

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-95048; File No. SR-FINRA-2022-014)

June 6, 2022

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend FINRA Rules 4111 (Restricted Firm Obligations) and 9561 (Procedures for Regulating Activities Under Rule 4111)

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on May 26, 2022, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as constituting a “non-controversial” rule change under paragraph (f)(6) of Rule 19b-4 under the Act,³ which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

FINRA is proposing to amend FINRA Rules 4111 and 9561 to make non-substantive and technical amendments.

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.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 17 CFR 240.19b-4(f)(6).

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

On July 30, 2021, the Commission approved rules concerning firms with a significant history of misconduct, including new Rule 4111 (Restricted Firm Obligations), amendments to Rule 9559 (Hearing Procedures for Expedited Proceedings Under the Rule 9550 Series), and new Rule 9561 (Procedures for Regulating Activities Under Rule 4111).⁴ The rules allow FINRA to impose obligations on broker-dealers with significantly higher levels of risk-related disclosures than other similarly sized peers based on numeric, threshold-based criteria.⁵ Specifically, Rule 4111 requires members that are identified as “Restricted Firms” to deposit cash or qualified

⁴ See Securities Exchange Act Release No. 92525 (July 30, 2021), 86 FR 42925 (August 5, 2021) (Order Approving File No. SR-FINRA-2020-041, as Modified by Amendment Nos. 1 and 2) (“SEC Order”); see also Securities Exchange Act Release No. 92525 (July 30, 2021), 86 FR 49589 (September 3, 2021) (Order Approving File No. SR-FINRA-2020-041, as Modified by Amendment Nos. 1 and 2) (Correction).

⁵ See SEC Order, 86 FR 42925, 42926.

securities in a segregated account, adhere to specified conditions or restrictions, or comply with a combination of such obligations.⁶

The annual Rule 4111 process through which FINRA will determine which members are Restricted Firms, and the obligations to impose on them, has several steps and includes features that narrowly focus the obligations on the firms of most concern.⁷ The first step is the annual calculation.⁸ Specifically, for each member, the Department of Member Regulation (“Department”) will compute annually the member’s “Preliminary Identification Metrics” to determine if it meets the “Preliminary Criteria for Identification.”⁹ The date, each calendar year, as of which the Department calculates the Preliminary Identification Metrics to determine if the member meets the Preliminary Criteria for Identification is the “Evaluation Date.”¹⁰

For a member that meets the Preliminary Criteria for Identification during the annual calculation, the Department will conduct an Initial Department Evaluation.¹¹ If the Department determines that the member warrants further review, and such member has met the Preliminary Criteria for the first time, the member will have a one-time staff-reduction opportunity to no longer meet the Preliminary Criteria for Identification.¹² A member that still meets the

⁶ See SEC Order, 86 FR 42925, 42926; see also Rule 4111(i)(16) (defining “Restricted Firm”).

⁷ See SEC Order, 86 FR 42925, 42927.

⁸ See Rule 4111(b).

⁹ See Rule 4111(b); Rule 4111(i)(9) (definition of “Preliminary Criteria for Identification”) and (i)(10) (definition of “Preliminary Identification Metrics”).

¹⁰ See Rule 4111(i)(5).

¹¹ See Rule 4111(c)(1).

¹² See Rule 4111(c)(2).

Preliminary Criteria for Identification after the staff-reduction opportunity, or that does not have a one-time staff-reduction opportunity available, will proceed to a Consultation.¹³

After the Consultation, the Department will issue a Department decision concerning the member.¹⁴ A Department decision will indicate whether the member is designated as a Restricted Firm.¹⁵ For a member that is designated as a Restricted Firm, the Department decision also will state the obligations that are imposed on that member.¹⁶ These obligations can include a “Restricted Deposit Requirement,” specified conditions or restrictions on the operations and activities of the member and its associated persons, or both.¹⁷ Rule 4111(e) includes provisions concerning, in pertinent part, the Department’s 30-day deadline for rendering, and issuing notice of, its decision.¹⁸

To implement Rule 4111, FINRA created two new expedited proceedings.¹⁹ Rule 9561(a) governs a new expedited proceeding that allows a member to request a prompt review of the Department’s determinations. Rule 9561(b) governs a new expedited proceeding to address a member’s failure to comply with any requirements, conditions or restrictions imposed on it pursuant to Rule 4111 and Rule 9561(a). The procedures for the Rule 9561(b) expedited

¹³ See Rule 4111(c); 4111(d).

