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Filing by **Financial Industry Regulatory Authority**  
 Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

<b>Initial *</b> <input type="checkbox"/>	<b>Amendment *</b> <input checked="" type="checkbox"/>	<b>Withdrawal</b> <input type="checkbox"/>	<b>Section 19(b)(2) *</b> <input checked="" type="checkbox"/>	<b>Section 19(b)(3)(A) *</b> <input type="checkbox"/>	<b>Section 19(b)(3)(B) *</b> <input type="checkbox"/>
<b>Pilot</b> <input type="checkbox"/>	<b>Extension of Time Period for Commission Action *</b> <input type="checkbox"/>	<b>Date Expires *</b> <input type="text"/>	Rule <input type="checkbox"/> 19b-4(f)(1) <input type="checkbox"/> 19b-4(f)(4) <input type="checkbox"/> 19b-4(f)(2) <input type="checkbox"/> 19b-4(f)(5) <input type="checkbox"/> 19b-4(f)(3) <input type="checkbox"/> 19b-4(f)(6)		

<b>Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010</b>	<b>Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934</b>
<b>Section 806(e)(1) *</b> <input type="checkbox"/>	<b>Section 806(e)(2) *</b> <input type="checkbox"/>
	<b>Section 3C(b)(2) *</b> <input type="checkbox"/>

<b>Exhibit 2 Sent As Paper Document</b> <input type="checkbox"/>	<b>Exhibit 3 Sent As Paper Document</b> <input type="checkbox"/>
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**Description**  
 Provide a brief description of the action (limit 250 characters, required when Initial is checked \*)

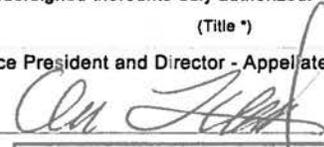
**Contact Information**  
 Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

<b>First Name *</b> Afshin	<b>Last Name *</b> Atabaki
<b>Title *</b> Associate General Counsel	
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**Signature**  
 Pursuant to the requirements of the Securities Exchange Act of 1934,  
 has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

(Title \*)  
 Vice President and Director - Appellate Group

Date   
 By   
 (Name \*)

  
 Alan Lawhead, alan.lawhead@finra.org

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

**Form 19b-4 Information \***

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change \***

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies \***

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit Sent As Paper Document

**Exhibit 3 - Form, Report, or Questionnaire**

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit Sent As Paper Document

**Exhibit 4 - Marked Copies**

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

**1. Text of the Proposed Rule Change**

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “SEA”),<sup>1</sup> Financial Industry Regulatory Authority, Inc. (“FINRA”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) Amendment No. 1 to SR-FINRA-2014-038, a proposed rule change to adopt NASD Rule 3010(e) (Qualifications Investigated) relating to background investigations as FINRA Rule 3110(e) (Responsibility of Member to Investigate Applicants for Registration) in the consolidated FINRA rulebook. The proposed rule change streamlines and clarifies the rule language and adds a provision to require members to adopt written procedures that are reasonably designed to verify the accuracy and completeness of the information contained in an applicant’s Form U4 (Uniform Application for Securities Industry Registration or Transfer). In addition, the proposed rule change adds Supplementary Material .15 (Temporary Program to Address Underreported Form U4 Information) to FINRA Rule 3110 (Supervision) to establish a temporary program that will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M, subject to specified conditions.

The proposed rule change would delete NASD Rule 3010(f) (Applicant’s Responsibility), Incorporated NYSE Rule 345.11 (Investigation and Records) and Incorporated NYSE Rule Interpretation 345.11/01 (Application – Investigation) and /02 (Application – Records).

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

The text of the proposed rule change is attached as Exhibit 5.

(b) Upon Commission approval and implementation by FINRA of the proposed rule change, NASD Rule 3010(e), NASD Rule 3010(f), Incorporated NYSE Rule 345.11 and Incorporated NYSE Rule Interpretation 345.11/01 and /02 will be eliminated from the current FINRA rulebook.

(c) Not applicable.

**2. Procedures of the Self-Regulatory Organization**

At its meeting on April 24, 2014, the FINRA Board of Governors authorized the filing of the proposed rule change with the SEC. No other action by FINRA is necessary for the filing of the proposed rule change.

FINRA proposes to implement proposed FINRA Rule 3110(e) on July 1, 2015. Proposed FINRA Rule 3110.15 has a retroactive effective date of April 24, 2014, and it will automatically sunset on July 31, 2015.

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

(a) Purpose

Rule Filing History

On September 18, 2014, FINRA filed with the SEC SR-FINRA-2014-038,<sup>2</sup> a proposed rule change to adopt NASD Rule 3010(e) relating to background investigations as FINRA Rule 3110(e) in the consolidated FINRA rulebook ("Consolidated FINRA

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<sup>2</sup> See Securities Exchange Act Release No. 73238 (September 26, 2014), 79 FR 59884 (October 3, 2014) (Notice of Filing of SR-FINRA-2014-038) ("Proposing Release"). The comment period closed on October 24, 2014.

Rulebook”).<sup>3</sup> The proposed rule change was published for comment in the Federal Register on October 3, 2014. The Commission received 10 comment letters in response to the proposed rule change.<sup>4</sup> Based on comments received, FINRA is filing this Amendment No. 1 to respond to the comments and to propose amendments, where appropriate.

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<sup>3</sup> 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).

<sup>4</sup> See Letter from Suzanne Shatto to Brent J. Fields, Secretary, SEC, dated October 6, 2014 (“Shatto”); Letter from Joseph C. Peiffer, Executive Vice President and President-Elect, Public Investors Arbitration Bar Association, to Brent J. Fields, Secretary, SEC, dated October 16, 2014 (“PIABA”); Letter from William A. Jacobson, Clinical Professor of Law, Cornell University Law School, to Brent J. Fields, Secretary, SEC, dated October 20, 2014 (“Cornell”); Letter from William Beatty, President, North American Securities Administrators Association, Inc., to Brent J. Fields, Secretary, SEC, dated October 22, 2014 (“NASAA”); Letter from Kyle Ortiz and Kathryn Hespe, Law Student Clinicians, Investor Advocacy Clinic, Michigan State University College of Law, to Brent J. Fields, Secretary, SEC, dated October 23, 2014 (“Michigan State”); Letter from John Astarita and Olivia Darius, Student Interns, John Jay Legal Services, Inc., Pace University School of Law, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“Pace”); Letter from Kevin Zambrowicz, Associate General Counsel and Managing Director, the Securities Industry and Financial Markets Association, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“SIFMA”); Letter from Michele Van Tassel, President, Association of Registration Management, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“ARM”); Letter from Robert J. McCarthy, Director of Regulatory Policy, Wells Fargo Advisors, LLC, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“Wells Fargo”); and Letter from David T. Bellaire, Executive Vice President and General Counsel, the Financial Services Institute, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“FSI”). (Available at <http://www.sec.gov/comments/sr-finra-2014-038/finra2014038.shtml>.)

Proposal

As described in the Proposing Release, as part of the process of developing the Consolidated FINRA Rulebook, FINRA is proposing to adopt NASD Rule 3010(e) relating to background investigations as FINRA Rule 3110(e).

FINRA is proposing to streamline and clarify the rule language. For instance, NASD Rule 3010(e) currently provides that “[e]ach member shall have the responsibility and duty to ascertain by investigation the good character, business repute, qualifications, and experience of any person prior to making such a certification in the application of such person for registration with this Association,” whereas proposed FINRA Rule 3110(e) provides that “[e]ach member shall ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before making a representation to that effect on the application for registration.” Further, proposed FINRA Rule 3110(e) clarifies that a firm is required to review a copy of an applicant’s most recent Form U5 (Uniform Termination Notice for Securities Industry Registration) if the applicant previously has been registered with FINRA or another self-regulatory organization. FINRA also is proposing to re-label current FINRA Rule 3110(e) (Definitions) as FINRA Rule 3110(f) (Definitions) and update the cross-references in FINRA Rule 3110 to reflect this change.

In addition, FINRA is proposing to include in proposed FINRA Rule 3110(e) a requirement that firms adopt written procedures that are reasonably designed to verify the accuracy and completeness of the information contained in an applicant’s Form U4 no later than 30 calendar days after the form is filed with FINRA. The proposed requirement

would only apply to an initial or a transfer Form U4 for an applicant for registration, and not to Form U4 amendments. Proposed FINRA Rule 3110(e) would also require that a firm's written procedures must, at a minimum, provide for a national search of reasonably available public records conducted by the member or a third-party service provider to verify the accuracy and completeness of the information contained in an applicant's Form U4. The requirement to conduct a public records search must be satisfied no later than 30 calendar days after the initial or transfer Form U4 is filed with FINRA, with the understanding that if a member becomes aware of any discrepancies as a result of a public records search conducted after the filing of the Form U4, the member would be required to file an amended Form U4 with FINRA.

Further, FINRA is proposing to add proposed Supplementary Material .15 to FINRA Rule 3110 to establish a temporary program that will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M, subject to specified conditions.

The proposed rule change would delete NASD Rule 3010(f) because it has been rendered obsolete. The proposed rule change would also delete Incorporated NYSE Rule 345.11<sup>5</sup> and NYSE Rule Interpretation 345.11/01 and /02 as they are substantially similar to proposed FINRA Rule 3110(e), addressed by other rules or otherwise rendered obsolete by the approach reflected in proposed FINRA Rule 3110(e).

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<sup>5</sup> For convenience, the proposed rule change refers to Incorporated NYSE Rules as NYSE Rules.

Response to Comments

A. Overview of Comments

Three commenters supported the proposal without any qualifications.<sup>6</sup> Three commenters supported the proposal, but had a few suggestions, including extending the scope of the proposed public records search to foreign jurisdictions,<sup>7</sup> clarifying the term “reasonably available public records,”<sup>8</sup> and limiting the proposed refund program to a one-time program.<sup>9</sup> Two of these commenters also requested additional clarification regarding the requirements under proposed FINRA Rule 3110(e).<sup>10</sup> One commenter supported the consolidation of NASD Rule 3010(e) and NYSE Rule 345.11 as proposed FINRA Rule 3110(e), but (1) requested further clarification regarding the investigation and verification requirements; (2) suggested changes to the verification requirement, to the implementation date of the proposal and to the sunset date of the refund program; and (3) requested clarification regarding Questions 14K and 14M on the Form U4.<sup>11</sup> Finally, two commenters supported the purpose of the verification requirement, but requested additional clarification regarding its scope,<sup>12</sup> and suggested changes to the refund

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<sup>6</sup> Shatto, NASAA and Michigan State.

