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October 7, 2020

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

**Re: File No. SR-FINRA-2020-011 (Proposed Rule Change to Address Brokers with a Significant History of Misconduct)**

Dear Ms. Countryman:

This letter is being submitted by the Financial Industry Regulatory Authority ("FINRA") in response to comments received by the Securities and Exchange Commission ("SEC" or "Commission") regarding the above-referenced rule filing to address the risks posed by brokers with a significant history of misconduct and the firms that employ them (the "Proposal").

The SEC published the proposed rule change for public comment in the Federal Register on April 14, 2020.[1] The Commission received five comments in response to the Proposal.[2] On July 2, 2020, FINRA responded to the comments and filed Partial

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1 See Securities Exchange Act Release No. 88600 (April 8, 2020), 85 FR 20745, 20745 (April 14, 2020) (Notice of Filing of File No. SR-FINRA-2011-011) ("Initial Filing").

2 See Letter from Andrew R. Harvin, Partner, Doyle, Restrepo, Harvin & Robbins, LLP, to Jill M. Petersen, Assistant Secretary, SEC, dated April 28, 2020 ("Harvin"); Letter from Lisa Miller, dated April 30, 2020 ("Miller"); Letter from William A. Jacobson & Ayomikun Loye, Cornell Law School and Cornell Securities Law Clinic, to Vanessa Countryman, Secretary, SEC, dated May 5, 2020 ("Cornell Clinic"); Letter from Samuel B. Edwards, President, Public Investors Advocate Bar Association, to Brent J. Fields, Secretary, SEC, dated May 5, 2020 ("PIABA"); and Letter from Lev Bagramian, Senior Securities Policy Advisor, Better Markets, Inc. to Vanessa A. Countryman, Secretary, SEC, dated June 19, 2020 ("Better Markets").

Amendment No. 1 to the Proposal to propose amendments based on the comments received by the SEC.[3]

On July 17, 2020, the SEC published a notice and order in the Federal Register to solicit comments on the Proposal as modified by Partial Amendment No. 1 and to institute proceedings pursuant to Section 19(b)(2)(B) of the Securities Exchange Act of 1934 ("SEA") in the above-referenced rule filing to determine whether to approve or disapprove the proposed rule change as modified by Partial Amendment No. 1.[4] The SEC received one comment letter in response.[5] FINRA believes it has previously considered the comments raised and does not believe additional changes to the Proposal are warranted at this time. FINRA submits this rebuttal to the commenter's material concerns.

Statistics and Fair Process Concerns

Alpine contends that FINRA has not justified the proposed changes to the Rule 9200 Series, 9300 Series, 9520 Series or the Rule 1000 Series.[6] In its Initial Filing, FINRA explained the purpose of the proposed rule change and why, consistent with the SEA, it is designed to protect investors and the public interest by strengthening the tools available to FINRA to address the risks posed by brokers with a significant history of misconduct and the firms that employ them. As stated in the Initial Filing, despite existing requirements and FINRA's ongoing efforts to strengthen protections for investors and the markets through its oversight of member firms and the brokers they employ, persistent compliance issues continue to arise in some member firms.

As FINRA explained, recent studies have shown that some firms persistently employ brokers who engage in misconduct, and that past disciplinary and other regulatory events associated with a member firm or individual can be predictive of similar future events, such as repeated disciplinary actions, arbitrations and complaints.[7] FINRA also

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3 See FINRA Response to Comments, dated July 2, 2020 ("Response Letter") and Partial Amendment No. 1 to SR-FINRA-2020-011 filed on July 2, 2020 ("Partial Amendment No. 1"), available at https://www.finra.org/rules-guidance/rule-filings/sr-finra-2020-011.

4 See Securities Exchange Act Release No. 89305 (July 13, 2020), 85 FR 43627 (July 17, 2020) (Order Instituting Proceedings to Determine Whether to Approve or Disapprove File No. SR-FINRA-2020-011).

