

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * <input type="text" value="66"/>	SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 Form 19b-4	File No.* SR - <input type="text" value="2010"/> - * <input type="text" value="034"/> Amendment No. (req. for Amendments *) <input type="text" value="1"/>
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Proposed Rule Change by Financial Industry Regulatory Authority
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

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

Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>
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Description
Provide a brief description of the proposed rule change (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 proposed rule change.

First Name * <input type="text" value="Afshin"/>	Last Name * <input type="text" value="Atabaki"/>
Title * <input type="text" value="Assistant General Counsel"/>	
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Telephone * <input type="text" value="(202) 728-8902"/>	Fax <input type="text" value="(202) 728-8264"/>

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 officer.

Date

By

(Name *) (Title *)

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 (required)

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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 (required)

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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 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

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 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

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 4 - Marked Copies

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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

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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

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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 Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “SEA”),¹ Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) Amendment No. 1 to SR-FINRA-2010-034, a proposed rule change to adopt NASD Rule 3070 (Reporting Requirements) as FINRA Rule 4530 (Reporting Requirements) in the consolidated FINRA rulebook, subject to certain amendments, and to delete paragraphs (a) through (d) of Incorporated NYSE Rule 351 (Reporting Requirements) and Incorporated NYSE Rules 351.10 and 351.13. The proposed rule change also would add a supplementary material section to proposed FINRA Rule 4530.

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

(b) Upon Commission approval and implementation by FINRA of the proposed rule change as modified by Amendment No. 1, the corresponding NASD and Incorporated NYSE rules, or sections thereof, will be eliminated from the current FINRA rulebook.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

At its meeting on September 16, 2008, 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 as modified by Amendment No. 1.

¹ 15 U.S.C. 78s(b)(1).

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

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

(a) Purpose

Rule Filing History

On July 30, 2010, FINRA filed with the SEC SR-FINRA-2010-034,² a proposed rule change to adopt NASD Rule 3070 as FINRA Rule 4530 in the consolidated FINRA rulebook (“Consolidated FINRA Rulebook”),³ subject to certain amendments as described in the Proposing Release. The proposed rule change also would delete paragraphs (a) through (d) of Incorporated NYSE Rule 351⁴ and NYSE Rules 351.10 and

² See Securities Exchange Act Release No. 62621 (July 30, 2010), 75 FR 47863 (August 9, 2010) (Notice of Filing of SR-FINRA-2010-034) (“Proposing Release”). The comment period closed on August 30, 2010.

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

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

351.13 from the Transitional Rulebook.⁵ Further, the proposed rule change would add a supplementary material section to proposed FINRA Rule 4530 as detailed in the Proposing Release. The proposed rule change was published for comment in the Federal Register on August 9, 2010. The Commission received seven comment letters in response to the proposed rule change.⁶ Based on comments received, FINRA is filing this Amendment No. 1 to respond to the comments and to propose amendments, where appropriate.

⁵ NYSE Rule 351(e) and NYSE Rule Interpretation 351(e)/01 (Reports of Investigation) govern trade investigation reporting requirements. NYSE Rules 351(f), 351.11 and 351.12 govern the annual attestation requirement of the research analyst conflict of interest rules. These provisions will be addressed as part of the supervision rules and research analyst conflict of interest rules, respectively. See Regulatory Notice 08-24 (May 2008) (Proposed Consolidated FINRA Rules Governing Supervision and Supervisory Controls) and Regulatory Notice 08-55 (October 2008) (FINRA Requests Comment on Proposed Research Registration and Conflict of Interest Rules).

⁶ See Letter from Brendan Daly, Legal and Compliance Counsel, Commonwealth Financial Network, to Elizabeth M. Murphy, Secretary, SEC, dated August 27, 2010 (“Commonwealth”); Letter from Clifford Kirsch and Susan Krawczyk, Sutherland Asbill & Brennan LLP, for the Committee of Annuity Insurers, to Elizabeth M. Murphy, Secretary, SEC, dated August 30, 2010 (“CAI”); Letter from Joan Hinchman, Executive Director, President and CEO, National Society of Compliance Professionals, Inc., to Elizabeth M. Murphy, Secretary, SEC, dated August 30, 2010 (“NSCP”); Letter from Kristin Bulls, Products and Broker-Dealer Compliance Director, State Farm VP Management Corp., to Elizabeth M. Murphy, Secretary, SEC, dated August 30, 2010 (“State Farm”); Letter from Michael Lesutis, Assistant General Counsel, PFS Investments, Inc., to Elizabeth M. Murphy, Secretary, SEC, dated September 1, 2010 (“PFS”); Letter from James T. McHale, Managing Director and Associate General Counsel, the Securities Industry and Financial Markets Association, to Elizabeth M. Murphy, Secretary, SEC, dated September 1, 2010 (“SIFMA”); and Letter from Dale E. Brown, President & CEO, the Financial Services Institute, to Elizabeth M. Murphy, Secretary, SEC, dated September 15, 2010 (“FSI”). (Available at <http://www.sec.gov/comments/sr-finra-2010-034/finra2010034.shtml>.)

Proposal

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

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

Response to Comments

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

One commenter argues that the requirement to report external findings related to any insurance matter is unwarranted and burdensome.⁷ For instance, the proposed rule may capture findings related to an associated person's failure to timely meet insurance continuing education requirements. The commenter asks that FINRA limit the proposal to those external findings that derive from a transaction with a customer.

⁷ State Farm.

As noted in the Proposing Release, current NASD Rule 3070(a)(1) requires that a firm report whenever the firm or an associated person of the firm has been found to have violated “any” rule or standard of conduct of “any” governmental agency, self-regulatory organization (“SRO”), or financial business or professional organization. Thus, firms currently are required to report external findings related to “insurance” matters, and it is not a novel requirement. The proposed rule simply continues this requirement, which has been a part of NASD Rule 3070 since its adoption. Further, the requirement to report insurance matters is consistent with other provisions of the current rules.⁸ More importantly, this information is relevant to FINRA’s programs since it assists FINRA in identifying firms, offices and associated persons that may pose a regulatory risk.

Another commenter requests that FINRA provide additional examples of the kinds of external events that firms should report under the proposed rule.⁹ As stated in FINRA Rule 4530.02, FINRA Rule 4530(a)(1)(A) is limited to situations where there has been a finding of violative conduct by an external body, such as a court, domestic or foreign regulatory body, SRO or business or professional organization. For example,

⁸ See NASD Rule 3070(a)(3) and NYSE Rule 351(a)(3) (requiring reporting where a firm or an associated person is named as a defendant or respondent in any proceeding brought by a regulatory or self-regulatory body alleging the violation of any insurance laws, rules or regulations); NASD Rule 3070(a)(4) and NYSE Rule 351(a)(4) (requiring reporting where a firm or an associated is disciplined by any insurance regulatory or self-regulatory body, is denied membership or continued membership in any such self-regulatory body, or is barred from becoming associated with any member of any such self-regulatory body); and NASD Rule 3070(a)(6) and NYSE Rule 351(a)(6) (requiring reporting where a firm or an associated person is a director, controlling stockholder, partner, officer, sole proprietor, or an associated person of an insurance company that was suspended, expelled or had its registration denied or revoked).

⁹ NSCP.

consistent with the requirements of current NASD Rule 3070(a)(1), firms will continue to be required to report a court finding relating to the violation of insurance laws.

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

As discussed in the Proposing Release, the proposed rule requires the reporting of any “insurance” civil litigation or arbitration that is “financial related.”