<sup>7</sup> PIABA.

<sup>8</sup> Cornell.

<sup>9</sup> Pace.

<sup>10</sup> PIABA and Cornell.

<sup>11</sup> SIFMA. Wells Fargo supported SIFMA’s comment letter.

<sup>12</sup> ARM.

program.<sup>13</sup> One of these commenters also requested clarification regarding Questions 14K and 14M on the Form U4.<sup>14</sup>

B. Relationship Between Requirements of Proposed FINRA Rule 3110(e)

Several commenters requested that FINRA clarify the relationship between the requirements under proposed FINRA Rule 3110(e).<sup>15</sup> Two of these commenters also asked whether the investigation and verification requirements are duplicative, whether firms can use any of the information obtained in the investigation process to comply with the verification process and whether firms are required to conduct the verification process after the Form U4 has been filed and separate from the investigation process.<sup>16</sup>

Although the requirements of proposed FINRA Rule 3110(e) are closely related, the requirements are complementary, not duplicative, in nature. The requirements essentially come together to form an overarching process for the background investigation of applicants for registration.

First, proposed FINRA Rule 3110(e) requires that each member ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before making a representation to that effect on the application for registration.<sup>17</sup> This is a

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<sup>13</sup> FSI.

<sup>14</sup> FSI.

<sup>15</sup> PIABA, Cornell, SIFMA and ARM.

<sup>16</sup> SIFMA and ARM.

<sup>17</sup> Firms must comply with MSRB Rule G-7 (Information Concerning Associated Persons) regarding those applicants engaged solely in municipal securities activities.

principle-based requirement, and it is substantially similar to the current requirement under NASD Rule 3010(e). Firms are required to complete the investigation process prior to filing the Form U4. Further, FINRA does not place any limits on the scope of such a background investigation – a firm must obtain all the necessary information to make an evaluation.<sup>18</sup> Firms should consider all available information gathered in the pre-registration process for this purpose, including, but not limited to, Form U4 and Form U5 responses, authorized searches of the Central Registration Depository (CRD®) system, fingerprint results obtained under SEA Rule 17f-2 and communications with previous employers.<sup>19</sup> Firms also may wish to consider private background checks, credit reports and reference letters for this purpose.<sup>20</sup> However, firms must ensure that such background investigations are conducted in accordance with all applicable laws, rules and regulations, including federal and state requirements, and that all necessary approvals, consents and authorizations have been obtained.<sup>21</sup>

Second, if an applicant previously has been registered with FINRA or another self-regulatory organization, proposed FINRA Rule 3110(e) requires that a firm review a copy of the applicant's most recent Form U5, including any amendments, within 60 days

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<sup>18</sup> See Regulatory Notice 07-55 (November 2007).

<sup>19</sup> See supra note 18.

<sup>20</sup> See supra note 18.

<sup>21</sup> See supra note 18.

of the filing date of the applicant's Form U4.<sup>22</sup> If the firm is unable to review the Form U5, it has to demonstrate that it has made reasonable efforts to do so.<sup>23</sup> This requirement also is substantially similar to the current requirement under NASD Rule 3010(e).

Third, proposed FINRA Rule 3110(e) requires that a firm establish and implement written procedures reasonably designed to verify the accuracy and completeness of the information contained in an applicant's Form U4 by no later than 30 calendar days after an initial or a transfer Form U4 is filed with FINRA. While this is a new requirement, it is based on an underlying requirement in the Form U4 that the person signing the form on behalf of the firm certify that he or she has taken appropriate steps to verify the accuracy and completeness of the information contained in and with that form. Proposed FINRA Rule 3110(e) expressly requires that a firm's written procedures specify the firm's process for verifying the information in the Form U4 and that the firm complete that verification process by no later than 30 calendar days after the Form U4 is filed.

FINRA understands that the verification process could vary firm by firm. For instance, one firm may verify an applicant's identity and name by checking a valid state-issued driver's license whereas another firm may do so by reviewing a valid government-issued passport. Further, the verification process for some of the information in the Form U4 is embedded in the form itself. For example, the Form U4 provides that the person

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<sup>22</sup> If the applicant has been recently employed by a Futures Commission Merchant or an Introducing Broker that is notice-registered with the SEC pursuant to Section 15(b)(11) of the Act, the registering firm also is required to review a copy of the individual's most recent CFTC Form 8-T.

<sup>23</sup> FINRA expects firms to use this provision in very limited circumstances, such as where the previous firm fails to file a Form U5 or goes out of business before filing a Form U5.

signing the form on behalf of the firm certify that the firm has communicated with the applicant's previous employers for the past three years and has documentation on file with the names of the persons contacted and the date of contact. Moreover, FINRA does not expect firms to verify all of the information in the Form U4 where such verification is not feasible or practical. However, in such cases, a firm should document that the information could not be verified and the basis for it.

Under proposed FINRA Rule 3110(e), firms must complete the verification process by no later than 30 calendar days after the Form U4 is filed with FINRA. Proposed FINRA Rule 3110(e) does not require firms to conduct the verification process only during the 30-day window after the Form U4 has been filed or base the verification on information that is obtained only in the 30-day window after the form has been filed. Rather, the 30-day window is intended to accommodate firms that may find it difficult to conduct the verification process before filing an applicant's Form U4, such as where an applicant is hired immediately to fill a needed role at the firm. For most applicants, FINRA expects that firms will conduct the investigation and verification process concurrently using some of the same information and prior to filing the Form U4. Moreover, FINRA encourages firms to complete the verification process prior to filing the Form U4. In this regard, as is the case today with respect to amended filings, a firm will be subject to a Late Disclosure Fee if the disclosure event should have been reported on the initial or transfer Form U4, regardless of whether the firm completes the verification process within the 30-day window in proposed FINRA Rule 3110(e).

FINRA also recognizes that there will on occasion be circumstances beyond a firm's control that prevent completion of the verification process within the 30-day

window after the Form U4 is filed with FINRA. For example, a firm may not be able to comply with the proposed 30-day window where the firm is relying on fingerprint results for verifying criminal information, and the FBI determines the fingerprints to be “illegible” and requires resubmission of the fingerprints. In such circumstances, the firm’s procedures should provide that the verification must be completed as soon as practical, and the firm should document the basis for the delay.

Finally, proposed FINRA Rule 3110(e) requires that a firm’s verification process must, at a minimum, provide for a national search of reasonably available public records conducted by the firm or a third-party service provider to verify the accuracy and completeness of the information contained in an applicant’s Form U4. Similar to the overall verification process, the requirement to conduct a public records search must be satisfied by no later than 30 calendar days after an initial or a transfer Form U4 is filed with FINRA. The public records search is a new requirement, and it is a mandatory component of the overall verification process described above. Public records include, but are not limited to: general information, such as name and address of individuals; criminal records; bankruptcy records; civil litigations and judgments; liens; and business records. However, proposed FINRA Rule 3110(e) only requires a national search of reasonably available public records. The scope of what is considered reasonably available public records may change over time, but FINRA understands that currently such records include criminal records, bankruptcy records, judgments and liens. This is a minimum or base requirement. A firm may find it necessary to conduct a more in-depth search of public records depending on the applicant’s job function, responsibilities or position at the firm.

As stated in the Proposing Release, a firm could comply with the requirement to conduct a national search of reasonably available public records in several ways. For example, a firm may satisfy the requirement by: (1) reviewing a credit report from a major national credit reporting agency that contains public record information (such as bankruptcies, judgments and liens) and the applicant's fingerprint results;<sup>24</sup> (2) searching a reputable national public records database and reviewing the applicant's fingerprint results; or (3) reviewing a consolidated report from a specialized provider, such as Business Information Group, Inc. (BIG),<sup>25</sup> that includes criminal and financial public records. Moreover, as explained above, the scope of the requirement is limited to reasonably available public records, which currently include criminal records, bankruptcies, judgments and liens. FINRA notes that the proposed public records search requirement does not require firms to obtain a credit report, which contains both public

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<sup>24</sup> Firms currently have an obligation to comply with SEA Rule 17f-2. Pursuant to SEA Rule 17f-2, specific persons employed in the securities industry are required to be fingerprinted for purposes of a criminal background check. Firms are responsible for obtaining a prospective employee's fingerprints and required identifying information. Firms then submit the prospective employee's fingerprints together with the required identifying information to FINRA. FINRA, in turn, submits these fingerprints to the FBI. FINRA also makes the fingerprint results available to the employing member and regulators, consistent with applicable federal laws and FBI and FINRA requirements. See Notice to Members 05-39 (May 2005). Firms may rely on these fingerprint results to comply with the requirement to conduct a public records search of criminal records.

<sup>25</sup> FINRA has contracted with BIG to provide competitive pricing to members that are conducting background investigations of applicants, currently at a cost of \$10 to \$13 per applicant (depending on volume). In general, FINRA does not endorse any particular third-party service and a firm's use of BIG's services, or the services of any other specific provider, would not be deemed to be a safe harbor by FINRA.

and non-public records. FINRA included a credit report in the list above as an example of a type of document that includes reasonably available public records. FINRA further reiterates that, as is the case with the investigative process, firms must ensure that such public records searches are conducted in accordance with all applicable laws, rules and regulations, including federal and state requirements, and that all necessary approvals, consents and authorizations have been obtained.

C. Member's Obligation to Adopt Written Procedures for Verification of Information in the Form U4 (Proposed FINRA Rule 3110(e))

Two commenters asked whether firms are required to verify all of the information in the Form U4 and stated that it may not be feasible or practical to do so in some cases.<sup>26</sup> For example, one of these commenters stated that existing resources do not allow firms to verify the response to Question 13 (Other Business) on the Form U4, and the commenter was not aware of a central data source that could serve to verify for an applicant's outside business.<sup>27</sup> As discussed above, FINRA does not expect firms to verify all of the information in the Form U4 where such verification is not feasible or practical. However, in such cases, a firm should document that the information could not be verified and the basis for it.

One commenter recommended that the proposed verification requirement, including the minimum public records search requirement, be removed altogether.<sup>28</sup> Alternatively, the commenter requested that firms should be given 90 days to complete a

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<sup>26</sup> SIFMA and ARM.

<sup>27</sup> ARM.