5 See Letter from Aaron Lebenta, Esq., Parsons Behle & Latimer, on behalf of Alpine Securities Corporation, to Vanessa Countryman, Office of the Secretary, SEC, dated August 3, 2020 ("Alpine").

6 Alpine, supra note 5, at 3-5.

7 See Initial Filing, 85 FR 20745-46.

explained how these risks cannot always be adequately addressed by FINRA's existing rules and programs.[8] The proposed rule change would impact a discrete set of individuals with a significant history of misconduct, and FINRA's Economic Impact Assessment ("EIA") demonstrated the specific potential risks these individuals pose.[9]

FINRA also explained how the proposed new protections—conditions and restrictions, heightened supervision requirements, and mandatory materiality consultations—are designed to protect investors and the public interest against these specific risks. In short, FINRA believes the proposed new protections will create strong measures of deterrence during an appeal proceeding, require that employing firms act with increased scrutiny during appeal and eligibility proceedings, give FINRA an opportunity to assess whether certain proposed associations with persons who have a significant history of misconduct are material, and create incentives for brokers and firms to change activities and behaviors.[10]

Alpine points to how the number of FINRA regulatory actions has decreased during the last five years, and it challenges FINRA's analysis of appeals of disciplinary matters,[11] but FINRA has provided detailed information in the EIA to support the proposed approach. For example, the EIA identified specific categories of individuals with a significant history of misconduct during the 2013-2018 review period and demonstrated that these individuals

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8 See Initial Filing, 85 FR 20745-46.

9 See Initial Filing, 85 FR 20745, 20756 (estimating that 21 of the 75 brokers (or 28%) who appealed to the National Adjudicatory Council ("NAC") during the 2013-16 period were associated with a total of 28 disclosure events that occurred during the interstitial period after the filing of their appeal to the NAC); id. at 20757 (estimating that 26 of the 51 statutorily disqualified individuals (or 51%) associated with applications to continue their employment ("SD Application") during the 2013-2016 period had a total of 41 disclosure events during the interstitial period after the filing of their application). These rates of disclosure events for individuals associated with NAC appeals and SD Applications are much higher than the rate among all registered individuals. See Initial Filing, Exh. 3c (showing that 167 individuals registered in 2018 had final criminal matter(s) and 2,218 had "specified risk event(s)," which is less than 0.5% of the approximately 630,000 registered individuals). See also Initial Filing, Exh. 3e (showing that individuals who would have met the proposed Rule 1017(a)(7) criteria during the 2013-2016 review period had 16-49 times more new "final criminal matters" and "specified risk events" in the years after identification than other individuals).

10 See Initial Filing, 85 FR 20745, 20754.

11 Alpine, supra note 5, at 4-5; see also note 9, supra.

are substantially more likely than other individuals to harm investors.[12] Moreover, FINRA believes the estimated number of disclosure events associated with persons who appeal disciplinary decisions reflects a specific potential risk that is troubling, especially considering how it "likely underrepresent[s] the overall risk of customer harm posed by these brokers."[13]

Alpine also comments that the proposal raises "due process concerns."[14] Alpine's primary critique is that the proposed rule change would involve, or be similar to, using "pure propensity evidence as a means to establish guilt of wrongdoing."[15]

FINRA disagrees with these assertions. The proposed rule change seeks to strengthen the tools FINRA has to respond to brokers who have a significant history of misconduct and the firms that employ them, while including significant steps to ensure fair processes. As FINRA previously addressed extensively, fair process is vital and FINRA believes the proposed processes are fair ones.[16] Further, FINRA emphasizes that individual brokers subject to the proposed rules would have existing disciplinary history, and FINRA believes the Proposal would lead to greater oversight of their activities by their firms, thereby enhancing investor protections. For example, proposed Rule 9285(a) provides that the conditions and restrictions imposed would be ones that the Hearing Officer considers reasonably necessary for the purpose of preventing customer harm. The conditions and restrictions should target the misconduct demonstrated in the disciplinary proceeding and

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12 See Initial Filing, 85 FR 20745, 20758, 20759 (explaining how there were 110-215 individuals per year during the 2013-2018 review period who would have met the proposed Rule 1017(a)(7) criteria, and how these persons had on average approximately 16-49 times more disclosure events than other brokers who sought the proposed roles).