¹⁴ See Rule 4111(e).

¹⁵ See Rule 4111(e)(1).

¹⁶ See Rule 4111(e)(1)(B) and (C).

¹⁷ See Rule 4111(e)(1)(B) and (C); see also Rule 4111(d)(1); Rule 4111(i)(15) (defining “Restricted Deposit Requirement”).

¹⁸ See Rule 4111(e)(1) and (e)(2).

¹⁹ See SEC Order, 86 FR 42925, 42926.

proceeding include, in pertinent part, provisions concerning the notices that the Department may issue to commence a Rule 9561(b) expedited proceeding and the contents of those notices.²⁰ Rule 9561(b) is expressly referenced in Rule 4111(h), which concerns notices of a member's failures to comply with a Restricted Deposit Requirement or conditions or restrictions imposed pursuant to Rule 4111.

Rules 4111 and 9561, and the amendments to Rule 9559, became effective on January 1, 2022.²¹ The first Evaluation Date for Rule 4111 will be June 1, 2022.²²

FINRA is proposing technical, non-substantive changes to Rules 4111 and 9561, for clarity and consistency, and to avoid unintended consequences of the 30-day deadline currently specified in Rule 4111(e). Specifically, FINRA is proposing amendments to: (1) Rule 4111(b), which concerns the annual calculation of the Preliminary Criteria for Identification, to delete the reference to “on a calendar-year basis,” as the Evaluation Date establishes the operative time periods under the rule; (2) Rule 4111(e), to modify and clarify when the 30-day time period commences for the Department to render, and issue notice of, its decisions; (3) Rule 4111(h), to more closely align its description of the notices issued pursuant to Rule 9561(b) with the text of Rule 9561(b); (4) Rule 9561(b)(3), to modify the second sentence to use the phrase “suspension or cancellation of membership,” to be consistent with how the phrase “suspension or cancellation

²⁰ See Rule 9561(b)(1) and (3).

²¹ See Regulatory Notice 21-34 (September 2021).

²² See Information Notice, February 1, 2022 (FINRA Announces Rule 4111 (Restricted Firm Obligations) Evaluation Date). As FINRA explained in that Information Notice, FINRA plans to actually perform the annual calculation at least 30 days after the June 1, 2022 Evaluation Date, to account for the time between when relevant disclosure events occurred and when firms must report those events on the Uniform Registration Forms. See Rule 4111(i)(17) (defining “Uniform Registration Forms” for purposes of Rule 4111).

of membership” is used throughout Rule 9561; and (5) Rules 4111(f)(3), (i)(2), and (i)(15), to remove the capitalization from the term “Associated Person,” to be consistent with how the term is used throughout the FINRA Rulebook.

Proposed Amendments to Rule 4111(b)

Rule 4111(b) currently provides that, for each member, the Department will compute “annually (on a calendar-year basis) the Preliminary Identification Metrics to determine if the member meets the Preliminary Criteria for Identification.” FINRA proposes to delete from Rule 4111(b) the words “on a calendar-year basis.”