<sup>28</sup> SIFMA.

public records search and any necessary follow ups and asked whether firms are required to complete the entire verification process within the proposed 30-day window. One commenter requested that firms should be given a 60- or 90-day period to complete the verification process.<sup>29</sup> Another commenter suggested that FINRA amend the proposed rule text to require that a firm's written procedures provide that if the firm is unable to complete the verification process within the 30-day window, it must demonstrate to FINRA that it has made reasonable efforts to do so and explain the cause for the delayed verification.<sup>30</sup>

FINRA is retaining the proposed Form U4 verification requirement and the minimum requirement to conduct a public records search. FINRA continues to believe that the proposed requirements will enhance the accuracy of the information in the CRD system and ultimately in BrokerCheck, which is critical from both a regulatory and an investor protection standpoint. Further, as described above, firms must complete the verification process by no later than 30 calendar days after the Form U4 is filed with FINRA. For most applicants, FINRA expects that firms will conduct the proposed verification process, including the public records search, prior to filing the Form U4. Moreover, FINRA encourages firms to complete the verification process prior to filing the Form U4.

FINRA does not believe that it is necessary to extend the period by which firms must complete the verification process for the following reason. Pursuant to the FINRA

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<sup>29</sup> ARM.

<sup>30</sup> PIABA.

By-Laws, a firm is obligated to file an amended Form U4 no later than 30 calendar days after learning of the facts or circumstances giving rise to the amendment.<sup>31</sup> Therefore, if a firm completes its verification process during the 30-day window in proposed FINRA Rule 3110(e) and learns of facts or circumstances that require the filing of an amended Form U4, the firm will continue to have 30 calendar days from the date it learns of such facts or circumstances to file an amended Form U4, provided that the firm will be subject to any applicable Late Disclosure Fees.

FINRA recognizes that there will on occasion be circumstances beyond a firm's control that prevent completion of the verification process within the 30-day window. In such cases, the firm's procedures should provide that the verification must be completed as soon as practical, and the firm should document the basis for the delay. FINRA does not believe that it is necessary to amend the proposed rule text to clarify this point.

One commenter requested that FINRA confirm that the proposed verification requirement, including the public records search, applies to an initial Form U4 filed with FINRA through the CRD system requesting registration with FINRA and that the proposed requirement does not apply to a Form U4 filed by an affiliate of a member or a registration transferred through the mass transfer process.<sup>32</sup> The commenter also suggested that FINRA replace the term "transfer Form U4" as used in the Proposing Release with the term "relicense Form U4" and amend the proposed rule text to include a reference to "an applicant's initial or relicense Form U4."

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<sup>31</sup> See FINRA By-Laws, Article V, Section 2(c).

<sup>32</sup> SIFMA.

The proposed verification requirement, including the public records search, applies to an initial Form U4 or a transfer Form U4. The term “initial Form U4” refers to the Form U4 filing required when an individual is registering with a FINRA member for the first time, including in the context of dual registration, or is registering with a FINRA member after more than two years have passed since the individual was last registered with a FINRA member. The term “transfer Form U4” refers to the Form U4 filing required when a registered person transfers from one FINRA member to another FINRA member. FINRA does not believe that it is necessary to replace the term “transfer Form U4” with the term “relicense Form U4” based on the explanation provided above. With respect to a Form U4 filed by a member that is an affiliate of another member, the verification requirement would apply to the filing to the extent that it is considered an initial or a transfer Form U4 (e.g., a dual registration). The proposed verification requirement would not apply to the mass transfer process because that process does not require the filing of a Form U4, which is the basis for the proposed verification requirement under proposed FINRA Rule 3110(e). FINRA is proposing to amend proposed FINRA Rule 3110(e) to clarify that the verification requirement, including the public records search, applies to an applicant’s initial or transfer Form U4.

**D. Member’s Obligation to Conduct a Search of Reasonably Available Public Records (Proposed FINRA Rule 3110(e))**

One commenter suggested that the public records search should extend to foreign jurisdictions in some circumstances, such as where an applicant has been registered with a foreign securities regulator or has resided in a foreign jurisdiction.<sup>33</sup> FINRA believes

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<sup>33</sup> PIABA.

that it is often difficult to assess the comparability of a foreign country's laws, rules and regulations to those in the United States, particularly as it relates to the purposes of this proposed rule, and believes, therefore, that the requirement should be limited to a national search of reasonably available public records. However, firms may find it necessary to conduct a search of public records in a foreign jurisdiction as part of their verification process and, where appropriate, should consider such a search consistent with applicable foreign laws, rules and regulations.

One commenter recommended that FINRA clarify the term "reasonably available public records" so that firms have an objective standard for compliance purposes.<sup>34</sup> One commenter stated that FINRA should revise the proposed rule text to specifically identify the information in the Form U4 that firms are expected to verify through a public records search or define the term "public records" so the scope of the requirement is less uncertain.<sup>35</sup> The commenter noted that business records are listed as an example of public records, but many business records (e.g., business formation documents) are not maintained in a comprehensive national database and may not be offered by a third-party service provider. While public records include, among other records, business records, proposed FINRA Rule 3110(e) only requires a national search of reasonably available public records. As stated above, the scope of what is considered reasonably available public records may change over time. Therefore, rather than define the term "reasonably available public records," FINRA believes that it is more useful for compliance purposes

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<sup>34</sup> Cornell.

<sup>35</sup> SIFMA.

to specify the public records that are currently considered reasonably available, which include criminal records, bankruptcy records, judgments and liens.

One commenter asked that FINRA confirm that, to the extent that the proposed rule requires firms to obtain an investigative consumer report for an applicant, firms can rely on the applicant's consent on a Form U4 (citing to Item 15A on the Form U4) for purposes of complying with applicable laws, rules and regulations requiring an applicant's consent to obtain such reports, otherwise firms will need to implement additional procedures to ensure compliance with such laws, rules and regulations in each jurisdiction.<sup>36</sup> The proposed rule does not require firms to obtain investigative consumer reports to comply with the requirements of the rule. Moreover, FINRA reiterates that a firm must continue to comply with all applicable laws, rules and regulations in the course of the registration process, as is the case today. Therefore, if a firm is relying on a particular report that requires an applicant's consent under the laws, rules and regulations of a particular jurisdiction, FINRA expects that the firm will obtain the requisite consent in accordance with such laws, rules and regulations. With respect to the commenter's request regarding the validity of an applicant's Form U4 consent, it is the responsibility of the registering firm to determine whether such consent is in compliance with the laws, rules and regulations of the particular jurisdiction in which the firm and the applicant are operating.

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<sup>36</sup> SIFMA.

E. Implementation Date of Proposed FINRA Rule 3110(e)

One commenter requested that FINRA extend the implementation date of proposed FINRA Rule 3110(e) from December 1, 2014 to December 1, 2015 so that firms have sufficient time to establish or revise their written procedures and address the operational issues resulting from the proposed rule.<sup>37</sup>

FINRA expects firms to have an existing process in place to verify the information contained in an applicant's Form U4 because currently the person signing the form on behalf of the firm must certify that he or she has taken appropriate steps to verify the accuracy and completeness of the information in the form. FINRA also understands that most firms already conduct some form of public records search. Therefore, the proposed new requirements should not create an unreasonable burden for firms.

However, FINRA recognizes that the proposed rule imposes an affirmative obligation on firms to establish and implement written procedures to comply with the Form U4 verification process to the extent they currently do not have such procedures and that such procedures must include a search of reasonably available public records. Thus, to accommodate any potential operational issues resulting from the proposed new requirements, FINRA is proposing to extend the implementation date of proposed FINRA Rule 3110(e) from December 1, 2014 to July 1, 2015.

F. Temporary Program to Address Underreported Form U4 Information  
(Proposed FINRA Rule 3110.15)

One commenter recommended that the refund program should be a one-time program and stated that FINRA should not use such programs in the future for late

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<sup>37</sup> SIFMA.

disclosure reporting because it may provide firms with negative reinforcement for untimely Form U4 reporting.<sup>38</sup> The refund program under proposed FINRA Rule 3110.15 is intended to incentivize members to report underreported information and save FINRA the time and regulatory resources expended in contacting firms and requesting that such information be reported. The program is intended to run concurrent with FINRA's one-time search of specific financial public records, and thus is of limited duration. FINRA may find it necessary to provide such programs in the future depending on the circumstances, but it will do so judiciously and only where appropriate.

Another commenter, while supportive of the purpose of the refund program, requested that FINRA consider adopting a more permanent refund program or extending the sunset date from March 31, 2015 to December 1, 2015.<sup>39</sup> The refund program is intended to run concurrent with FINRA's one-time search of specific financial public records on all registered persons, which FINRA expects to complete on or before August 2015. Because the refund program is intended to run concurrent with FINRA's search process, FINRA is extending the sunset date of the program from March 31, 2015 to July 31, 2015, which should provide firms additional time to identify and report information to FINRA.

One commenter suggested that Question 14M on the Form U4 is ambiguous and open to interpretation and requested that FINRA revise the eligibility conditions under the

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<sup>38</sup> Pace.

<sup>39</sup> SIFMA.

refund program to address this perceived ambiguity.<sup>40</sup> According to the commenter, Question 14M on the Form U4 is confusing because one could argue that if an unsatisfied judgment or lien is satisfied within the 30-day window of having to file an amended Form U4, the firm would not have to amend the Form U4 to mark “yes” because the lien is satisfied prior to the filing deadline. The commenter also stated that if a firm learns of an unreported satisfied lien, the language of Question 14M suggests that the firm does not have to report such lien because it is not currently unsatisfied. The commenter stated that FINRA should modify the program to refund members if the judgment or lien (1) occurred while the individual was registered with a prior firm; (2) is more than five years old; or (3) is under \$5,000. The commenter also asked whether the refund will be automated or whether firms have the burden to prove that they satisfy the conditions of the program to receive a refund.

As set forth in the Proposing Release, the temporary program would issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M (unsatisfied judgments or liens) if the following conditions are met: (1) the Form U4 amendment is filed between April 24, 2014 and March 31, 2015; (2) the judgment or lien is under \$5,000 and more than five years old (from the date the judgment or lien is filed with a court as reported on Form U4 Judgment/Lien DRP, Question 4); and (3) the registered person was not employed by, or otherwise associated with, the firm filing the amended Form U4 on the date the judgment or lien was filed with the court.

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<sup>40</sup> FSI.

FINRA is proposing to revise the refund program to address concerns regarding the assessment of the Late Disclosure Fee in circumstances where the unsatisfied judgment or lien has been satisfied, and at the time it was unsatisfied was of a relatively low amount (under \$5,000) and was reportable prior to the introduction of the procedures regarding the application of the Late Disclosure Fee to the reporting of judgments and liens on the Form U4 that became effective on August 13, 2012.<sup>41</sup> The proposed revisions also address circumstances where the failure to report related to a mistaken belief that satisfying the judgment or lien shortly after learning it was unsatisfied (within 30 calendar days of when it became unsatisfied) obviated the need to report the matter.<sup>42</sup> In addition, as noted above, FINRA is proposing to extend the sunset date of the refund program to July 31, 2015 (rather than March 31, 2015 as originally proposed).