13 As discussed above, the estimated rate of disclosure events for individuals who appeal disciplinary decisions (28%) is more than 50 times higher than the corresponding rate among all registered individuals (less than 0.5%). See note 9, supra; see also Initial Filing, 85 FR 20745, 20756 n.75 (explaining how the estimates only included the specific events and outcomes described in the proposed amendments to the membership rules). Alpine criticizes how the estimate includes disclosure events "through the year-end after the year in which the appeal reached a decision," but that parameter is "to allow sufficient time for events that occurred during the pendency of the NAC appeal to reach a resolution." See Initial Filing, 85 FR 20745, 20756 & n.74.

14 Alpine, supra note 5, at 5-6.

15 Alpine, supra note 5, at 5-6.

16 See Response Letter, supra note 3, at 2-3; see also Initial Filing, 85 FR 20745, 20755, 20763, 20764.

be tailored to the specific risks posed by the broker or member firm. Further, the proposed fair process would require each of the following steps: a motion to be filed with a Hearing Officer, an opportunity for the respondent to file a written opposition or other response, a written order by the Hearing Officer, the right for a respondent to seek expedited review before the NAC's Review Subcommittee of an order that imposes conditions or restrictions, and an automatic stay when a respondent requests such an expedited review.[17]

Proposed Conditions and Restrictions

Alpine writes that FINRA did not explain why proposed Rule 9285 would allow conditions and restrictions to be imposed by a Hearing Officer instead of a Hearing Panel.[18] FINRA has explained, however, that the Hearing Officer would be able to issue orders more expeditiously.[19] This will be critical, considering the interim period during which the conditions and restrictions would apply. Moreover, the Hearing Officer would be knowledgeable about the case and, therefore, well suited to craft conditions or restrictions that are tailored to addressing the potential customer harm.[20] And as explained above, there are significant procedural protections. Respondents would have the ability to seek expedited reviews of orders imposing conditions or restrictions, and a request for such an expedited review would automatically stay the Hearing Officer's order.

Alpine contends that the standard for imposing conditions and restrictions is vague.[21] Proposed Rule 9285(a)(5) would permit a Hearing Officer to impose conditions and restrictions that the Hearing Officer "considers reasonably necessary for the purpose of preventing customer harm." As FINRA previously explained in addressing similar comments, this standard is consistent with the rules of numerous other self-regulatory organizations,[22] and FINRA believes that it provides sufficient and appropriate limiting parameters that will yield conditions or restrictions that are targeted at the specific, identifiable risks to customers and are not overly burdensome.[23] FINRA also has provided guidance about the standard and several examples of conditions and restrictions that could

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17 The proposed rules also would give the Hearing Officer and the Review Subcommittee the discretion to allow replies and oral arguments.

18 Alpine, supra note 5, at 6-7.

19 See Initial Filing, 85 FR 20745, 20747.

20 See Initial Filing, 85 FR 20745, 20747, 20763.

21 Alpine, supra note 5, at 7.

22 See Initial Filing, 85 FR 20745, 20763 & n.112.

23 See Initial Filing, 85 FR 20745, 20763.

be imposed.[24] Although Alpine expresses concern that the conditions and restrictions could be more onerous than the sanctions, that is not consistent with FINRA's stated intent.[25]

Alpine analogizes conditions and restrictions to "injunctive-type" sanctions, and then contends that Section 15A(b)(7) of the SEA does not authorize FINRA to impose injunctive-type sanctions.[26] The conditions and restrictions that could be imposed, however, are not sanctions; rather, they are protections against risks of customer harm that would apply during a disciplinary appeal while the sanctions are not yet effective.[27]