What establishes the relevant time periods for the Rule 4111 annual calculation is the Evaluation Date. The Evaluation Date is defined as “the date, each calendar year, as of which the Department calculates the Preliminary Identification Metrics to determine if the member meets the Preliminary Criteria for Identification.”²³ The first Evaluation Date under Rule 4111 will be June 1, 2022, and FINRA expects that, in subsequent years, the Evaluation Dates also will be on June 1.²⁴ Because the Evaluation Date establishes the operative time periods for the

²³ See Rule 4111(i)(5). The Evaluation Date impacts numerous aspects of the annual Rule 4111 calculation—including, among other things, the dates of the “Evaluation Period,” the “Preliminary Identification Metrics,” the number of “Registered Persons In-Scope,” and the number of “Registered Persons Associated with Previously Expelled Firms”—and which firm-size “Preliminary Identification Metrics Thresholds” apply. See Rule 4111(i)(6) (defining the “Evaluation Period”); 4111(i)(10) (defining “Preliminary Identification Metrics”); 4111(i)(13) (defining “Registered Persons In-Scope”); 4111(i)(4)(F) (defining “Registered Persons Associated with Previously Expelled Firms”); 4111(i)(11) (defining the “Preliminary Identification Metrics Thresholds”).

²⁴ See Information Notice, February 1, 2022 (FINRA Announces Rule 4111 (Restricted Firm Obligations) Evaluation Date). FINRA also has explained, both in Regulatory Notice 21-34 and Information Notice, February 1, 2022, that FINRA will evaluate whether future adjustments of the annual Evaluation Date are warranted and would announce any changes in such date sufficiently in advance.

Rule 4111 annual calculation, FINRA is proposing to delete from Rule 4111(b) the words “on a calendar-year basis.”

Proposed Amendments to Rule 4111(e)

FINRA is proposing to make technical, non-substantive changes to the provisions in Rule 4111(e) that concern the timing of the Department decisions, to modify and clarify when the 30-day time period commences for the Department to render, and issue notice of, its decisions.

Currently, Rule 4111(e)(1) provides, in pertinent part, that “[f]ollowing the Consultation, but no later than 30 days from the date of the latest letter provided to the member under paragraph (d)(2) of this Rule, the Department shall render a Department Decision”

Similarly, Rule 4111(e)(2) provides, in pertinent part, that “[n]o later than 30 days following the latest letter provided to the member under paragraph (d)(2) of this Rule, the Department shall issue a notice of the Department’s decision pursuant to Rule 9561(a)” The letters that FINRA can provide pursuant to Rule 4111(d)(2) include ones that schedule the Consultation and ones that postpone the commencement of the Consultation for good cause shown.²⁵ Rule 4111(d)(2) requires that the Department provide the written Consultation scheduling letter to the member firm “at least seven days prior to the Consultation.” Rule 4111(d)(2) further provides that “[p]ostponements shall not exceed 30 days unless the member establishes the reasons a longer postponement is necessary.”

FINRA’s intent was to provide the Department with a reasonable amount of time following the Consultation to evaluate the information that a member provides during the Consultation and prepare its decision. However, commencing the 30-day deadline period from the “date of the latest letter to the member under [Rule 4111(d)(2)]” could result in the

²⁵ See Rule 4111(d)(2).

Department having little to no time to prepare its decision after the Consultation, especially when the Department sends a written letter granting a postponement of a Consultation for good cause shown. When a postponement is granted, the amount of time the Department would have to prepare its decision would depend on how far in advance of the postponed Consultation the Department sends the letter granting the postponement request. In some cases, depending on how long a postponement is granted, postponement letters could be provided 30 days or more before a postponed Consultation, leaving the Department with no time to prepare a decision following the postponed Consultation or evaluate the information provided by the member during the Consultation.²⁶

Commencing the 30-day decision deadline period from the “date of the latest letter provided to the member under [Rule 4111(d)(2)]” also could have other unintended impacts on the Rule 4111 process. Rule 4111(d)(2) requires the Department to provide a written letter scheduling the Consultation “at least seven days prior to the Consultation,” but the “latest letter” provisions in Rule 4111(e) could create a disincentive for the Department to provide more than seven days’ notice of the Consultation; each additional day of notice provided would translate into one less day for the Department to prepare its decision following the Consultation. Likewise, Rule 4111(d)(2) provides that postponements of Consultations “shall not exceed 30 days unless the member establishes the reasons a longer postponement is necessary,” but the “latest letter” provisions could create a disincentive for the Department to grant postponements of a length that would leave it with little or no time to prepare its decisions.