As revised, the temporary program will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M (unsatisfied judgments or liens) if the Form U4 amendment is filed between April 24, 2014 and July 31, 2015 and one of the following conditions is met: (1) the judgment or lien has been satisfied, and at the time it was unsatisfied, it was under \$5,000 and the date the judgment or lien was filed with a court (as reported on Form U4 Judgment/Lien DRP,

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<sup>41</sup> See Information Notice August 17, 2012 (Late Disclosure Fee Related to Reporting of Judgment/Lien Events).

<sup>42</sup> FINRA believes that there is a misconception regarding the obligation to report unsatisfied judgments and liens under Question 14M on the Form U4. The obligation to amend a Form U4 arises on the date a registered person receives notice or learns that he or she is subject to an unsatisfied judgment or lien, and an amended Form U4 should be filed no later than 30 calendar days from that date, regardless of whether the registered person satisfies the judgment or lien in the interim period prior to the 30-day deadline for filing a Form U4 amendment.

Question 4.A.) was on or before August 13, 2012; or (2) the unsatisfied judgment or lien was satisfied within 30 days after the individual learned of the judgment or lien (as reported on Form U4 Judgment/Lien DRP, Question 4.B.). The revised program has a retroactive effective date of April 24, 2014, and it will automatically sunset on July 31, 2015. Thus, firms will not be able to use the program after July 31, 2015. Firms initially will be charged a Late Disclosure Fee and subsequently receive a refund in their FINRA Flex-Funding Account if they can establish, or if FINRA otherwise determines, that the conditions of the revised program have been satisfied.

G. Clarification of Questions 14K and 14M on the Form U4

One commenter requested that FINRA file with the SEC as part of a proposed rule change its FAQ statement<sup>43</sup> that a compromise with creditors is a compromise with one or more creditors for purposes of Question 14K on the Form U4.<sup>44</sup> The commenter also noted that Question 14M on the Form U4 is confusing because it asks “Do you have any unsatisfied judgments or liens against you,” which could imply that a “yes” response is required only if an applicant currently has an outstanding unsatisfied judgment or lien. To clarify this point, the commenter suggested model language for FINRA’s consideration. Similarly, another commenter requested that FINRA clarify Question 14M on the Form U4 to remove any confusion regarding its scope.<sup>45</sup> In addition, the

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<sup>43</sup> See Form U4 and U5 Interpretive Questions and Answers. (Available at <http://www.finra.org/web/groups/industry/@ip/@comp/@regis/documents/appsup/portdocs/p119944.pdf>.)

<sup>44</sup> SIFMA.

<sup>45</sup> FSI.

commenter stated that FINRA should clarify that it will not fine firms in instances where they did not treat a short sale as a compromise with creditors under Question 14K on the Form U4 prior to FINRA's guidance on the subject. FINRA believes that these comments are outside the scope of the proposed rule change, and should be addressed in the context of changes to the Form U4 or its interpretations. FINRA, however, will consider these comments in determining whether to make any future changes to the Form U4 or its interpretations.

FINRA believes that the foregoing fully responds to the issues raised by the commenters.

As noted in Item 2 of this filing, FINRA proposes to implement proposed FINRA Rule 3110(e) on July 1, 2015. Proposed FINRA Rule 3110.15 has a retroactive effective date of April 24, 2014, and it will automatically sunset on July 31, 2015.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>46</sup> 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 streamline and clarify members' obligations relating to background investigations, which will, in turn, improve members' compliance efforts. Further, the proposed rule change's requirement to adopt written procedures to verify the accuracy and completeness of the information contained

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<sup>46</sup> 15 U.S.C. 78o-3(b)(6).

in an applicant's Form U4, including the requirement to conduct a public records search, will enhance the accuracy of the information in the CRD system and ultimately in BrokerCheck, which is critical from both a regulatory and an investor protection standpoint. In addition, FINRA believes that the proposed rule change to establish a temporary program under proposed FINRA Rule 3110.15 that will issue a refund to members of Late Disclosure Fees would incentivize members to report underreported information relating to judgments and liens and would save FINRA the time and regulatory resources expended in contacting firms and requesting that such information be reported.

**4. 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. FINRA provided a comprehensive statement regarding the burden on competition in the Proposing Release. FINRA's response to comments and proposed revisions as set forth in this Amendment No. 1 do not change FINRA's statement in the Proposing Release.

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

Written comments on the proposed rule change were solicited by the Commission in response to the publication of SR-FINRA-2014-038.<sup>47</sup> The Commission received 10 comment letters,<sup>48</sup> which are summarized above.

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<sup>47</sup> See Proposing Release, supra note 2.

<sup>48</sup> See supra note 4.

6. **Extension of Time Period for Commission Action**

FINRA has granted an extension of the time period for Commission action until December 31, 2014.

7. **Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)**

Not applicable.

8. **Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission**

Not applicable.

9. **Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act**

Not applicable.

10. **Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act**

Not applicable.

11. **Exhibits**

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 4. Text of the proposed rule change marked to show additions to and deletions from the changes proposed by the original filing.

Exhibit 5. Text of the proposed rule change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- ; File No. SR-FINRA-2014-038)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 to a Proposed Rule Change to Adopt FINRA Rule 3110(e) (Responsibility of Member to Investigate Applicants for Registration) in the Consolidated FINRA Rulebook

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “SEA”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on , Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) and amended on -----, 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 Amendment No. 1 to SR-FINRA-2014-038, a proposed rule change to adopt NASD Rule 3010(e) (Qualifications Investigated) relating to background investigations as FINRA Rule 3110(e) (Responsibility of Member to Investigate Applicants for Registration) in the consolidated FINRA rulebook. The proposed rule change streamlines and clarifies the rule language and adds a provision to require members to adopt written procedures that are reasonably designed to verify the accuracy and completeness of the information contained in an applicant’s Form U4 (Uniform

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

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

Application for Securities Industry Registration or Transfer). In addition, the proposed rule change adds Supplementary Material .15 (Temporary Program to Address Underreported Form U4 Information) to FINRA Rule 3110 (Supervision) to establish a temporary program that will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M, subject to specified conditions. The proposed rule change would delete NASD Rule 3010(f) (Applicant's Responsibility), Incorporated NYSE Rule 345.11 (Investigation and Records) and Incorporated NYSE Rule Interpretation 345.11/01 (Application – Investigation) and /02 (Application – Records).

The text of the proposed rule change is available on FINRA's website at <http://www.finra.org>, at the principal office of FINRA 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, 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

### Rule Filing History

On September 18, 2014, FINRA filed with the SEC SR-FINRA-2014-038,<sup>3</sup> a proposed rule change to adopt NASD Rule 3010(e) relating to background investigations as FINRA Rule 3110(e) in the consolidated FINRA rulebook (“Consolidated FINRA Rulebook”).<sup>4</sup> The proposed rule change was published for comment in the Federal Register on October 3, 2014. The Commission received 10 comment letters in response to the proposed rule change.<sup>5</sup> Based on comments received, FINRA is filing this

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<sup>3</sup> See Securities Exchange Act Release No. 73238 (September 26, 2014), 79 FR 59884 (October 3, 2014) (Notice of Filing of SR-FINRA-2014-038) (“Proposing Release”). The comment period closed on October 24, 2014.

<sup>4</sup> 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).

<sup>5</sup> See Letter from Suzanne Shatto to Brent J. Fields, Secretary, SEC, dated October 6, 2014 (“Shatto”); Letter from Joseph C. Peiffer, Executive Vice President and President-Elect, Public Investors Arbitration Bar Association, to Brent J. Fields, Secretary, SEC, dated October 16, 2014 (“PIABA”); Letter from William A. Jacobson, Clinical Professor of Law, Cornell University Law School, to Brent J. Fields, Secretary, SEC, dated October 20, 2014 (“Cornell”); Letter from William Beatty, President, North American Securities Administrators Association, Inc., to Brent J. Fields, Secretary, SEC, dated October 22, 2014 (“NASAA”); Letter from Kyle Ortiz and Kathryn Hesse, Law Student Clinicians, Investor Advocacy Clinic, Michigan State University College of Law, to Brent J. Fields, Secretary, SEC, dated October 23, 2014 (“Michigan State”); Letter from John Astarita and Olivia Darius, Student Interns, John Jay Legal Services, Inc., Pace University School of Law, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“Pace”); Letter from Kevin Zambrowicz, Associate General Counsel and Managing Director, the Securities Industry and Financial Markets Association, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“SIFMA”); Letter from Michele Van Tassel, President, Association of Registration Management, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“ARM”); Letter from Robert J.

Amendment No. 1 to respond to the comments and to propose amendments, where appropriate.

Proposal

As described in the Proposing Release, as part of the process of developing the Consolidated FINRA Rulebook, FINRA is proposing to adopt NASD Rule 3010(e) relating to background investigations as FINRA Rule 3110(e).

FINRA is proposing to streamline and clarify the rule language. For instance, NASD Rule 3010(e) currently provides that “[e]ach member shall have the responsibility and duty to ascertain by investigation the good character, business repute, qualifications, and experience of any person prior to making such a certification in the application of such person for registration with this Association,” whereas proposed FINRA Rule 3110(e) provides that “[e]ach member shall ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before making a representation to that effect on the application for registration.” Further, proposed FINRA Rule 3110(e) clarifies that a firm is required to review a copy of an applicant’s most recent Form U5 (Uniform Termination Notice for Securities Industry Registration) if the applicant previously has been registered with FINRA or another self-regulatory organization. FINRA also is proposing to re-label current FINRA Rule 3110(e) (Definitions) as FINRA

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McCarthy, Director of Regulatory Policy, Wells Fargo Advisors, LLC, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“Wells Fargo”); and Letter from David T. Bellaire, Executive Vice President and General Counsel, the Financial Services Institute, to Brent J. Fields, Secretary, SEC, dated October 24, 2014 (“FSI”). (Available at <http://www.sec.gov/comments/sr-finra-2014-038/finra2014038.shtml>.)

Rule 3110(f) (Definitions) and update the cross-references in FINRA Rule 3110 to reflect this change.