Three commenters believe that the phrase “financial related” needs additional clarification.¹⁰ In response, FINRA has added FINRA Rule 4530.09 to the proposal defining the term “financial related” to mean related to the provision of financial services. Two of these commenters also suggest that the requirement to report insurance matters stemming from civil litigation or arbitration be limited to insurance products that are securities.¹¹ The proposed rule excludes certain insurance products, such as traditional auto and health insurance. However, FINRA does not believe that the proposed rule should be limited to insurance products that are securities. Civil litigation or arbitration involving non-securities insurance products that is related to the provision of financial services will be subject to the proposed rule.

The proposed rule also requires the reporting of any claim for damages by a customer or broker-dealer that is “financial” or “transactional” in nature. As noted in the Proposing Release, FINRA believes that transactional claims by customers, including contractual disputes, are relevant to its programs since they may reveal misconduct, such as an impermissible customer loan.

¹⁰ CAI, NSCP and State Farm.

¹¹ CAI and NSCP.

One commenter argues that the example offered (i.e., such information may reveal an impermissible customer loan) relates to a transaction that may be within the province of another regulator to address and not necessarily relevant to FINRA.¹² The commenter suggests that the proposed rule exclude matters that do not involve securities activities. FINRA disagrees. Moreover, the example offered in the Proposing Release relates directly to a FINRA rule, FINRA Rule 3240 (Borrowing From or Lending to Customers).

Another commenter believes that the provision requires further clarification since nearly all insurance related claims, including traditional auto and health insurance, ultimately are transactional (contractual) in nature.¹³ In response to this comment, FINRA has revised the proposed rule to require the reporting of any claim for damages by a customer or broker-dealer that relates to the provision of financial services or relates to a financial transaction.

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

As discussed in the Proposing Release, FINRA Rule 4530(b) generally incorporates the requirement under NYSE Rule 351(a)(1) and provides that a firm is required to report to FINRA no later than 30 calendar days after the firm has concluded, or reasonably should have concluded, on its own that an associated person of the firm or the firm itself has engaged in violations of any securities-, insurance-, commodities-,

¹² NSCP.

¹³ State Farm.

financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or SRO.

Two commenters believe that the requirement should be eliminated.¹⁴ One of these commenters argues that the proposal runs counter to the concept of voluntary self-reporting and credit for cooperation and to the implementation of robust compliance programs intended to identify and fix problems.¹⁵ Two commenters are concerned that the proposal will increase the administrative burden on firms.¹⁶ One of these commenters argues that FINRA has not described what matters firms are failing to disclose and whether existing practices have caused any impediments to identifying and addressing misconduct by firms or associated persons.¹⁷

One of the main purposes of the consolidation process is to consider both sets of rules, NASD and NYSE, and determine the appropriate investor protection standard to be included in the FINRA Rules. FINRA recognizes that NYSE Rule 351(a)(1) provides a heightened standard of investor protection by requiring firms to report internal conclusions of violative conduct. Moreover, FINRA's examination programs use this information as part of their assessment processes and risk-based analyses.

One commenter argues that compliance decisions are based on whether there has been a failure to comply with policies and procedures, which may not necessarily align with a specific regulatory violation, and that the proposal would require firms to further

¹⁴ CAI and State Farm.

¹⁵ CAI.

¹⁶ Commonwealth and NSCP.

¹⁷ NSCP.

analyze every compliance issue to determine whether there also has been a reportable regulatory violation.¹⁸ In response, FINRA notes that a firm’s policies and procedures are informed by applicable laws, rules and regulations. For instance, NASD Rule 3010 (Supervision) requires firms to establish, maintain and enforce written supervisory procedures that are reasonably designed to achieve compliance with applicable securities laws, rules and regulations. Further, in evaluating the nature and gravity of noncompliant conduct, firms would have to assess the extent to which applicable laws, rules and regulations have been violated.

Two commenters argue that the term “concluded” is vague.¹⁹ One of these commenters states that case-specific conclusions are routinely made in a number of departments.²⁰ The other commenter suggests that the proposal does not indicate who within a firm must have “concluded” that a violation occurred before it becomes reportable.²¹ A firm is free to determine the person(s) within the firm responsible for making such determinations. As explained in the Proposing Release, a firm is free to determine the level of seniority required of an associated person in making a determination of a reportable internal conclusion; however, it will not be a defense to a failure to report such conduct that it was of a nature that did not merit consideration by a person of such seniority. Additionally, it may be possible that a department within a firm reaches a conclusion of violation, but on review, senior management reaches a different

¹⁸ CAI.

¹⁹ NSCP and State Farm.

²⁰ State Farm.

²¹ NSCP.

conclusion. Nothing in the proposed rule would prohibit a firm from relying on senior management's determination, provided such determination is reasonable as explained below.

Several commenters are concerned with the "reasonably should have concluded" standard.²² Two of these commenters argue that FINRA did not explain why it was adding this standard.²³ Two commenters state that the "reasonably should have concluded" standard would create uncertainty and should be eliminated.²⁴ Another commenter believes that the standard is flawed since it is far too subjective and would be subject to inconsistent application by firms and FINRA.²⁵ One commenter believes that FINRA staff may use the standard to penalize firms when they have acted in good faith based on information available at the time in evaluating a compliance issue, but failed to anticipate how an issue might ultimately develop.²⁶ Two commenters believe that the standard could be used on a hindsight basis for FINRA to pursue actions if it concludes after the fact that a firm should have self reported.²⁷ Three commenters argue that the standard places a firm in the precarious position in which inherently subjective assessments will be susceptible to second guessing.²⁸ One of these commenters also

²² CAI, NSCP, PFS, SIFMA and FSI.

²³ CAI and NSCP.

²⁴ CAI and FSI.

²⁵ SIFMA.

²⁶ CAI.

²⁷ NSCP and SIFMA.

²⁸ CAI, PFS and FSI.

argues that the requirement to report within 30 calendar days of the date on which the firm “reasonably should have concluded” that a violation occurred may increase the threat of FINRA enforcement actions.²⁹ According to the commenter, a firm might take 60 calendar days to reach a conclusion and report the finding, only to have FINRA decide later that the conclusion should have been reached sooner.

As noted in the Proposing Release, the “knows or should have known” standard, which is applicable to other provisions of FINRA Rule 4530, does not fit in the context of internal findings. Rather, the standard applicable to a firm’s internal conclusion of violation is the “has concluded or reasonably should have concluded” standard. However, the “reasonably should have concluded” standard cannot be read in a vacuum. If a firm has made a good faith reasonable determination, it is not enough for FINRA to simply engage in second guessing. If a reasonable person would have concluded that a violation occurred, then the matter is reportable. Conversely, if a reasonable person would not have concluded that a violation occurred, then the matter is not reportable.

Two commenters argue that the requirement to report insurance matters should be eliminated.³⁰ One of these commenters asks whether FINRA will take action if the internal conclusion relates to a violation of insurance laws.³¹ The commenter also asks if a firm has an obligation to report if the determination regarding the violation of insurance laws is made by the firm’s insurance affiliate and involves the firm. As noted above, information relating to insurance matters is relevant to FINRA’s programs since it assists

²⁹ PFS.

³⁰ CAI and NSCP.

FINRA in identifying firms, offices and associated persons that may pose a regulatory risk. With respect to a determination by an affiliate of a firm, the firm should report it absent a reasonable rejection of such a determination.