Alpine also contends that FINRA has not established that its existing sanctions do not provide sufficient protections.[28] The conditions and restrictions, however, would be effective during a disciplinary appeal, when most sanctions are stayed.[29] Alpine notes that a permanent cease and desist order is not stayed during an appeal to the NAC, but the primary purpose of such a sanction is to order a respondent "to cease and desist permanently from violating a specific rule or statutory provision."[30] That is different from the purpose of proposed Rule 9285, which would allow FINRA to seek interim conditions and restrictions that are reasonably necessary for the purpose of preventing customer harm while a disciplinary appeal is pending. This is intended to prevent a specific type of harm with conditions and restrictions that are tailored to the specific risks posed by the broker or member firm.

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24 See Initial Filing, 85 FR 20745, 20747-48, 20763 (explaining that the conditions and restrictions imposed should "target the misconduct demonstrated in the disciplinary proceeding and be tailored to the specific risks posed by the member firm or broker").

25 Alpine, supra note 5, at 8; see also Initial Filing, 85 FR 20745, 20756.

26 Alpine, supra note 5, at 7.

27 FINRA also notes that Alpine's contention that FINRA may not impose injunctive-type sanctions is incorrect. Among the sanctions authorized by Section 15A(b)(7) of the SEA are "limitations of activities, functions, and operations" and "any [ ] fitting sanction." 15 U.S.C. 78o-3(b)(7). Moreover, FINRA's Sanction Guidelines include an array of injunctive-type requirements that FINRA adjudicators may impose to achieve deterrence and remediate misconduct. FINRA Sanction Guidelines, at 3-4 (2019).

28 Alpine, supra note 5, at 9-10.

29 See FINRA Rules 9311(b), 9370(a).

30 See FINRA Rule 9291(a).

Proposed Amendments to the Rule 1000 Series

With respect to the proposed definition of "specified risk event" in proposed Rule 1011(p), Alpine comments that the $15,000 threshold for including arbitration awards and settlements is too low.[31] FINRA extensively considered the dollar threshold. This included assessing a range of thresholds at, and higher than, $15,000 and estimating the number of individuals that would be impacted at different thresholds if such thresholds were included in the Rule 1017(a)(7) criteria, with the other proposed parameters (e.g., the lookback period, the number of disclosure events required, the types of roles sought) being fixed.[32] Moreover, as FINRA has previously explained, because the proposed Rule 1017(a) criteria—including the $15,000 threshold—are based on disclosure events required to be reported on the Uniform Registration Forms, firms, in general, would be able to identify the specific set of disclosure events that would count towards the proposed criteria and, using available data, determine independently whether a proposed association with an individual would require a materiality consultation.[33] Using a dollar threshold different than the current reporting requirements—which any threshold higher than $15,000 would be—could reduce transparency to the public, registered persons, and firms.[34]

Alpine similarly expresses concern with how the "specified risk event" definition includes arbitration settlements.[35] As FINRA has explained, when determining the proposed Rule 1017(a)(7) threshold for when a materiality consultation would be required, FINRA considered all categories of disclosure events reported on the Uniform Registration Forms, and it focused significant attention on the economic trade-off between including individuals who are less likely to subsequently pose risk of harm to customers, and not including individuals who are more likely to subsequently pose risk of harm to customers.[36] This led FINRA not only to include certain arbitration settlements but also to exclude others, such as "subject of" settlements, settlements beyond the five-year lookback period, and settlements by persons other than those seeking to be an owner, control person, principal, or registered person.[37]

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31 Alpine, supra note 5, at 11.