In addition, FINRA is proposing to include in proposed FINRA Rule 3110(e) a requirement that firms adopt written procedures that are reasonably designed to verify the accuracy and completeness of the information contained in an applicant's Form U4 no later than 30 calendar days after the form is filed with FINRA. The proposed requirement would only apply to an initial or a transfer Form U4 for an applicant for registration, and not to Form U4 amendments. Proposed FINRA Rule 3110(e) would also require that a firm's written procedures must, at a minimum, provide for a national search of reasonably available public records conducted by the member or a third-party service provider to verify the accuracy and completeness of the information contained in an applicant's Form U4. The requirement to conduct a public records search must be satisfied no later than 30 calendar days after the initial or transfer Form U4 is filed with FINRA, with the understanding that if a member becomes aware of any discrepancies as a result of a public records search conducted after the filing of the Form U4, the member would be required to file an amended Form U4 with FINRA.

Further, FINRA is proposing to add proposed Supplementary Material .15 to FINRA Rule 3110 to establish a temporary program that will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M, subject to specified conditions.

The proposed rule change would delete NASD Rule 3010(f) because it has been rendered obsolete. The proposed rule change would also delete Incorporated NYSE Rule

345.11<sup>6</sup> and NYSE Rule Interpretation 345.11/01 and /02 as they are substantially similar to proposed FINRA Rule 3110(e), addressed by other rules or otherwise rendered obsolete by the approach reflected in proposed FINRA Rule 3110(e).

Response to Comments

A. Overview of Comments

Three commenters supported the proposal without any qualifications.<sup>7</sup> Three commenters supported the proposal, but had a few suggestions, including extending the scope of the proposed public records search to foreign jurisdictions,<sup>8</sup> clarifying the term “reasonably available public records,”<sup>9</sup> and limiting the proposed refund program to a one-time program.<sup>10</sup> Two of these commenters also requested additional clarification regarding the requirements under proposed FINRA Rule 3110(e).<sup>11</sup> One commenter supported the consolidation of NASD Rule 3010(e) and NYSE Rule 345.11 as proposed FINRA Rule 3110(e), but (1) requested further clarification regarding the investigation and verification requirements; (2) suggested changes to the verification requirement, to the implementation date of the proposal and to the sunset date of the refund program; and (3) requested clarification regarding Questions 14K and 14M on the Form U4.<sup>12</sup> Finally,

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<sup>6</sup> For convenience, the proposed rule change refers to Incorporated NYSE Rules as NYSE Rules.

<sup>7</sup> Shatto, NASAA and Michigan State.

<sup>8</sup> PIABA.

<sup>9</sup> Cornell.

<sup>10</sup> Pace.

<sup>11</sup> PIABA and Cornell.

<sup>12</sup> SIFMA. Wells Fargo supported SIFMA’s comment letter.

two commenters supported the purpose of the verification requirement, but requested additional clarification regarding its scope,<sup>13</sup> and suggested changes to the refund program.<sup>14</sup> One of these commenters also requested clarification regarding Questions 14K and 14M on the Form U4.<sup>15</sup>

B. Relationship Between Requirements of Proposed FINRA Rule 3110(e)

Several commenters requested that FINRA clarify the relationship between the requirements under proposed FINRA Rule 3110(e).<sup>16</sup> Two of these commenters also asked whether the investigation and verification requirements are duplicative, whether firms can use any of the information obtained in the investigation process to comply with the verification process and whether firms are required to conduct the verification process after the Form U4 has been filed and separate from the investigation process.<sup>17</sup>

Although the requirements of proposed FINRA Rule 3110(e) are closely related, the requirements are complementary, not duplicative, in nature. The requirements essentially come together to form an overarching process for the background investigation of applicants for registration.

First, proposed FINRA Rule 3110(e) requires that each member ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before

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<sup>13</sup> ARM.

<sup>14</sup> FSI.

<sup>15</sup> FSI.

<sup>16</sup> PIABA, Cornell, SIFMA and ARM.

<sup>17</sup> SIFMA and ARM.

making a representation to that effect on the application for registration.<sup>18</sup> This is a principle-based requirement, and it is substantially similar to the current requirement under NASD Rule 3010(e). Firms are required to complete the investigation process prior to filing the Form U4. Further, FINRA does not place any limits on the scope of such a background investigation – a firm must obtain all the necessary information to make an evaluation.<sup>19</sup> Firms should consider all available information gathered in the pre-registration process for this purpose, including, but not limited to, Form U4 and Form U5 responses, authorized searches of the Central Registration Depository (CRD®) system, fingerprint results obtained under SEA Rule 17f-2 and communications with previous employers.<sup>20</sup> Firms also may wish to consider private background checks, credit reports and reference letters for this purpose.<sup>21</sup> However, firms must ensure that such background investigations are conducted in accordance with all applicable laws, rules and regulations, including federal and state requirements, and that all necessary approvals, consents and authorizations have been obtained.<sup>22</sup>

Second, if an applicant previously has been registered with FINRA or another self-regulatory organization, proposed FINRA Rule 3110(e) requires that a firm review a copy of the applicant's most recent Form U5, including any amendments, within 60 days

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<sup>18</sup> Firms must comply with MSRB Rule G-7 (Information Concerning Associated Persons) regarding those applicants engaged solely in municipal securities activities.

<sup>19</sup> See Regulatory Notice 07-55 (November 2007).

<sup>20</sup> See supra note 19.

<sup>21</sup> See supra note 19.

<sup>22</sup> See supra note 19.

of the filing date of the applicant's Form U4.<sup>23</sup> If the firm is unable to review the Form U5, it has to demonstrate that it has made reasonable efforts to do so.<sup>24</sup> This requirement also is substantially similar to the current requirement under NASD Rule 3010(e).

Third, proposed FINRA Rule 3110(e) requires that a firm establish and implement written procedures reasonably designed to verify the accuracy and completeness of the information contained in an applicant's Form U4 by no later than 30 calendar days after an initial or a transfer Form U4 is filed with FINRA. While this is a new requirement, it is based on an underlying requirement in the Form U4 that the person signing the form on behalf of the firm certify that he or she has taken appropriate steps to verify the accuracy and completeness of the information contained in and with that form. Proposed FINRA Rule 3110(e) expressly requires that a firm's written procedures specify the firm's process for verifying the information in the Form U4 and that the firm complete that verification process by no later than 30 calendar days after the Form U4 is filed.

FINRA understands that the verification process could vary firm by firm. For instance, one firm may verify an applicant's identity and name by checking a valid state-issued driver's license whereas another firm may do so by reviewing a valid government-issued passport. Further, the verification process for some of the information in the Form U4 is embedded in the form itself. For example, the Form U4 provides that the person signing the form on behalf of the firm certify that the firm has communicated with the

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<sup>23</sup> If the applicant has been recently employed by a Futures Commission Merchant or an Introducing Broker that is notice-registered with the SEC pursuant to Section 15(b)(11) of the Act, the registering firm also is required to review a copy of the individual's most recent CFTC Form 8-T.

<sup>24</sup> FINRA expects firms to use this provision in very limited circumstances, such as where the previous firm fails to file a Form U5 or goes out of business before filing a Form U5.

applicant's previous employers for the past three years and has documentation on file with the names of the persons contacted and the date of contact. Moreover, FINRA does not expect firms to verify all of the information in the Form U4 where such verification is not feasible or practical. However, in such cases, a firm should document that the information could not be verified and the basis for it.

Under proposed FINRA Rule 3110(e), firms must complete the verification process by no later than 30 calendar days after the Form U4 is filed with FINRA. Proposed FINRA Rule 3110(e) does not require firms to conduct the verification process only during the 30-day window after the Form U4 has been filed or base the verification on information that is obtained only in the 30-day window after the form has been filed. Rather, the 30-day window is intended to accommodate firms that may find it difficult to conduct the verification process before filing an applicant's Form U4, such as where an applicant is hired immediately to fill a needed role at the firm. For most applicants, FINRA expects that firms will conduct the investigation and verification process concurrently using some of the same information and prior to filing the Form U4. Moreover, FINRA encourages firms to complete the verification process prior to filing the Form U4. In this regard, as is the case today with respect to amended filings, a firm will be subject to a Late Disclosure Fee if the disclosure event should have been reported on the initial or transfer Form U4, regardless of whether the firm completes the verification process within the 30-day window in proposed FINRA Rule 3110(e).

FINRA also recognizes that there will on occasion be circumstances beyond a firm's control that prevent completion of the verification process within the 30-day window after the Form U4 is filed with FINRA. For example, a firm may not be able to comply with the proposed 30-day window where the firm is relying on fingerprint results

for verifying criminal information, and the FBI determines the fingerprints to be “illegible” and requires resubmission of the fingerprints. In such circumstances, the firm’s procedures should provide that the verification must be completed as soon as practical, and the firm should document the basis for the delay.

Finally, proposed FINRA Rule 3110(e) requires that a firm’s verification process must, at a minimum, provide for a national search of reasonably available public records conducted by the firm or a third-party service provider to verify the accuracy and completeness of the information contained in an applicant’s Form U4. Similar to the overall verification process, the requirement to conduct a public records search must be satisfied by no later than 30 calendar days after an initial or a transfer Form U4 is filed with FINRA. The public records search is a new requirement, and it is a mandatory component of the overall verification process described above. Public records include, but are not limited to: general information, such as name and address of individuals; criminal records; bankruptcy records; civil litigations and judgments; liens; and business records. However, proposed FINRA Rule 3110(e) only requires a national search of reasonably available public records. The scope of what is considered reasonably available public records may change over time, but FINRA understands that currently such records include criminal records, bankruptcy records, judgments and liens. This is a minimum or base requirement. A firm may find it necessary to conduct a more in-depth search of public records depending on the applicant’s job function, responsibilities or position at the firm.

As stated in the Proposing Release, a firm could comply with the requirement to conduct a national search of reasonably available public records in several ways. For example, a firm may satisfy the requirement by: (1) reviewing a credit report from a

major national credit reporting agency that contains public record information (such as bankruptcies, judgments and liens) and the applicant's fingerprint results;<sup>25</sup> (2) searching a reputable national public records database and reviewing the applicant's fingerprint results; or (3) reviewing a consolidated report from a specialized provider, such as Business Information Group, Inc. (BIG),<sup>26</sup> that includes criminal and financial public records. Moreover, as explained above, the scope of the requirement is limited to reasonably available public records, which currently include criminal records, bankruptcies, judgments and liens. FINRA notes that the proposed public records search requirement does not require firms to obtain a credit report, which contains both public and non-public records. FINRA included a credit report in the list above as an example of a type of document that includes reasonably available public records. FINRA further reiterates that, as is the case with the investigative process, firms must ensure that such public records searches are conducted in accordance with all applicable laws, rules and

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<sup>25</sup> Firms currently have an obligation to comply with SEA Rule 17f-2. Pursuant to SEA Rule 17f-2, specific persons employed in the securities industry are required to be fingerprinted for purposes of a criminal background check. Firms are responsible for obtaining a prospective employee's fingerprints and required identifying information. Firms then submit the prospective employee's fingerprints together with the required identifying information to FINRA. FINRA, in turn, submits these fingerprints to the FBI. FINRA also makes the fingerprint results available to the employing member and regulators, consistent with applicable federal laws and FBI and FINRA requirements. See Notice to Members 05-39 (May 2005). Firms may rely on these fingerprint results to comply with the requirement to conduct a public records search of criminal records.