Several commenters are concerned with the statement in the Proposing Release that an internal audit finding creates a strong presumption that the matter is reportable.³² The commenters argue that the “strong presumption” language has the potential to undermine the internal audit process. Some commenters suggest that matters subject to a firm’s internal review process as required under other rules (e.g., FINRA Rule 3130 (Annual Certification of Compliance and Supervisory Processes)) should be excluded from the proposed requirement.³³ Three of these commenters note that when the rules regarding internal review processes were adopted, FINRA staff assured firms that FINRA would not use the reports and review processes under those rules as a roadmap for disciplinary action against a firm or a registered person and that firms would be given latitude to resolve uncovered deficiencies resulting from their reviews.³⁴

The reporting obligation under the proposed rule and the internal review processes set forth under other rules (e.g., FINRA Rule 3130) are mutually exclusive. While internal review processes may inform a firm’s determination that a specific violation occurred, they do not by themselves lead to the conclusion that the matter is reportable for purposes of the proposed rule. For example, FINRA would not view a

³¹ CAI.

³² Commonwealth, NSCP and SIFMA.

³³ Commonwealth, CAI, NSCP, SIFMA and FSI.

³⁴ Commonwealth, CAI and FSI.

discussion in an internal audit report regarding the need for enhanced controls in a particular area, standing alone, as determinative of a reportable violation for purposes of the proposed rule. FINRA also wishes to clarify that, rather than creating a strong presumption, an internal audit finding would serve only as one factor, among others, that a firm should consider in determining whether a violation occurred.

Additionally, as set forth in the Proposing Release, FINRA Rule 4530.01 excluded from the reporting requirement an isolated violation by the firm or an associated person of the firm that could be reasonably viewed as a ministerial violation of the applicable rules that did not result in customer harm and was remedied promptly upon discovery. FINRA also provided an example in the Proposing Release of the types of reportable and non-reportable matters.

All of the commenters state that the proposed exclusion is too narrow and that the example provided in the Proposing Release does not provide sufficient clarity.³⁵ Some of these commenters ask that FINRA reevaluate the standard set forth in NYSE Information Memorandum 06-11 and modify the proposed exclusion.³⁶ As stated in the Proposing Release, FINRA believes that the standard set forth in Information Memorandum 06-11 is too narrow. However, in response to the comments, FINRA has revised FINRA Rule 4530.01 as follows.

With respect to violative conduct by a member, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member,

³⁵ Commonwealth, CAI, NSCP, State Farm, PFS, SIFMA and FSI.

³⁶ Commonwealth, CAI, NSCP, PFS, SIFMA and FSI.

its customers or the markets, or conduct that arises from a material failure of the member's systems, policies or practices involving numerous customers, multiple errors or significant dollar amounts. Regarding violative conduct by an associated person, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, conduct that has a significant monetary result with respect to a member(s), customer(s) or market(s), or multiple instances of any violative conduct. The revised standard is based, in part, on the standard in Information Memorandum 06-11. FINRA believes that this change provides greater clarity to firms and preserves the objectives of the proposed reporting requirement. Additionally, FINRA Rule 4530.01 continues to provide that if a firm disciplines an associated person in the manner described in FINRA Rule 4530(a)(2), the firm is required to report the event under paragraph (a)(2), rather than paragraph (b) of the proposed rule. Also, FINRA Rule 4530(e) continues to provide that a firm is not required to report an event otherwise required to be reported under FINRA Rule 4530(b) if the firm discloses the event on the Form U5, consistent with the requirements of that form.

D. Customer Complaints (Proposed FINRA Rules 4530(a)(1)(B), 4530(d) and 4530.08)

In the Proposing Release, FINRA clarified that for purposes of FINRA Rule 4530(d) a member is not required to report written complaints relating to non-securities products, but only to the extent that such complaints are not from customers that the member has engaged, or has sought to engage, in securities activities. However, if a member has engaged, or has sought to engage, in securities activities with a person, then

any written complaint from that person is reportable under the proposed rule, regardless of whether it relates to non-securities products.

One commenter believes that the clarification is problematic.³⁷ The commenter suggests that it may be difficult for a firm to determine whether it has “sought to engage” a person in securities activities. For instance, a registered representative may ask an insurance customer about mutual funds. Based on the clarification in the Proposing Release, all subsequent written complaints by the insurance customer would be reportable regardless of whether the customer engages in a securities transaction. According to the commenter, even if the clarification was limited to persons “engaged” in securities activities, it would still be concerned with the number of potential non-securities related written complaints that it would have to report.

Current NASD Rule 3070(c) defines the term “customer” to include any person, other than a broker-dealer, with whom the member has sought to engage in securities activities. Thus, firms currently must have procedures to identify whether the person submitting the written complaint is someone that the firm has sought to engage in securities activities.

FINRA also is revising the proposal to further clarify a firm’s reporting obligation regarding customer complaints. The revised proposal provides that firms are required to report under FINRA Rules 4530(a)(1)(B) and 4530(d) any written complaint from any person, other than a broker or dealer, with whom the member has engaged, or has sought to engage, in securities activities alleging theft or misappropriation of funds or securities

³⁷ State Farm.

or of forgery. In addition, for purposes of FINRA Rule 4530(d), with respect to a person, other than a broker or dealer, with whom the member “has engaged in securities activities,” the firm is required to report “any written grievance” by such person involving the member or an associated person. However, for purposes of FINRA Rule 4530(d), with respect to a person, other than a broker or dealer, with whom the member “has sought to engage in securities activities,” the firm is only required to report “any securities-related written grievance” by such person involving the member or an associated person and any written complaints reportable under FINRA Rule 4530(a)(1)(B).

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

Three commenters urge FINRA to eliminate duplicative reporting of information disclosed on the Forms BD and U4.³⁸ As noted in the Proposing Release, FINRA will work toward this goal. Additionally, as discussed in the Proposing Release, FINRA is proposing to eliminate duplicative reporting of information disclosed on the Form U5.

F. Former Associated Persons (Proposed FINRA Rule 4530.07)

Two commenters are concerned that the requirement to report information relating to former associated persons is overly burdensome.³⁹ The commenters request that FINRA set a time limit, consistent with the record retention period under the Act, with respect to how long after a representative’s termination such reporting would be required. One of these commenters asks that FINRA recast the requirement as a

³⁸ CAI, SIFMA and FSI.

³⁹ CAI and FSI.

requirement to maintain the information to the extent such information becomes known to firms, and make it available to FINRA examiners upon request.

Information relating to former associated persons is relevant to FINRA's programs since it assists FINRA in identifying firms, offices and associated persons that may pose a regulatory risk. Thus, firms are required to report this information as discussed in the Proposing Release. However, in response to the comments, FINRA has revised the proposed rule to clarify that a firm is not required to report where, based on its records, the firm cannot determine whether the person was an associated person, provided that the firm's records were preserved for the period of time and accessibility specified in SEA Rule 17a-4(e)(1), which requires firms to preserve records relating to associated persons in an easily accessible place for at least three years after the associated person's employment and any other connection with the firm has terminated.

G. Other Comments

One commenter argues that the Commission should reject the proposal because FINRA has not provided a demonstrated need for the proposal relating to internal conclusions and has not provided the Commission with sufficient information to evaluate whether the changes will advance the goals of customer protection and market integrity.⁴⁰ FINRA disagrees. As stated in the Proposing Release, FINRA believes that the proposed rule change, including FINRA Rule 4530(b) relating to internal conclusions, will enhance its ability to detect and investigate violative conduct. Further, as noted above, as part of the consolidation process, FINRA has determined that NYSE Rule 351(a)(1), which

⁴⁰ PFS.