FINRA is also seeking to provide clarity to members on when the 30-day decision deadline period would begin, because the “latest letter” provisions may create potential

²⁶ See Rule 4111(d)(2).

ambiguity as to what communication starts, or restarts, the 30-day clock. For example, there could be occasions when the Department, after sending an initial letter scheduling the Consultation, needs to send subsequent scheduling letters that revise minor scheduling details (e.g., adjustments to the day, starting time, or location of the Consultation; changes to audio or video conferencing details). In such situations, it may not be clear which scheduling letter would qualify as the “latest” letter from which the 30-day decision deadline period commences.

For these reasons, FINRA is proposing to amend Rule 4111(e)(1) and (e)(2) to require that the Department decision be rendered, and that notice of that decision be issued, no later than 30 days from the Consultation. This would ensure that the Department always has a reasonable amount of time to evaluate the information provided by a member during, and prepare its decisions after, the Consultation, and clarify when the 30-day decision deadline period begins.

Proposed Amendments to Rule 4111(h)

FINRA also is proposing non-substantive, technical changes to Rule 4111(h), to more closely align its description of the notices issued pursuant to Rule 9561(b) with the text of Rule 9561(b).

Currently, Rule 4111(h) provides that FINRA may issue a notice “pursuant to Rule 9561(b)” directing a member that is not in compliance with the Restricted Deposit Requirement or the conditions or restrictions imposed to “suspend all or a portion of its business.” The general description in Rule 4111(h) of the notices that may be issued pursuant to Rule 9561(b), however, does not align with how Rule 9561(b) describes them. In this regard, the phrase “suspension or cancellation of membership” (and, likewise, the phrase “suspension or cancellation”) is used throughout Rule 9561(b). For example, Rule 9561(b)(1) provides that if a

member fails to comply with any Rule 4111 Requirements imposed,²⁷ the Department, after receiving authorization from FINRA’s Chief Executive Officer or such other executive officer as the Chief Executive Officer may designate, may issue a “suspension or cancellation” notice to such member stating that the failure to comply with the Rule 4111 Requirements within seven days of service of the notice will result in a “suspension or cancellation of membership.” These phrases also are used in the title of Rule 9561(b)(1), as well as in Rule 9561(b)(3), (4), and (6).²⁸ In addition, Rule 4111(h) does not currently describe how notices issued pursuant to Rule 9561(b) shall state that the failure to comply within seven days of service of the notice will result in a suspension or cancellation of membership.²⁹

Rule 4111(h) was intended to be entirely consistent with Rule 9561(b), as reflected by the fact that Rule 4111(h) expressly provides that FINRA may issue a notice “pursuant to Rule 9561(b).” Thus, for purposes of consistency and clarity, FINRA proposes to amend Rule 4111(h) to provide that, pursuant to the procedure set forth in Rule 9561(b), FINRA may issue a suspension or cancellation notice to a member that is not in compliance with a Restricted Deposit Requirement or conditions or restrictions imposed by Rule 4111, stating that the failure to

²⁷ In Rule 9561, “the Rule 4111 Requirements” refer collectively to the requirements, conditions or restrictions to which a Restricted Firm is subject. See Rule 9561(a)(1).

²⁸ See Rule 9561(b)(1) (titled “Notice of Suspension or Cancellation”), 9561(b)(3) (explaining that the notice shall explain that a Hearing Officer “may approve or withdraw the suspension or cancellation of membership”), 9561(b)(4) (explaining the effective date of a “suspension or cancellation”), and 9561(b)(6) (explaining the effective date of a “suspension or cancellation” when no hearing is timely requested); see also Rule 9559(n)(6) (“In any action brought under Rule 9561(b), the Hearing Officer may approve or withdraw the suspension or cancellation of membership . . .”).