<sup>26</sup> FINRA has contracted with BIG to provide competitive pricing to members that are conducting background investigations of applicants, currently at a cost of \$10 to \$13 per applicant (depending on volume). In general, FINRA does not endorse any particular third-party service and a firm's use of BIG's services, or the services of any other specific provider, would not be deemed to be a safe harbor by FINRA.

regulations, including federal and state requirements, and that all necessary approvals, consents and authorizations have been obtained.

C. Member's Obligation to Adopt Written Procedures for Verification of Information in the Form U4 (Proposed FINRA Rule 3110(c))

Two commenters asked whether firms are required to verify all of the information in the Form U4 and stated that it may not be feasible or practical to do so in some cases.<sup>27</sup> For example, one of these commenters stated that existing resources do not allow firms to verify the response to Question 13 (Other Business) on the Form U4, and the commenter was not aware of a central data source that could serve to verify for an applicant's outside business.<sup>28</sup> As discussed above, FINRA does not expect firms to verify all of the information in the Form U4 where such verification is not feasible or practical. However, in such cases, a firm should document that the information could not be verified and the basis for it.

One commenter recommended that the proposed verification requirement, including the minimum public records search requirement, be removed altogether.<sup>29</sup> Alternatively, the commenter requested that firms should be given 90 days to complete a public records search and any necessary follow ups and asked whether firms are required to complete the entire verification process within the proposed 30-day window. One commenter requested that firms should be given a 60- or 90-day period to complete the verification process.<sup>30</sup> Another commenter suggested that FINRA amend the proposed

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<sup>27</sup> SIFMA and ARM.

<sup>28</sup> ARM.

<sup>29</sup> SIFMA.

<sup>30</sup> ARM.

rule text to require that a firm's written procedures provide that if the firm is unable to complete the verification process within the 30-day window, it must demonstrate to FINRA that it has made reasonable efforts to do so and explain the cause for the delayed verification.<sup>31</sup>

FINRA is retaining the proposed Form U4 verification requirement and the minimum requirement to conduct a public records search. FINRA continues to believe that the proposed requirements will enhance the accuracy of the information in the CRD system and ultimately in BrokerCheck, which is critical from both a regulatory and an investor protection standpoint. Further, as described above, firms must complete the verification process by no later than 30 calendar days after the Form U4 is filed with FINRA. For most applicants, FINRA expects that firms will conduct the proposed verification process, including the public records search, prior to filing the Form U4. Moreover, FINRA encourages firms to complete the verification process prior to filing the Form U4.

FINRA does not believe that it is necessary to extend the period by which firms must complete the verification process for the following reason. Pursuant to the FINRA By-Laws, a firm is obligated to file an amended Form U4 no later than 30 calendar days after learning of the facts or circumstances giving rise to the amendment.<sup>32</sup> Therefore, if a firm completes its verification process during the 30-day window in proposed FINRA Rule 3110(e) and learns of facts or circumstances that require the filing of an amended Form U4, the firm will continue to have 30 calendar days from the date it learns of such

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<sup>31</sup> PIABA.

<sup>32</sup> See FINRA By-Laws, Article V, Section 2(c).

facts or circumstances to file an amended Form U4, provided that the firm will be subject to any applicable Late Disclosure Fees.

FINRA recognizes that there will on occasion be circumstances beyond a firm's control that prevent completion of the verification process within the 30-day window. In such cases, the firm's procedures should provide that the verification must be completed as soon as practical, and the firm should document the basis for the delay. FINRA does not believe that it is necessary to amend the proposed rule text to clarify this point.

One commenter requested that FINRA confirm that the proposed verification requirement, including the public records search, applies to an initial Form U4 filed with FINRA through the CRD system requesting registration with FINRA and that the proposed requirement does not apply to a Form U4 filed by an affiliate of a member or a registration transferred through the mass transfer process.<sup>33</sup> The commenter also suggested that FINRA replace the term "transfer Form U4" as used in the Proposing Release with the term "relicense Form U4" and amend the proposed rule text to include a reference to "an applicant's initial or relicense Form U4."

The proposed verification requirement, including the public records search, applies to an initial Form U4 or a transfer Form U4. The term "initial Form U4" refers to the Form U4 filing required when an individual is registering with a FINRA member for the first time, including in the context of dual registration, or is registering with a FINRA member after more than two years have passed since the individual was last registered with a FINRA member. The term "transfer Form U4" refers to the Form U4 filing required when a registered person transfers from one FINRA member to another FINRA

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<sup>33</sup> SIFMA.

member. FINRA does not believe that it is necessary to replace the term “transfer Form U4” with the term “relicense Form U4” based on the explanation provided above. With respect to a Form U4 filed by a member that is an affiliate of another member, the verification requirement would apply to the filing to the extent that it is considered an initial or a transfer Form U4 (e.g., a dual registration). The proposed verification requirement would not apply to the mass transfer process because that process does not require the filing of a Form U4, which is the basis for the proposed verification requirement under proposed FINRA Rule 3110(e). FINRA is proposing to amend proposed FINRA Rule 3110(e) to clarify that the verification requirement, including the public records search, applies to an applicant’s initial or transfer Form U4.

D. Member’s Obligation to Conduct a Search of Reasonably Available Public Records (Proposed FINRA Rule 3110(e))

One commenter suggested that the public records search should extend to foreign jurisdictions in some circumstances, such as where an applicant has been registered with a foreign securities regulator or has resided in a foreign jurisdiction.<sup>34</sup> FINRA believes that it is often difficult to assess the comparability of a foreign country’s laws, rules and regulations to those in the United States, particularly as it relates to the purposes of this proposed rule, and believes, therefore, that the requirement should be limited to a national search of reasonably available public records. However, firms may find it necessary to conduct a search of public records in a foreign jurisdiction as part of their verification process and, where appropriate, should consider such a search consistent with applicable foreign laws, rules and regulations.

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<sup>34</sup> PIABA.

One commenter recommended that FINRA clarify the term “reasonably available public records” so that firms have an objective standard for compliance purposes.<sup>35</sup> One commenter stated that FINRA should revise the proposed rule text to specifically identify the information in the Form U4 that firms are expected to verify through a public records search or define the term “public records” so the scope of the requirement is less uncertain.<sup>36</sup> The commenter noted that business records are listed as an example of public records, but many business records (e.g., business formation documents) are not maintained in a comprehensive national database and may not be offered by a third-party service provider. While public records include, among other records, business records, proposed FINRA Rule 3110(e) only requires a national search of reasonably available public records. As stated above, the scope of what is considered reasonably available public records may change over time. Therefore, rather than define the term “reasonably available public records,” FINRA believes that it is more useful for compliance purposes to specify the public records that are currently considered reasonably available, which include criminal records, bankruptcy records, judgments and liens.

One commenter asked that FINRA confirm that, to the extent that the proposed rule requires firms to obtain an investigative consumer report for an applicant, firms can rely on the applicant’s consent on a Form U4 (citing to Item 15A on the Form U4) for purposes of complying with applicable laws, rules and regulations requiring an applicant’s consent to obtain such reports, otherwise firms will need to implement additional procedures to ensure compliance with such laws, rules and regulations in each

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<sup>35</sup> Cornell.

<sup>36</sup> SIFMA.

jurisdiction.<sup>37</sup> The proposed rule does not require firms to obtain investigative consumer reports to comply with the requirements of the rule. Moreover, FINRA reiterates that a firm must continue to comply with all applicable laws, rules and regulations in the course of the registration process, as is the case today. Therefore, if a firm is relying on a particular report that requires an applicant's consent under the laws, rules and regulations of a particular jurisdiction, FINRA expects that the firm will obtain the requisite consent in accordance with such laws, rules and regulations. With respect to the commenter's request regarding the validity of an applicant's Form U4 consent, it is the responsibility of the registering firm to determine whether such consent is in compliance with the laws, rules and regulations of the particular jurisdiction in which the firm and the applicant are operating.

E. Implementation Date of Proposed FINRA Rule 3110(e)

One commenter requested that FINRA extend the implementation date of proposed FINRA Rule 3110(e) from December 1, 2014 to December 1, 2015 so that firms have sufficient time to establish or revise their written procedures and address the operational issues resulting from the proposed rule.<sup>38</sup>

FINRA expects firms to have an existing process in place to verify the information contained in an applicant's Form U4 because currently the person signing the form on behalf of the firm must certify that he or she has taken appropriate steps to verify the accuracy and completeness of the information in the form. FINRA also understands

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<sup>37</sup> SIFMA.

<sup>38</sup> SIFMA.

that most firms already conduct some form of public records search. Therefore, the proposed new requirements should not create an unreasonable burden for firms.

However, FINRA recognizes that the proposed rule imposes an affirmative obligation on firms to establish and implement written procedures to comply with the Form U4 verification process to the extent they currently do not have such procedures and that such procedures must include a search of reasonably available public records. Thus, to accommodate any potential operational issues resulting from the proposed new requirements, FINRA is proposing to extend the implementation date of proposed FINRA Rule 3110(e) from December 1, 2014 to July 1, 2015.

F. Temporary Program to Address Underreported Form U4 Information  
(Proposed FINRA Rule 3110.15)

One commenter recommended that the refund program should be a one-time program and stated that FINRA should not use such programs in the future for late disclosure reporting because it may provide firms with negative reinforcement for untimely Form U4 reporting.<sup>39</sup> The refund program under proposed FINRA Rule 3110.15 is intended to incentivize members to report underreported information and save FINRA the time and regulatory resources expended in contacting firms and requesting that such information be reported. The program is intended to run concurrent with FINRA's one-time search of specific financial public records, and thus is of limited duration. FINRA may find it necessary to provide such programs in the future depending on the circumstances, but it will do so judiciously and only where appropriate.

Another commenter, while supportive of the purpose of the refund program, requested that FINRA consider adopting a more permanent refund program or extending

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<sup>39</sup> Pace.

the sunset date from March 31, 2015 to December 1, 2015.<sup>40</sup> The refund program is intended to run concurrent with FINRA's one-time search of specific financial public records on all registered persons, which FINRA expects to complete on or before August 2015. Because the refund program is intended to run concurrent with FINRA's search process, FINRA is extending the sunset date of the program from March 31, 2015 to July 31, 2015, which should provide firms additional time to identify and report information to FINRA.