FINRA Rule 4530(b) in large part is based on, provides a heightened standard of investor protection by requiring firms to report internal conclusions of violative conduct. Moreover, FINRA's examination programs use this information as part of their assessment processes and risk-based analyses.

One commenter argues that FINRA does not currently have the jurisdiction to require firms to report the type of information required to be reported under the proposed rule, such as matters involving violations of any insurance-, commodities-, financial- or investment-related laws, rules or regulations, matters involving foreign regulatory bodies and matters involving insurance related civil litigation or arbitration.⁴¹ The commenter also suggests that the current dollar thresholds for reporting are too low and outdated. FINRA has analyzed and addressed these issues in the Proposing Release and in this Amendment No. 1 and, therefore, FINRA is not addressing them further here.

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

As noted in Item 2 of this filing, FINRA will announce the implementation date of the proposed rule change in a Notice to be published no later than 90 days following Commission approval. The implementation date will be no later than 240 days following Commission approval.

⁴¹ FSI.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁴² which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will further the purposes of the Act by enhancing FINRA's ability to detect and investigate violative conduct.

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.

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-2010-034.⁴³ The Commission received seven comment letters,⁴⁴ which are summarized above.

6. Extension of Time Period for Commission Action

FINRA has granted an extension of the time period for Commission action until November 8, 2010.

⁴² 15 U.S.C. 78o-3(b)(6).

⁴³ See Proposing Release.

⁴⁴ See supra note 6.

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

Not applicable.

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

Not applicable.

9. **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-2010-034)

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

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “SEA”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on July 30, 2010, Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”) 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-2010-034, a proposed rule change to adopt NASD Rule 3070 (Reporting Requirements) as FINRA Rule 4530 (Reporting Requirements) in the consolidated FINRA rulebook, subject to certain amendments, and to delete paragraphs (a) through (d) of Incorporated NYSE Rule 351 (Reporting Requirements) and Incorporated NYSE Rules 351.10 and 351.13. The proposed rule change also would add a supplementary material section to proposed FINRA Rule 4530.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

The text of the proposed rule change is available on FINRA's Web site 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 July 30, 2010, FINRA filed with the SEC SR-FINRA-2010-034,³ a proposed rule change to adopt NASD Rule 3070 as FINRA Rule 4530 in the consolidated FINRA rulebook ("Consolidated FINRA Rulebook"),⁴ subject to certain amendments as

³ See Securities Exchange Act Release No. 62621 (July 30, 2010), 75 FR 47863 (August 9, 2010) (Notice of Filing of SR-FINRA-2010-034) ("Proposing Release"). The comment period closed on August 30, 2010.

⁴ 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).

described in the Proposing Release. The proposed rule change also would delete paragraphs (a) through (d) of Incorporated NYSE Rule 351⁵ and NYSE Rules 351.10 and 351.13 from the Transitional Rulebook.⁶ Further, the proposed rule change would add a supplementary material section to proposed FINRA Rule 4530 as detailed in the Proposing Release. The proposed rule change was published for comment in the Federal Register on August 9, 2010. The Commission received seven comment letters in response to the proposed rule change.⁷ Based on comments received, FINRA is filing

⁵ For convenience, the Incorporated NYSE Rules are referred to as the NYSE Rules.

⁶ NYSE Rule 351(e) and NYSE Rule Interpretation 351(e)/01 (Reports of Investigation) govern trade investigation reporting requirements. NYSE Rules 351(f), 351.11 and 351.12 govern the annual attestation requirement of the research analyst conflict of interest rules. These provisions will be addressed as part of the supervision rules and research analyst conflict of interest rules, respectively. See Regulatory Notice 08-24 (May 2008) (Proposed Consolidated FINRA Rules Governing Supervision and Supervisory Controls) and Regulatory Notice 08-55 (October 2008) (FINRA Requests Comment on Proposed Research Registration and Conflict of Interest Rules).

⁷ See Letter from Brendan Daly, Legal and Compliance Counsel, Commonwealth Financial Network, to Elizabeth M. Murphy, Secretary, SEC, dated August 27, 2010 (“Commonwealth”); Letter from Clifford Kirsch and Susan Krawczyk, Sutherland Asbill & Brennan LLP, for the Committee of Annuity Insurers, to Elizabeth M. Murphy, Secretary, SEC, dated August 30, 2010 (“CAI”); Letter from Joan Hinchman, Executive Director, President and CEO, National Society of Compliance Professionals, Inc., to Elizabeth M. Murphy, Secretary, SEC, dated August 30, 2010 (“NSCP”); Letter from Kristin Bulls, Products and Broker-Dealer Compliance Director, State Farm VP Management Corp., to Elizabeth M. Murphy, Secretary, SEC, dated August 30, 2010 (“State Farm”); Letter from Michael Lesutis, Assistant General Counsel, PFS Investments, Inc., to Elizabeth M. Murphy, Secretary, SEC, dated September 1, 2010 (“PFS”); Letter from James T. McHale, Managing Director and Associate General Counsel, the Securities Industry and Financial Markets Association, to Elizabeth M. Murphy, Secretary, SEC, dated September 1, 2010 (“SIFMA”); and Letter from Dale E. Brown, President & CEO, the Financial Services Institute, to Elizabeth M. Murphy, Secretary, SEC, dated September 15, 2010 (“FSI”). (Available at <http://www.sec.gov/comments/sr-finra-2010-034/finra2010034.shtml>.)

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

Proposal

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

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

Response to Comments

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

One commenter argues that the requirement to report external findings related to any insurance matter is unwarranted and burdensome.⁸ For instance, the proposed rule may capture findings related to an associated person's failure to timely meet insurance continuing education requirements. The commenter asks that FINRA limit the proposal to those external findings that derive from a transaction with a customer.

⁸ State Farm.

As noted in the Proposing Release, current NASD Rule 3070(a)(1) requires that a firm report whenever the firm or an associated person of the firm has been found to have violated “any” rule or standard of conduct of “any” governmental agency, self-regulatory organization (“SRO”), or financial business or professional organization. Thus, firms currently are required to report external findings related to “insurance” matters, and it is not a novel requirement. The proposed rule simply continues this requirement, which has been a part of NASD Rule 3070 since its adoption. Further, the requirement to report insurance matters is consistent with other provisions of the current rules.⁹ More importantly, this information is relevant to FINRA’s programs since it assists FINRA in identifying firms, offices and associated persons that may pose a regulatory risk.

Another commenter requests that FINRA provide additional examples of the kinds of external events that firms should report under the proposed rule.¹⁰ As stated in FINRA Rule 4530.02, FINRA Rule 4530(a)(1)(A) is limited to situations where there has been a finding of violative conduct by an external body, such as a court, domestic or foreign regulatory body, SRO or business or professional organization. For example,

⁹ See NASD Rule 3070(a)(3) and NYSE Rule 351(a)(3) (requiring reporting where a firm or an associated person is named as a defendant or respondent in any proceeding brought by a regulatory or self-regulatory body alleging the violation of any insurance laws, rules or regulations); NASD Rule 3070(a)(4) and NYSE Rule 351(a)(4) (requiring reporting where a firm or an associated is disciplined by any insurance regulatory or self-regulatory body, is denied membership or continued membership in any such self-regulatory body, or is barred from becoming associated with any member of any such self-regulatory body); and NASD Rule 3070(a)(6) and NYSE Rule 351(a)(6) (requiring reporting where a firm or an associated person is a director, controlling stockholder, partner, officer, sole proprietor, or an associated person of an insurance company that was suspended, expelled or had its registration denied or revoked).