²⁹ See Rule 9561(b)(1).

comply within seven days of service of the notice will result in a suspension or cancellation of membership.

Proposed Amendments to Rule 9561(b)(3)

FINRA also is proposing technical amendments to modify the second sentence of Rule 9561(b)(3) to use the phrase “suspension or cancellation of membership,” to be consistent with how the phrase “suspension or cancellation of membership” is used throughout Rule 9561.

Rule 9561(b)(3) governs the contents of a Rule 9561(b)(1) notice of suspension or cancellation of membership. Currently, the second sentence of Rule 9561(b)(3) provides, in pertinent part, that “[t]he notice shall state when the suspension will take effect and explain what the respondent must do to avoid such suspension.” This use of the word “suspension” is inconsistent with how the phrase “suspension or cancellation” (and, similarly, “suspension or cancellation of membership”) is used throughout Rule 9561(b), including in a later sentence in Rule 9561(b)(3).³⁰ Accordingly, for consistency and clarity, FINRA proposes to modify the second sentence of Rule 9561(b)(3) to use the phrase “suspension or cancellation of membership.”

Other Technical, Non-Substantive Changes

³⁰ See Rule 9561(b)(1), (3), (4) and (6); see also Rule 9559(n)(6).

FINRA also proposes to amend various provisions in Rule 4111 to remove the capitalization of the term “Associated Persons.”³¹ This would be consistent with how, throughout the FINRA Rulebook, the term “associated person” is generally not capitalized.³²

FINRA has filed the proposed rule change for immediate effectiveness and has requested that the SEC waive the requirement that the proposed rule change not become operative for 30 days after the date of the filing, so FINRA can implement the proposed rule change immediately.³³

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,³⁴ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable

³¹ The capitalized term “Associated Persons” is in Rule 4111(f)(3) (concerning requests by Previously Designated Restricted Firms for withdrawals from a Restricted Deposit Requirement), (i)(2) (defining “Covered Pending Arbitration Claim”), and (i)(15) (defining “Restricted Deposit Requirement”).

³² The definition of “Covered Pending Arbitration Claim” in Rule 4111(i)(2) was modeled on the definition of the same term in Rule 1011(c), which is in the Rule 1000 Series (Member Application and Associated Person Registration). See Securities Exchange Act Release No. 90527 (November 27, 2020), 85 FR 78540, 78541-42 n.10 (December 4, 2020) (Notice of Filing of SR-FINRA-2020-041). In Rule 1011(c), as well as in some other provisions in the Rule 1000 Series, the term “Associated Person” is capitalized. The Rule 1000 Series, however, has a specific definition of the term “Associated Person” that applies specifically to the Rule 1000 Series. See Rule 1011(b).

³³ FINRA notes that the proposed rule change would impact all members, including members that have elected to be treated as capital acquisition brokers (“CABs”), given that the CAB rule set incorporates the impacted FINRA rules by reference. The proposed rule change would not impact, however, member firms that are funding portals, because the Funding Portal rule set neither incorporates the impacted FINRA rules by reference nor contains parallel rule provisions. See Funding Portal Rule 900(a) (excepting FINRA Rule 9561 from the application of the FINRA Rule 9000 Series to funding portals).

³⁴ 15 U.S.C. 78q-3(b)(6).

principles of trade, and, in general, to protect investors and the public interest. The proposed rule change will make non-substantive, technical amendments that FINRA believes will provide greater clarity and consistency to its rules.

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. The proposed rule change brings clarity and consistency to FINRA rules without adding any burden on firms.

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

Written comments were neither solicited nor received.

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

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act³⁵ and Rule 19b-4(f)(6) thereunder.³⁶

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the

³⁵ 15 U.S.C. 78s(b)(3)(A).

³⁶ 17 CFR 240.19b-4(f)(6).

Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2022-014 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2022-014. 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 10:00 a.m.

and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2022-014 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.³⁷

J. Matthew DeLesDernier
Assistant Secretary

³⁷ 17 CFR 200.30-3(a)(12).