One commenter suggested that Question 14M on the Form U4 is ambiguous and open to interpretation and requested that FINRA revise the eligibility conditions under the refund program to address this perceived ambiguity.<sup>41</sup> According to the commenter, Question 14M on the Form U4 is confusing because one could argue that if an unsatisfied judgment or lien is satisfied within the 30-day window of having to file an amended Form U4, the firm would not have to amend the Form U4 to mark "yes" because the lien is satisfied prior to the filing deadline. The commenter also stated that if a firm learns of an unreported satisfied lien, the language of Question 14M suggests that the firm does not have to report such lien because it is not currently unsatisfied. The commenter stated that FINRA should modify the program to refund members if the judgment or lien (1) occurred while the individual was registered with a prior firm; (2) is more than five years old; or (3) is under \$5,000. The commenter also asked whether the refund will be automated or whether firms have the burden to prove that they satisfy the conditions of the program to receive a refund.

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<sup>40</sup> SIFMA.

<sup>41</sup> FSI.

As set forth in the Proposing Release, the temporary program would issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M (unsatisfied judgments or liens) if the following conditions are met: (1) the Form U4 amendment is filed between April 24, 2014 and March 31, 2015; (2) the judgment or lien is under \$5,000 and more than five years old (from the date the judgment or lien is filed with a court as reported on Form U4 Judgment/Lien DRP, Question 4); and (3) the registered person was not employed by, or otherwise associated with, the firm filing the amended Form U4 on the date the judgment or lien was filed with the court.

FINRA is proposing to revise the refund program to address concerns regarding the assessment of the Late Disclosure Fee in circumstances where the unsatisfied judgment or lien has been satisfied, and at the time it was unsatisfied was of a relatively low amount (under \$5,000) and was reportable prior to the introduction of the procedures regarding the application of the Late Disclosure Fee to the reporting of judgments and liens on the Form U4 that became effective on August 13, 2012.<sup>42</sup> The proposed revisions also address circumstances where the failure to report related to a mistaken belief that satisfying the judgment or lien shortly after learning it was unsatisfied (within 30 calendar days of when it became unsatisfied) obviated the need to report the matter.<sup>43</sup>

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<sup>42</sup> See Information Notice August 17, 2012 (Late Disclosure Fee Related to Reporting of Judgment/Lien Events).

<sup>43</sup> FINRA believes that there is a misconception regarding the obligation to report unsatisfied judgments and liens under Question 14M on the Form U4. The obligation to amend a Form U4 arises on the date a registered person receives notice or learns that he or she is subject to an unsatisfied judgment or lien, and an amended Form U4 should be filed no later than 30 calendar days from that date, regardless of whether the registered person satisfies the judgment or lien in the interim period prior to the 30-day deadline for filing a Form U4 amendment.

In addition, as noted above, FINRA is proposing to extend the sunset date of the refund program to July 31, 2015 (rather than March 31, 2015 as originally proposed).

As revised, the temporary program will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M (unsatisfied judgments or liens) if the Form U4 amendment is filed between April 24, 2014 and July 31, 2015 and one of the following conditions is met: (1) the judgment or lien has been satisfied, and at the time it was unsatisfied, it was under \$5,000 and the date the judgment or lien was filed with a court (as reported on Form U4 Judgment/Lien DRP, Question 4.A.) was on or before August 13, 2012; or (2) the unsatisfied judgment or lien was satisfied within 30 days after the individual learned of the judgment or lien (as reported on Form U4 Judgment/Lien DRP, Question 4.B.). The revised program has a retroactive effective date of April 24, 2014, and it will automatically sunset on July 31, 2015. Thus, firms will not be able to use the program after July 31, 2015. Firms initially will be charged a Late Disclosure Fee and subsequently receive a refund in their FINRA Flex-Funding Account if they can establish, or if FINRA otherwise determines, that the conditions of the revised program have been satisfied.

G. Clarification of Questions 14K and 14M on the Form U4

One commenter requested that FINRA file with the SEC as part of a proposed rule change its FAQ statement<sup>44</sup> that a compromise with creditors is a compromise with one or more creditors for purposes of Question 14K on the Form U4.<sup>45</sup> The commenter

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<sup>44</sup> See Form U4 and U5 Interpretive Questions and Answers. (Available at <http://www.finra.org/web/groups/industry/@ip/@comp/@regis/documents/appspportdocs/p119944.pdf>.)

<sup>45</sup> SIFMA.

also noted that Question 14M on the Form U4 is confusing because it asks “Do you have any unsatisfied judgments or liens against you,” which could imply that a “yes” response is required only if an applicant currently has an outstanding unsatisfied judgment or lien. To clarify this point, the commenter suggested model language for FINRA’s consideration. Similarly, another commenter requested that FINRA clarify Question 14M on the Form U4 to remove any confusion regarding its scope.<sup>46</sup> In addition, the commenter stated that FINRA should clarify that it will not fine firms in instances where they did not treat a short sale as a compromise with creditors under Question 14K on the Form U4 prior to FINRA’s guidance on the subject. FINRA believes that these comments are outside the scope of the proposed rule change, and should be addressed in the context of changes to the Form U4 or its interpretations. FINRA, however, will consider these comments in determining whether to make any future changes to the Form U4 or its interpretations.

FINRA believes that the foregoing fully responds to the issues raised by the commenters.

FINRA proposes to implement proposed FINRA Rule 3110(e) on July 1, 2015. Proposed FINRA Rule 3110.15 has a retroactive effective date of April 24, 2014, and it will automatically sunset on July 31, 2015.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>47</sup> which requires, among other things, that FINRA rules

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<sup>46</sup> FSI.

<sup>47</sup> 15 U.S.C. 78o-3(b)(6).

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 streamline and clarify members' obligations relating to background investigations, which will, in turn, improve members' compliance efforts. Further, the proposed rule change's requirement to adopt written procedures to verify the accuracy and completeness of the information contained in an applicant's Form U4, including the requirement to conduct a public records search, will enhance the accuracy of the information in the CRD system and ultimately in BrokerCheck, which is critical from both a regulatory and an investor protection standpoint. In addition, FINRA believes that the proposed rule change to establish a temporary program under proposed FINRA Rule 3110.15 that will issue a refund to members of Late Disclosure Fees would incentivize members to report underreported information relating to judgments and liens and would save FINRA the time and regulatory resources expended in contacting firms and requesting that such information be reported.

**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. FINRA provided a comprehensive statement regarding the burden on competition in the Proposing Release. FINRA's response to comments and proposed revisions as set forth in this Amendment No. 1 do not change FINRA's statement in the Proposing Release.

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

Written comments on the proposed rule change were solicited by the Commission in response to the publication of SR-FINRA-2014-038.<sup>48</sup> The Commission received 10 comment letters,<sup>49</sup> which are summarized above.

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 (i) as the Commission may designate up to 90 days of such date 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 such 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

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<sup>48</sup> See Proposing Release, supra note 3.

<sup>49</sup> See supra note 5.

- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2014-038 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2014-038. 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 website (<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 website 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 a.m. and 3 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 available publicly. All submissions should refer to File Number SR-FINRA-2014-038 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.<sup>50</sup>

Brent J. Fields

Secretary

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<sup>50</sup> 17 CFR 200.30-3(a)(12).

## **EXHIBIT 4**

Exhibit 4 shows the changes proposed in this Amendment No. 1 only as to FINRA Rule 3110, with the proposed changes in the original filing shown as if adopted. New language proposed in this Amendment No. 1 is underlined; deletions proposed in this Amendment No. 1 are in brackets.

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### **3110. Supervision**

#### **(a) Supervisory System**

Each member shall establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules. Final responsibility for proper supervision shall rest with the member. A member's supervisory system shall provide, at a minimum, for the following:

(1) through (2) No Change.

(3) The registration and designation as a branch office or an office of supervisory jurisdiction (OSJ) of each location, including the main office, that meets the definitions contained in paragraph (f) of this Rule.

(4) through (7) No Change.

(b) through (d) No Change.

#### **(e) Responsibility of Member to Investigate Applicants for Registration**

Each member shall ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before making a representation to that effect on the application for registration.

If the applicant previously has been registered with FINRA or another self-regulatory organization, the member shall review a copy of the applicant's most recent Form U5, including any amendments thereto, within 60 days of the filing date of an application for registration, or demonstrate to FINRA that it has made reasonable efforts to do so. In conducting its review of the Form U5, the member shall take such action as may be deemed appropriate.

The member shall also review an applicant's employment experience to determine if the applicant has been recently employed by a Futures Commission Merchant or an Introducing Broker that is notice-registered with the SEC pursuant to Section 15(b)(11) of the Exchange Act. In such a case, the member shall also review a copy of the applicant's most recent CFTC Form 8-T, including any amendments thereto, within 60 days of the filing date of an application for registration, or demonstrate to FINRA that it has made reasonable efforts to do so. In conducting its review of a Form 8-T, the member shall take such action as may be deemed appropriate.

In addition, each member shall establish and implement written procedures reasonably designed to verify the accuracy and completeness of the information contained in an applicant's initial or transfer Form U4 no later than 30 calendar days after the form is filed with FINRA. Such procedures shall, at a minimum, provide for a search of reasonably available public records to be conducted by the member, or a third-party service provider, to verify the accuracy and completeness of the information contained in the applicant's initial or transfer Form U4.

**(f) Definitions**

- (1) No Change.

(2) (A) through (B) No Change.

(C) The term “business day” as used in paragraph (f)(2)(A) of this Rule shall not include any partial business day provided that the associated person spends at least four hours on such business day at his or her designated branch office during the hours that such office is normally open for business.

••• **Supplementary Material:** -----

**.01 Registration of Main Office.** A member’s main office location is required to be registered and designated as a branch office or OSJ if it meets the definitions of a “branch office” or “office of supervisory jurisdiction” as set forth in Rule 3110(f). In general, the nature of activities conducted at a main office will satisfy the requirements of such terms.

**.02 Designation of Additional OSJs.** In addition to the locations that meet the definition of OSJ in Rule 3110(f), each member shall also register and designate other offices as OSJs as is necessary to supervise its associated persons in accordance with the standards set forth in Rule 3110. In making a determination as to whether to designate a location as an OSJ, the member should consider the following factors:

(a) through (e) No Change.