¹⁰ NSCP.

consistent with the requirements of current NASD Rule 3070(a)(1), firms will continue to be required to report a court finding relating to the violation of insurance laws.

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

As discussed in the Proposing Release, the proposed rule requires the reporting of any “insurance” civil litigation or arbitration that is “financial related.”

Three commenters believe that the phrase “financial related” needs additional clarification.¹¹ In response, FINRA has added FINRA Rule 4530.09 to the proposal defining the term “financial related” to mean related to the provision of financial services. Two of these commenters also suggest that the requirement to report insurance matters stemming from civil litigation or arbitration be limited to insurance products that are securities.¹² The proposed rule excludes certain insurance products, such as traditional auto and health insurance. However, FINRA does not believe that the proposed rule should be limited to insurance products that are securities. Civil litigation or arbitration involving non-securities insurance products that is related to the provision of financial services will be subject to the proposed rule.

The proposed rule also requires the reporting of any claim for damages by a customer or broker-dealer that is “financial” or “transactional” in nature. As noted in the Proposing Release, FINRA believes that transactional claims by customers, including contractual disputes, are relevant to its programs since they may reveal misconduct, such as an impermissible customer loan.

¹¹ CAI, NSCP and State Farm.

¹² CAI and NSCP.

One commenter argues that the example offered (i.e., such information may reveal an impermissible customer loan) relates to a transaction that may be within the province of another regulator to address and not necessarily relevant to FINRA.¹³ The commenter suggests that the proposed rule exclude matters that do not involve securities activities. FINRA disagrees. Moreover, the example offered in the Proposing Release relates directly to a FINRA rule, FINRA Rule 3240 (Borrowing From or Lending to Customers).

Another commenter believes that the provision requires further clarification since nearly all insurance related claims, including traditional auto and health insurance, ultimately are transactional (contractual) in nature.¹⁴ In response to this comment, FINRA has revised the proposed rule to require the reporting of any claim for damages by a customer or broker-dealer that relates to the provision of financial services or relates to a financial transaction.

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

As discussed in the Proposing Release, FINRA Rule 4530(b) generally incorporates the requirement under NYSE Rule 351(a)(1) and provides that a firm is required to report to FINRA no later than 30 calendar days after the firm has concluded, or reasonably should have concluded, on its own that an associated person of the firm or the firm itself has engaged in violations of any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or SRO.

¹³ NSCP.

¹⁴ State Farm.

Two commenters believe that the requirement should be eliminated.¹⁵ One of these commenters argues that the proposal runs counter to the concept of voluntary self-reporting and credit for cooperation and to the implementation of robust compliance programs intended to identify and fix problems.¹⁶ Two commenters are concerned that the proposal will increase the administrative burden on firms.¹⁷ One of these commenters argues that FINRA has not described what matters firms are failing to disclose and whether existing practices have caused any impediments to identifying and addressing misconduct by firms or associated persons.¹⁸

One of the main purposes of the consolidation process is to consider both sets of rules, NASD and NYSE, and determine the appropriate investor protection standard to be included in the FINRA Rules. FINRA recognizes that NYSE Rule 351(a)(1) provides a heightened standard of investor protection by requiring firms to report internal conclusions of violative conduct. Moreover, FINRA's examination programs use this information as part of their assessment processes and risk-based analyses.

One commenter argues that compliance decisions are based on whether there has been a failure to comply with policies and procedures, which may not necessarily align with a specific regulatory violation, and that the proposal would require firms to further analyze every compliance issue to determine whether there also has been a reportable

¹⁵ CAI and State Farm.

¹⁶ CAI.

¹⁷ Commonwealth and NSCP.

¹⁸ NSCP.

regulatory violation.¹⁹ In response, FINRA notes that a firm's policies and procedures are informed by applicable laws, rules and regulations. For instance, NASD Rule 3010 (Supervision) requires firms to establish, maintain and enforce written supervisory procedures that are reasonably designed to achieve compliance with applicable securities laws, rules and regulations. Further, in evaluating the nature and gravity of noncompliant conduct, firms would have to assess the extent to which applicable laws, rules and regulations have been violated.

Two commenters argue that the term "concluded" is vague.²⁰ One of these commenters states that case-specific conclusions are routinely made in a number of departments.²¹ The other commenter suggests that the proposal does not indicate who within a firm must have "concluded" that a violation occurred before it becomes reportable.²² A firm is free to determine the person(s) within the firm responsible for making such determinations. As explained in the Proposing Release, a firm is free to determine the level of seniority required of an associated person in making a determination of a reportable internal conclusion; however, it will not be a defense to a failure to report such conduct that it was of a nature that did not merit consideration by a person of such seniority. Additionally, it may be possible that a department within a firm reaches a conclusion of violation, but on review, senior management reaches a different conclusion. Nothing in the proposed rule would prohibit a firm from relying on senior

¹⁹ CAI.

²⁰ NSCP and State Farm.

²¹ State Farm.

²² NSCP.

management's determination, provided such determination is reasonable as explained below.

Several commenters are concerned with the “reasonably should have concluded” standard.²³ Two of these commenters argue that FINRA did not explain why it was adding this standard.²⁴ Two commenters state that the “reasonably should have concluded” standard would create uncertainty and should be eliminated.²⁵ Another commenter believes that the standard is flawed since it is far too subjective and would be subject to inconsistent application by firms and FINRA.²⁶ One commenter believes that FINRA staff may use the standard to penalize firms when they have acted in good faith based on information available at the time in evaluating a compliance issue, but failed to anticipate how an issue might ultimately develop.²⁷ Two commenters believe that the standard could be used on a hindsight basis for FINRA to pursue actions if it concludes after the fact that a firm should have self reported.²⁸ Three commenters argue that the standard places a firm in the precarious position in which inherently subjective assessments will be susceptible to second guessing.²⁹ One of these commenters also argues that the requirement to report within 30 calendar days of the date on which the

²³ CAI, NSCP, PFS, SIFMA and FSI.

²⁴ CAI and NSCP.

²⁵ CAI and FSI.

²⁶ SIFMA.

²⁷ CAI.

²⁸ NSCP and SIFMA.

²⁹ CAI, PFS and FSI.

firm “reasonably should have concluded” that a violation occurred may increase the threat of FINRA enforcement actions.³⁰ According to the commenter, a firm might take 60 calendar days to reach a conclusion and report the finding, only to have FINRA decide later that the conclusion should have been reached sooner.

As noted in the Proposing Release, the “knows or should have known” standard, which is applicable to other provisions of FINRA Rule 4530, does not fit in the context of internal findings. Rather, the standard applicable to a firm’s internal conclusion of violation is the “has concluded or reasonably should have concluded” standard. However, the “reasonably should have concluded” standard cannot be read in a vacuum. If a firm has made a good faith reasonable determination, it is not enough for FINRA to simply engage in second guessing. If a reasonable person would have concluded that a violation occurred, then the matter is reportable. Conversely, if a reasonable person would not have concluded that a violation occurred, then the matter is not reportable.

Two commenters argue that the requirement to report insurance matters should be eliminated.³¹ One of these commenters asks whether FINRA will take action if the internal conclusion relates to a violation of insurance laws.³² The commenter also asks if a firm has an obligation to report if the determination regarding the violation of insurance laws is made by the firm’s insurance affiliate and involves the firm. As noted above, information relating to insurance matters is relevant to FINRA’s programs since it assists FINRA in identifying firms, offices and associated persons that may pose a regulatory

³⁰ PFS.

³¹ CAI and NSCP.