32 See Initial Filing, 85 FR 20745, 20761 (explaining how FINRA considered thresholds between $15,000-$100,000).

33 See Initial Filing, 85 FR 20745, 20754.

34 See Initial Filing, 85 FR 20745, 20754, 20758, 20761, 20767.

35 Alpine, supra note 5, at 12.

36 See Initial Filing, 85 FR 20745, 20754, 20759, 20760.

37 See Initial Filing, 85 FR 20745, 20760-62.

FINRA also disagrees with Alpine's comment that the "specified risk event" definition "attempts to replace the analysis" conducted in a continuing membership application ("CMA") with "a bright-line rule that any customer arbitration" at or above the $15,000 threshold "is defined as creating a risk to investors."[38] Under proposed Rule 1017(a)(7), the only arbitration awards or settlements that are considered are the ones that meet the specific parameters in Rule 1017(a)(7). A single award or settlement would not require a materiality consultation. Furthermore, when a person meets the Rule 1017(a)(7) standard, that would not necessarily mean a CMA is required or, if it is, that the firm could not satisfy FINRA's membership standards.

Anticipated Costs

Alpine comments that the proposed changes to the Rule 9200 Series, 9300 Series, 9520 Series and Rule 1000 Series will impose costs on firms and individuals.[39] FINRA, however, has already assessed and considered the economic impact by analyzing the regulatory need for the proposed rulemaking, its potential economic impacts, including anticipated benefits and costs, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.[40] This assessment included various factors that would lessen the anticipated costs and the expected number of individuals who would be directly impacted by the proposed rule changes.[41]

Alpine writes that preparing a CMA "carries a risk of denial that can be very detrimental, including possible disciplinary action."[42] Alpine, however, has provided no

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38 Alpine, supra note 5, at 11-12.

39 Alpine, supra note 5, at 8-10, 12.

40 See Initial Filing, 85 FR 20745, 20755-20762. For example, Alpine comments about the potential impacts of an unstayed condition or restriction on a firm's relationships with customers, counterparties and self-regulatory organizations, and the costs of preparing a submission for a materiality consultation. Alpine, supra note 5, at 9, 12. The EIA, however, noted the potential impacts of conditions and restrictions on economic opportunities and services to customers, and that firms would be impacted by the requirement to seek a materiality consultation. See, e.g., Initial Filing, 85 FR 20745, 20757, 20758.

41 See Initial Filing, 85 FR 20745, 20756-59 & n.80 (explaining that during a five-year review period, 77 disciplined brokers were employed by a member firm for all or a part of the disciplinary appeal process; that during a four-year review period, 51 statutorily disqualified individuals were associated with SD Applications; and that 110-215 individuals each year during the review period would have met the proposed Rule 1017(a)(7) criteria).

42 Alpine, supra note 5, at 12.

evidence of instances where the filing of a CMA that was denied was itself the basis of a FINRA disciplinary action. Moreover, FINRA notes that the CMA process requires FINRA to review an application consistent with the membership standards set forth in Rule 1014 which, among other things, require the applicant to demonstrate it is "capable of complying with" applicable federal securities laws and FINRA rules.

Alpine also generally comments about regulatory burdens on small firms.[43] The anticipated costs—which would be borne by firms of all sizes[44]—would apply only in narrowly defined circumstances, as reflected by the number of individuals whom FINRA expects to be impacted by the proposed changes.[45] FINRA believes that these costs are outweighed by the anticipated benefits of adding further protections against the potential risks posed by brokers with a significant history of misconduct.

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FINRA believes that the foregoing responds to the material issues raised by the commenter. If you have any questions, please contact me at [redacted], email: [redacted].

Best regards,

/s/ Michael Garawski

Michael Garawski
Associate General Counsel
FINRA Office of General Counsel

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43 Alpine, supra note 5, at 2.

44 See, e.g., Initial Filing, 85 FR 20745, 20760.

45 Alpine asserts that the cost of heightened supervision would be higher for small firms without providing any analysis to support this assertion. See Alpine, supra note 5, at 10. As discussed in the Initial Filing, the costs and complexity of heightened supervision plans would likely depend on the role, capacity, and risk posed by the applicable individuals. See Initial Filing, 85 FR 20745, 20756-57. These factors would be relevant for all firms that employ these individuals, irrespective of the firm size.