**.03 through .14** No Change.

**.15 Temporary Program to Address Underreported Form U4 Information.** FINRA is establishing a temporary program that will issue a refund to members of Late Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M (unsatisfied judgments or liens) if [the following conditions are met: (1)] the Form U4 amendment is filed between April 24, 2014 and July[March] 31, 2015[;] and one of the

following conditions is met: (1)[(2)] the judgment or lien has been satisfied, and at the time it was unsatisfied, it was [is] under \$5,000 and the date the judgment or lien was filed with a court [and more than five years old] ([from the date the judgment or lien is filed with a court] as reported on Form U4 Judgment/Lien DRP, Question 4.A.) was on or before August 13, 2012; or (2)[and (3) the registered person was not employed by, or otherwise associated with, the firm filing the amended Form U4 on the date] the unsatisfied judgment or lien was [filed with the court] satisfied within 30 days after the individual learned of the judgment or lien (as reported on Form U4 Judgment/Lien DRP, Question 4.B.). This program has a retroactive effective date of April 24, 2014, and it will automatically sunset on July[March] 31, 2015. Members will not be able to use the program after July[March] 31, 2015.

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\* No Change.

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**EXHIBIT 5**

Exhibit 5 shows the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

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**Text of Proposed New FINRA Rule 3110(e)**

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**3000. SUPERVISION AND RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS**

**3100. SUPERVISORY RESPONSIBILITIES**

**3110. Supervision**

**(a) Supervisory System**

Each member shall establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules. Final responsibility for proper supervision shall rest with the member. A member's supervisory system shall provide, at a minimum, for the following:

(1) through (2) No Change.

(3) The registration and designation as a branch office or an office of supervisory jurisdiction (OSJ) of each location, including the main office, that meets the definitions contained in paragraph [(e)](f) of this Rule.

(4) through (7) No Change.

(b) through (d) No Change.

**(e) Responsibility of Member to Investigate Applicants for Registration**

Each member shall ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before making a representation to that effect on the application for registration.

If the applicant previously has been registered with FINRA or another self-regulatory organization, the member shall review a copy of the applicant's most recent Form U5, including any amendments thereto, within 60 days of the filing date of an application for registration, or demonstrate to FINRA that it has made reasonable efforts to do so. In conducting its review of the Form U5, the member shall take such action as may be deemed appropriate.

The member shall also review an applicant's employment experience to determine if the applicant has been recently employed by a Futures Commission Merchant or an Introducing Broker that is notice-registered with the SEC pursuant to Section 15(b)(11) of the Exchange Act. In such a case, the member shall also review a copy of the applicant's most recent CFTC Form 8-T, including any amendments thereto, within 60 days of the filing date of an application for registration, or demonstrate to FINRA that it has made reasonable efforts to do so. In conducting its review of a Form 8-T, the member shall take such action as may be deemed appropriate.

In addition, each member shall establish and implement written procedures reasonably designed to verify the accuracy and completeness of the information contained in an applicant's initial or transfer Form U4 no later than 30 calendar days after the form is filed with FINRA. Such procedures shall, at a minimum, provide for a search of reasonably available public records to be conducted by the member, or a third-party

service provider, to verify the accuracy and completeness of the information contained in the applicant's initial or transfer Form U4.

**[(e)](f) Definitions**

(1) No Change.

(2) (A) through (B) No Change.

(C) The term "business day" as used in paragraph [(e)](f)(2)(A) of this Rule shall not include any partial business day provided that the associated person spends at least four hours on such business day at his or her designated branch office during the hours that such office is normally open for business.

**••• Supplementary Material: -----**

**.01 Registration of Main Office.** A member's main office location is required to be registered and designated as a branch office or OSJ if it meets the definitions of a "branch office" or "office of supervisory jurisdiction" as set forth in Rule 3110[(e)](f). In general, the nature of activities conducted at a main office will satisfy the requirements of such terms.

**.02 Designation of Additional OSJs.** In addition to the locations that meet the definition of OSJ in Rule 3110[(e)](f), each member shall also register and designate other offices as OSJs as is necessary to supervise its associated persons in accordance with the standards set forth in Rule 3110. In making a determination as to whether to designate a location as an OSJ, the member should consider the following factors:

(a) through (e) No Change.

**.03 through .14** No Change.

**.15 Temporary Program to Address Underreported Form U4 Information. FINRA**  
**is establishing a temporary program that will issue a refund to members of Late**  
**Disclosure Fees assessed for the late filing of responses to Form U4 Question 14M**  
**(unsatisfied judgments or liens) if the Form U4 amendment is filed between April 24,**  
**2014 and July 31, 2015 and one of the following conditions is met: (1) the judgment or**  
**lien has been satisfied, and at the time it was unsatisfied, it was under \$5,000 and the date**  
**the judgment or lien was filed with a court (as reported on Form U4 Judgment/Lien DRP,**  
**Question 4.A.) was on or before August 13, 2012; or (2) the unsatisfied judgment or lien**  
**was satisfied within 30 days after the individual learned of the judgment or lien (as**  
**reported on Form U4 Judgment/Lien DRP, Question 4.B.). This program has a**  
**retroactive effective date of April 24, 2014, and it will automatically sunset on July 31,**  
**2015. Members will not be able to use the program after July 31, 2015.**

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\* No Change.

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**Text of NASD Rule  
to be Deleted in its Entirety from the Transitional Rulebook**

\* \* \* \* \*

**[3010. Supervision]**

**Entire text deleted.**

\* \* \* \* \*

**Text of Incorporated NYSE Rule and Incorporated NYSE Rule Interpretation  
to Remain in the Transitional Rulebook**

\* \* \* \* \*

**Incorporated NYSE Rule**

\* \* \* \* \*

**Rule 345. Employees—Registration, Approval, Records**

(a) No Change.

**• • • Supplementary Material -----**

**Registration of Employees**

.10 No Change.

.11 [Investigation and Records] Reserved.

[(a) Members and member organizations shall thoroughly investigate the previous record of persons whom they contemplate employing including, (1) persons required to be registered with the Exchange, (2) persons who regularly handle or process securities or monies or maintain the books and records relating to securities or monies and (3) persons having direct supervisory responsibility over persons engaged in the activities referred to in (1) and (2) above who are not otherwise required to be registered.]

[Investigatory requirements for persons required to be registered with the Exchange (referred to in (a)(1) above) shall be satisfied when the member or member organization fulfills its obligation to verify the information contained in the Uniform Application for Securities Industry Registration or Transfer (Form U-4) and reviews the most recent Form U-5, as described below, if applicable.]

[In addition, a member or member organization shall obtain from an applicant, if applicable, a copy of his or her Uniform Termination Notice of Securities Industry Registration (Form U-5) and any amendments filed thereto, by

the most recent employer. A member or member organization shall request said Form U-5 from any person who was previously registered with the Exchange or other self-regulatory organization that requires its members to provide a copy of Form U-5 to its terminated registered persons. (See also Rule 345.17.)]

[The member or member organization shall obtain said Form U-5 no later than sixty (60) days following the filing of the application for registration or demonstrate to the Exchange that it has made reasonable efforts to comply with the requirement. A member or member organization receiving a Form U-5 pursuant to this provision shall review the Form U-5 and any amendment thereto as part of its investigatory process and shall take such action as may be deemed appropriate.]

[Investigatory requirements pertaining to persons specified in (a)(2) and (3) above shall be satisfied if a member or member organization verifies the information obtained pursuant to paragraph (c) below. Notwithstanding the above, further inquiry shall be made where appropriate in light of background information developed, the position for which the person is being considered or other circumstances. Investigation and verification shall be done by a member or person designated under the provisions of Rule 342(b)(1).]

**[(b)** Any applicant for registration who receives a request for a copy of his or her Form U-5 from a member or member organization pursuant to (a) above shall provide such copy to the member or member organization within two (2) business days of the request if the Form U-5 has been provided to such person by his or her former employer. If an employer has failed to provide the Form U-5 to

the applicant for registration, such person shall promptly request the Form U-5, and shall provide it to the requesting member or member organization within two (2) business days of receipt thereof. The applicant shall promptly provide any subsequent amendments to a Form U-5 he or she receives to the requesting member or member organization.]

[(c) Members and member organizations are reminded to obtain and keep on file all information required under Rule 17a-3(a)(12) of the Securities Exchange Act of 1934 for persons included within the definition of “associated person” pursuant to Rule 17a-3(a)(12)(ii). In addition, the Exchange requires that a record be kept of whether a bonding company has ever denied or revoked, or paid out on any bond because of such person.]

[If an employee is registered with the Exchange, a duplicated copy of Form U-4 signed by an authorized person shall satisfy all the recordkeeping requirements of this paragraph.]

.12 through .16 No Change.

#### **General Information Regarding Employees**

.17 through .18 No Change.

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#### **Incorporated NYSE Rule Interpretation**

\* \* \* \* \*

#### **Rule 345 Employees — Registration, Approval, Records**

(a) through (b) No Change.

.11 [INVESTIGATION AND RECORDS] Reserved.

[/01 Application — Investigation]

[Member organizations must investigate the previous record of persons whom they contemplate employing including, (1) persons required to be registered with the Exchange, (2) persons who regularly have access to the keeping, handling or processing of securities, monies or the original books and records relating to securities or monies and (3) persons having direct supervisory responsibility over persons engaged in the activities referred to in (1) and (2) above.]

[Investigatory requirements for persons required to be registered with the Exchange (referred to in (1) above) will be satisfied when the member organization fulfills its obligation to verify the information contained in the Uniform Application for Securities Industry Registration Or Transfer (Form U4). Similarly, investigatory requirements pertaining to persons specified in (2) and (3) above shall be satisfied if a member organization verifies the information obtained pursuant to SEA Rule 17a-3(a)(12). (See /02 below.) Notwithstanding the above, further inquiry must be made where appropriate in light of background information developed, the position for which the person is being considered or other circumstances.]

[For those persons a member organization contemplates employing who are not specifically required to be investigated, a member organization should tailor its investigation in a manner it deems appropriate in light of the position to be held by such person. (See also Rule 346(f) regarding persons subject to “statutory disqualifications”).]

[/02 Application — Records]

[Member organizations are reminded to obtain and keep on file all information required under SEA Rule 17a-3(a)(12) for persons included within the definition of “associated person” (see Rule 17a-3(a)(12)(ii)). Further, the Exchange requires that a record be kept of whether a bonding company has ever denied or revoked, or paid out on any bond because of such person.]

[For persons required to be registered with the Exchange, a duplicate copy of Form U4 signed by an authorized person will satisfy all the recordkeeping requirements of NYSE Rule 345.11.]

.12 No Change.

.15 No Change.

.18 No Change.

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