³² CAI.

risk. With respect to a determination by an affiliate of a firm, the firm should report it absent a reasonable rejection of such a determination.

Several commenters are concerned with the statement in the Proposing Release that an internal audit finding creates a strong presumption that the matter is reportable.³³ The commenters argue that the “strong presumption” language has the potential to undermine the internal audit process. Some commenters suggest that matters subject to a firm’s internal review process as required under other rules (e.g., FINRA Rule 3130 (Annual Certification of Compliance and Supervisory Processes)) should be excluded from the proposed requirement.³⁴ Three of these commenters note that when the rules regarding internal review processes were adopted, FINRA staff assured firms that FINRA would not use the reports and review processes under those rules as a roadmap for disciplinary action against a firm or a registered person and that firms would be given latitude to resolve uncovered deficiencies resulting from their reviews.³⁵

The reporting obligation under the proposed rule and the internal review processes set forth under other rules (e.g., FINRA Rule 3130) are mutually exclusive. While internal review processes may inform a firm’s determination that a specific violation occurred, they do not by themselves lead to the conclusion that the matter is reportable for purposes of the proposed rule. For example, FINRA would not view a discussion in an internal audit report regarding the need for enhanced controls in a particular area, standing alone, as determinative of a reportable violation for purposes of

³³ Commonwealth, NSCP and SIFMA.

³⁴ Commonwealth, CAI, NSCP, SIFMA and FSI.

³⁵ Commonwealth, CAI and FSI.

the proposed rule. FINRA also wishes to clarify that, rather than creating a strong presumption, an internal audit finding would serve only as one factor, among others, that a firm should consider in determining whether a violation occurred.

Additionally, as set forth in the Proposing Release, FINRA Rule 4530.01 excluded from the reporting requirement an isolated violation by the firm or an associated person of the firm that could be reasonably viewed as a ministerial violation of the applicable rules that did not result in customer harm and was remedied promptly upon discovery. FINRA also provided an example in the Proposing Release of the types of reportable and non-reportable matters.

All of the commenters state that the proposed exclusion is too narrow and that the example provided in the Proposing Release does not provide sufficient clarity.³⁶ Some of these commenters ask that FINRA reevaluate the standard set forth in NYSE Information Memorandum 06-11 and modify the proposed exclusion.³⁷ As stated in the Proposing Release, FINRA believes that the standard set forth in Information Memorandum 06-11 is too narrow. However, in response to the comments, FINRA has revised FINRA Rule 4530.01 as follows.

With respect to violative conduct by a member, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, or conduct that arises from a material failure of the member's systems, policies or practices involving numerous customers, multiple errors or significant dollar amounts. Regarding violative conduct by an associated person, FINRA

³⁶ Commonwealth, CAI, NSCP, State Farm, PFS, SIFMA and FSI.

³⁷ Commonwealth, CAI, NSCP, PFS, SIFMA and FSI.

expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, conduct that has a significant monetary result with respect to a member(s), customer(s) or market(s), or multiple instances of any violative conduct. The revised standard is based, in part, on the standard in Information Memorandum 06-11. FINRA believes that this change provides greater clarity to firms and preserves the objectives of the proposed reporting requirement. Additionally, FINRA Rule 4530.01 continues to provide that if a firm disciplines an associated person in the manner described in FINRA Rule 4530(a)(2), the firm is required to report the event under paragraph (a)(2), rather than paragraph (b) of the proposed rule. Also, FINRA Rule 4530(e) continues to provide that a firm is not required to report an event otherwise required to be reported under FINRA Rule 4530(b) if the firm discloses the event on the Form U5, consistent with the requirements of that form.

D. Customer Complaints (Proposed FINRA Rules 4530(a)(1)(B), 4530(d) and 4530.08)

In the Proposing Release, FINRA clarified that for purposes of FINRA Rule 4530(d) a member is not required to report written complaints relating to non-securities products, but only to the extent that such complaints are not from customers that the member has engaged, or has sought to engage, in securities activities. However, if a member has engaged, or has sought to engage, in securities activities with a person, then any written complaint from that person is reportable under the proposed rule, regardless of whether it relates to non-securities products.

One commenter believes that the clarification is problematic.³⁸ The commenter suggests that it may be difficult for a firm to determine whether it has “sought to engage” a person in securities activities. For instance, a registered representative may ask an insurance customer about mutual funds. Based on the clarification in the Proposing Release, all subsequent written complaints by the insurance customer would be reportable regardless of whether the customer engages in a securities transaction. According to the commenter, even if the clarification was limited to persons “engaged” in securities activities, it would still be concerned with the number of potential non-securities related written complaints that it would have to report.

Current NASD Rule 3070(c) defines the term “customer” to include any person, other than a broker-dealer, with whom the member has sought to engage in securities activities. Thus, firms currently must have procedures to identify whether the person submitting the written complaint is someone that the firm has sought to engage in securities activities.

FINRA also is revising the proposal to further clarify a firm’s reporting obligation regarding customer complaints. The revised proposal provides that firms are required to report under FINRA Rules 4530(a)(1)(B) and 4530(d) any written complaint from any person, other than a broker or dealer, with whom the member has engaged, or has sought to engage, in securities activities alleging theft or misappropriation of funds or securities or of forgery. In addition, for purposes of FINRA Rule 4530(d), with respect to a person, other than a broker or dealer, with whom the member “has engaged in securities activities,” the firm is required to report “any written grievance” by such person

³⁸ State Farm.

involving the member or an associated person. However, for purposes of FINRA Rule 4530(d), with respect to a person, other than a broker or dealer, with whom the member “has sought to engage in securities activities,” the firm is only required to report “any securities-related written grievance” by such person involving the member or an associated person and any written complaints reportable under FINRA Rule 4530(a)(1)(B).

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

Three commenters urge FINRA to eliminate duplicative reporting of information disclosed on the Forms BD and U4.³⁹ As noted in the Proposing Release, FINRA will work toward this goal. Additionally, as discussed in the Proposing Release, FINRA is proposing to eliminate duplicative reporting of information disclosed on the Form U5.

F. Former Associated Persons (Proposed FINRA Rule 4530.07)

Two commenters are concerned that the requirement to report information relating to former associated persons is overly burdensome.⁴⁰ The commenters request that FINRA set a time limit, consistent with the record retention period under the Act, with respect to how long after a representative’s termination such reporting would be required. One of these commenters asks that FINRA recast the requirement as a requirement to maintain the information to the extent such information becomes known to firms, and make it available to FINRA examiners upon request.

Information relating to former associated persons is relevant to FINRA’s programs since it assists FINRA in identifying firms, offices and associated persons that

³⁹ CAI, SIFMA and FSI.

⁴⁰ CAI and FSI.

may pose a regulatory risk. Thus, firms are required to report this information as discussed in the Proposing Release. However, in response to the comments, FINRA has revised the proposed rule to clarify that a firm is not required to report where, based on its records, the firm cannot determine whether the person was an associated person, provided that the firm's records were preserved for the period of time and accessibility specified in SEA Rule 17a-4(e)(1), which requires firms to preserve records relating to associated persons in an easily accessible place for at least three years after the associated person's employment and any other connection with the firm has terminated.

