the data is used and how it benefits the industry.³⁸ FINRA uses the reported information for its internal examination and enforcement purposes. Among other things, the information assists FINRA to identify and investigate firms, offices and associated persons that may pose a regulatory risk.

Additionally, in response to one commenter,³⁹ FINRA wishes to clarify an interpretive position related to FINRA Rule 4530(c). In Notice to Members 96-85, FINRA (then NASD) stated that for purposes of reporting written customer complaints under NASD Rule 3070(c), the term “customer” is defined as any person other than a broker-dealer with whom the member has engaged, or has sought to engage, in securities activities, therefore, it was intended to exclude non-securities products. A member is not required to report written complaints relating to non-securities products, but only to the extent that such complaints are not from customers that the

³⁷ NSCP.

³⁸ Puplava.

³⁹ Schwab.

member has engaged, or has sought to engage, in securities activities. However, if a member has engaged, or has sought to engage, in securities activities with a person, then any written complaint from that person is reportable under the proposed rule, regardless of whether it relates to non-securities products.⁴⁰

9. Reporting Obligation (Proposed FINRA Rule 4530(e))

As originally proposed in Regulatory Notice 08-71, the rule required members to report an event under the rule regardless of whether the event was disclosed on the Forms BD, U4 or U5. Several commenters raised concerns regarding this obligation.⁴¹ FINRA has revised the proposed rule to provide that a firm is not required to report an event otherwise required to be reported under FINRA Rules 4530(a) or (b) if the firm has disclosed the event on the Form U5, consistent with the requirements of that form. This exception to FINRA Rules 4530(a) and (b) only applies to information that has been disclosed on the Form U5. As noted above, FINRA will also work toward the goal of eliminating duplicative reporting of information disclosed on the Forms BD and U4.

10. Filing of Related Documents with FINRA (Proposed FINRA Rule 4530(f))

As originally proposed in Regulatory Notice 08-71, the rule required members to file, in addition to report, any insurance-related civil litigation or arbitration. Several commenters argued that the proposed requirement will result in voluminous filings regarding insurance

⁴⁰ FINRA notes that the original proposal in Regulatory Notice 08-71 included a provision reminding firms of their obligations under proposed FINRA Rule 3110(b)(5) to have procedures to capture, acknowledge and respond to all written (including electronic) customer complaints. Proposed FINRA Rule 3110(b)(5) is part of the proposed consolidated supervision rules. See Regulatory Notice 08-24 (May 2008) (Proposed Consolidated FINRA Rules Governing Supervision and Supervisory Controls). FINRA will consider whether to re-propose the reference to FINRA Rule 3110(b)(5) at a later date.

⁴¹ CAI, Cutter, FSI, NAIBD, NSCP, Schwab and SIFMA.

matters completely unrelated to securities activities.⁴² Consistent with the revisions to FINRA Rule 4530(a)(1)(G) discussed above, FINRA Rule 4530(f) has been revised to require the filing of copies of any “insurance” civil litigation complaint or arbitration claim that is “financial related.”

11. Calculation of Monetary Thresholds and Former Associated Persons
(Proposed FINRA Rules 4530.06 and .07)

Several commenters raise concerns regarding the inclusion of attorneys fees and interest when calculating the dollar thresholds for reporting civil litigations, arbitrations or other claims for damages.⁴³ Based on FINRA’s experience, some firms have considered structuring settlements using attorneys fees to avoid the dollar thresholds for reporting. The inclusion of attorneys fees and interest in the proposed rule is intended to address this concern. One commenter believes that “joint and several” liability should not be aggregated for purposes of the proposed rule.⁴⁴ As noted above, since each party subject to “joint and several” liability is separately liable for the aggregate amount, the aggregate amount must be reported for each party. For instance, if two parties have “joint and several” liability for \$40,000, the amount reported would be \$40,000 for each party.

Some commenters are also concerned that it may be too difficult to obtain information from former associated persons.⁴⁵ As discussed above, in general, firms should report the information in their custody, possession, or control or to which they have knowledge and provide an explanation in the appropriate reporting system fields of the information that they were unable

⁴² CAI, Farmers, NSCP and State Farm.

⁴³ CAI, Cutter, FSI, NAIBD, Northwestern, NSCP, Schwab and SIFMA.

⁴⁴ Schwab.

⁴⁵ CAI, FSI, Northwestern and NSCP.

to obtain due to circumstances beyond their control, with the understanding that firms cannot intentionally avoid becoming aware of a reportable event.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove the proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. 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 e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2010-034 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2010-034. This file number should be included on the subject line if e-mail 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 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 the 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 available publicly. All submissions should refer to File Number SR-FINRA-2010-034 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁶

Florence E. Harmon
Deputy Secretary

⁴⁶ 17 CFR 200.30-3(a)(12).