G. Other Comments

One commenter argues that the Commission should reject the proposal because FINRA has not provided a demonstrated need for the proposal relating to internal conclusions and has not provided the Commission with sufficient information to evaluate whether the changes will advance the goals of customer protection and market integrity.⁴¹ FINRA disagrees. As stated in the Proposing Release, FINRA believes that the proposed rule change, including FINRA Rule 4530(b) relating to internal conclusions, will enhance its ability to detect and investigate violative conduct. Further, as noted above, as part of the consolidation process, FINRA has determined that NYSE Rule 351(a)(1), which FINRA Rule 4530(b) in large part is based on, provides a heightened standard of investor protection by requiring firms to report internal conclusions of violative conduct. Moreover, FINRA's examination programs use this information as part of their assessment processes and risk-based analyses.

⁴¹ PFS.

One commenter argues that FINRA does not currently have the jurisdiction to require firms to report the type of information required to be reported under the proposed rule, such as matters involving violations of any insurance-, commodities-, financial- or investment-related laws, rules or regulations, matters involving foreign regulatory bodies and matters involving insurance related civil litigation or arbitration.⁴² The commenter also suggests that the current dollar thresholds for reporting are too low and outdated. FINRA has analyzed and addressed these issues in the Proposing Release and in this Amendment No. 1 and, therefore, FINRA is not addressing them further here.

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

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

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁴³ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will further the purposes of the Act by enhancing FINRA's ability to detect and investigate violative conduct.

⁴² FSI.

⁴³ 15 U.S.C. 78q-3(b)(6).

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

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

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

Written comments on the proposed rule change were solicited by the Commission in response to the publication of SR-FINRA-2010-034.⁴⁴ The Commission received seven comment letters,⁴⁵ which are summarized above.

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

Within 35 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 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:

⁴⁴ See Proposing Release.

⁴⁵ See supra note 7.

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2010-034 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2010-034. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 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-2010-034 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

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

Florence E. Harmon

Deputy Secretary

⁴⁶ 17 CFR 200.30-3(a)(12).

EXHIBIT 4

Exhibit 4 shows the changes proposed in this Amendment No. 1 only as to proposed FINRA Rule 4530, 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.

* * * * *

4530. Reporting Requirements

(a) Each member shall promptly report to FINRA, but in any event not later than 30 calendar days, after the member knows or should have known of the existence of any of the following:

(1) the member or an associated person of the member:

(A) has been found to have violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body, self-regulatory organization or business or professional organization;

(B) is the subject of any written customer complaint involving allegations of theft or misappropriation of funds or securities or of forgery;

(C) is named as a defendant or respondent in any proceeding brought by a domestic or foreign regulatory body or self-regulatory organization alleging the violation of any provision of the Exchange Act, or of any other federal, state or foreign securities, insurance or commodities statute, or of any rule or regulation thereunder, or of any provision of the by-laws, rules or similar governing instruments of any securities, insurance or commodities domestic or foreign regulatory body or self-regulatory organization;

(D) is denied registration or is expelled, enjoined, directed to cease and desist, suspended or otherwise disciplined by any securities, insurance or commodities industry domestic or foreign regulatory body or self-regulatory organization or is denied membership or continued membership in any such self-regulatory organization; or is barred from becoming associated with any member of any such self-regulatory organization;

(E) is indicted, or convicted of, or pleads guilty to, or pleads no contest to, any felony; or any misdemeanor that involves the purchase or sale of any security, the taking of a false oath, the making of a false report, bribery, perjury, burglary, larceny, theft, robbery, extortion, forgery, counterfeiting, fraudulent concealment, embezzlement, fraudulent conversion, or misappropriation of funds, or securities, or a conspiracy to commit any of these offenses, or substantially equivalent activity in a domestic, military or foreign court;

(F) is a director, controlling stockholder, partner, officer or sole proprietor of, or an associated person with, a broker, dealer, investment company, investment advisor, underwriter or insurance company that was suspended, expelled or had its registration denied or revoked by any domestic or foreign regulatory body, jurisdiction or organization or is associated in such a capacity with a bank, trust company or other financial institution that was convicted of or pleaded no contest to, any felony or misdemeanor in a domestic or foreign court;

(G) is a defendant or respondent in any securities- or commodities-related civil litigation or arbitration, is a defendant or respondent in any financial-related insurance civil litigation or arbitration, or is the subject of any claim for damages by a customer, broker or dealer that relates to the provision of [is] financial services or relates to a financial transaction[al in nature], and such civil litigation, arbitration or claim for damages has been disposed of by judgment, award or settlement for an amount exceeding \$15,000. However, when the member is the defendant or respondent or is the subject of any claim for damages by a customer, broker or dealer, then the reporting to FINRA shall be required only when such judgment, award or settlement is for an amount exceeding \$25,000; or

(H) is, or is involved in the sale of any financial instrument, the provision of any investment advice or the financing of any such activities with any person who is, subject to a “statutory disqualification” as that term is defined in the Exchange Act. The report shall include the name of the person subject to the statutory disqualification and details concerning the disqualification; or

(2) an associated person of the member is the subject of any disciplinary action taken by the member involving suspension, termination, the withholding of compensation or of any other remuneration in excess of \$2,500, the imposition of fines in excess of \$2,500 or is otherwise disciplined in any manner that would

have a significant limitation on the individual's activities on a temporary or permanent basis.

(b) Each member shall promptly report to FINRA, but in any event not later than 30 calendar days, after the member has concluded or reasonably should have concluded that an associated person of the member or the member itself has violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or self-regulatory organization.

(c) Each person associated with a member shall promptly report to the member the existence of any of the events set forth in paragraph (a)(1) of this Rule.

(d) Each member shall report to FINRA statistical and summary information regarding written customer complaints in such detail as FINRA shall specify by the 15th day of the month following the calendar quarter in which customer complaints are received by the member. [For the purposes of this paragraph, "customer" includes any person other than a broker or dealer with whom the member has engaged, or has sought to engage, in securities activities, and "complaint" includes any written grievance by a customer involving the member or person associated with the member.]

(e) Nothing contained in this Rule shall eliminate, reduce or otherwise abrogate the responsibilities of a member or person associated with a member to promptly disclose required information on the Forms BD, U4 or U5, as applicable, to make any other required filings or to respond to FINRA with respect to any customer complaint, examination or inquiry. In addition, members are required to comply with the reporting obligations under paragraphs (a), (b) and (d) of this Rule, regardless of whether the

information is reported or disclosed pursuant to any other rule or requirement, including the requirements of the Forms BD or U4. However, a member need not report an event otherwise required to be reported under paragraphs (a) or (b) of this Rule if the member discloses the event on the Form U5, consistent with the requirements of that form.

(f) Each member shall promptly file with FINRA copies of:

(1) any indictment, information or other criminal complaint or plea agreement for conduct reportable under paragraph (a)(1)(E) of this Rule;

(2) any complaint in which a member is named as a defendant or respondent in any securities- or commodities-related private civil litigation, or is named as a defendant or respondent in any financial-related insurance private civil litigation;

(3) any securities- or commodities-related arbitration claim, or financial-related insurance arbitration claim, filed against a member in any forum other than the FINRA Dispute Resolution forum;

(4) any indictment, information or other criminal complaint, any plea agreement, or any private civil complaint or arbitration claim against a person associated with a member that is reportable under question 14 on Form U4, irrespective of any dollar thresholds Form U4 imposes for notification, unless, in the case of an arbitration claim, the claim has been filed in the FINRA Dispute Resolution forum.

(g) Members shall not be required to comply separately with paragraph (f) in the event that any of the documents required by paragraph (f) have been the subject of a request by FINRA's Registration and Disclosure staff, provided that the member

produces those requested documents to the Registration and Disclosure staff not later than 30 days after receipt of such request. This paragraph does not supersede any FINRA rule or policy that requires production of documents specified in paragraph (f) sooner than 30 days after receipt of a request by the Registration and Disclosure staff.

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

.01 Reporting of Firms' Conclusions of Violations. For purposes of paragraph (b) of this Rule, with respect to violative conduct by a member, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, or conduct that arises from a material failure of the member's systems, policies or practices involving numerous customers, multiple errors or significant dollar amounts. With respect to violative conduct by an associated person, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, conduct that has a significant monetary result with respect to a member(s), customer(s) or market(s), or multiple instances of any violative conduct. In addition, with respect to violative conduct by an associated person, the reporting obligation under paragraph (b) must be read in conjunction with the reporting obligation under paragraph (a)(2) of this Rule. If a member has concluded that an associated person has engaged in violative conduct and imposes the discipline set forth under paragraph (a)(2) of this Rule, then the member is required to report the event under paragraph (a)(2), and it need not report the event under paragraph (b). [In addition, for purposes of paragraph (b) of this Rule, FINRA does not expect a member to report an isolated violation by the member or an associated person of

the member that can be reasonably viewed as a ministerial violation of the applicable rules that did not result in customer harm and was remedied promptly upon discovery.]

.02 Firms' Conclusions of Violations versus External Findings. Members should be aware that paragraph (b) of this Rule is limited to situations where the member has concluded or reasonably should have concluded on its own that violative conduct has occurred. Paragraph (a)(1)(A) of this Rule is limited to situations where there has been a finding of violative conduct by an external body, such as a court, domestic or foreign regulatory body, self-regulatory organization or business or professional organization.

.03 Meaning of "Found." The term "found" as used in paragraph (a)(1)(A) of this Rule includes among other formal findings, adverse final actions, including consent decrees in which the respondent has neither admitted nor denied the findings, but does not include informal agreements, deficiency letters, examination reports, memoranda of understanding, cautionary actions, admonishments and similar informal resolutions of matters. For example, a Letter of Acceptance, Waiver and Consent or an Offer of Settlement is considered an adverse final action. The term "found" also includes any formal finding, regardless of whether the finding will be appealed. The term "found" does not include a violation of a self-regulatory organization rule that has been designated as "minor" pursuant to a plan approved by the SEC, if the sanction imposed consists of a fine of \$2,500 or less, and if the sanctioned person does not contest the fine.

.04 Meaning of "Regulatory Body." For [the] purposes of this Rule, the term "regulatory body" refers to governmental regulatory bodies and authorized non-governmental regulatory bodies, such as the Financial Services Authority.

.05 Reporting of Individual and Related Events. With respect to a reportable event under paragraphs (a) or (b) of this Rule, members should not report the same event under more than one paragraph or subparagraph. Members should report the event under the most appropriate paragraph or subparagraph. However, members should be aware that they may be required to report related events under more than one paragraph or subparagraph. For instance, if a member is named as a respondent in a proceeding brought by a self-regulatory organization alleging the violation of the self-regulatory organization's rules, the member would be required to report that event under paragraph (a)(1)(C) of this Rule. In addition, if the member subsequently is found to have violated the self-regulatory organization's rules, the member would be required to report that finding under paragraph (a)(1)(A) of this Rule.

.06 Calculation of Monetary Thresholds. For purposes of paragraph (a)(1)(G) of this Rule, when determining the dollar amount that would require a report, members must include any attorneys fees and interest in the total amount. In addition if the parties are subject to "joint and several" liability, the amount for each party must be aggregated and reported, if above the dollar thresholds under paragraph (a)(1)(G), as if each party is separately liable for the aggregated amount. For instance, if two parties have "joint and several" liability for \$40,000, the amount reported would be \$40,000 for each party.

.07 Former Associated Persons. For purposes of paragraphs (a), (b) and (d) of this Rule, members should report an event relating to a former associated person if the event occurred while the individual was associated with the member. A member is not required to report such an event where, based on its records, the member cannot determine that the

person was an associated person of the member, provided that the member's records were preserved for the period of time and accessibility specified in SEA Rule 17a-4(e)(1).

.08 Customer Complaints. For purposes of paragraph (a)(1)(B) of this Rule, a "customer" includes any person, other than a broker or dealer, with whom the member has engaged, or has sought to engage, in securities activities. Any written customer complaint reported under paragraph (a)(1)(B) of this Rule also must be reported pursuant to paragraph (d) of this Rule. For purposes of paragraph (d) of this Rule, with respect to a person, other than a broker or dealer, with whom the member has engaged in securities activities, the member must report any written grievance by such person involving the member or a person associated with the member. In addition, with respect to a person, other than a broker or dealer, with whom the member has sought to engage in securities activities, the member must report any securities-related written grievance by such person involving the member or a person associated with the member and any written complaint reportable under paragraph (a)(1)(B) of this Rule.

.09 Financial Related. For purposes of this Rule, the term "financial related" means related to the provision of financial services.

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EXHIBIT 5

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

* * * * *

**Text of Proposed New FINRA Rule
(Marked to Show Changes from NASD Rule 3070; NASD Rule 3070 to be Deleted in
its Entirety from the Transitional Rulebook)**

* * * * *

4500. BOOKS, RECORDS AND REPORTS

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[3070]4530. Reporting Requirements

(a) Each member shall promptly report to FINRA, [the Association whenever such member or person associated with the member] but in any event not later than 30 calendar days, after the member knows or should have known of the existence of any of the following:

(1) the member or an associated person of the member:

(A) has been found to have violated any securities-, insurance-, commodities-, financial- or investment-related [provision of any securities] laws, rules, [or] regulations[, any rule] or standards of conduct of any domestic or foreign [governmental agency,] regulatory body, self-regulatory organization[,] or [financial] business or professional organization[, or engaged in conduct which is inconsistent with just and equitable principles of trade; and the member knows or should have known that any of the aforementioned events have occurred];

[(2)] (B) is the subject of any written customer complaint involving allegations of theft or misappropriation of funds or securities or of forgery;

[(3)] (C) is named as a defendant or respondent in any proceeding brought by a domestic or foreign regulatory body or self-regulatory [body] organization alleging the violation of any provision of the Exchange Act, or of any other federal, [or] state or foreign securities, insurance[,] or commodities statute, or of any rule or regulation thereunder, or of any provision of the [B]by-laws, rules or similar governing instruments of any securities, insurance or commodities domestic or foreign regulatory body or self-regulatory organization;

[(4)] (D) is denied registration or is expelled, enjoined, directed to cease and desist, suspended or otherwise disciplined by any securities, insurance or commodities industry domestic or foreign regulatory body or self-regulatory organization or is denied membership or continued membership in any such self-regulatory organization; or is barred from becoming associated with any member of any such self-regulatory organization;

[(5)] (E) is indicted, or convicted of, or pleads guilty to, or pleads no contest to, any felony; or any misdemeanor that involves the purchase or sale of any security, the taking of a false oath, the making of a false report, bribery, perjury, burglary, larceny, theft, robbery, extortion, forgery, counterfeiting, fraudulent concealment, embezzlement, fraudulent conversion, or misappropriation of funds, or securities, or a conspiracy to

commit any of these offenses, or substantially equivalent activity in a domestic, military[,] or foreign court;

[(6)] (F) is a director, controlling stockholder, partner, officer or sole proprietor of, or an associated person with, a broker, dealer, investment company, investment advisor, underwriter or insurance company [which] that was suspended, expelled or had its registration denied or revoked by any domestic or foreign [agency] regulatory body, jurisdiction or organization or is associated in such a capacity with a bank, trust company or other financial institution [which] that was convicted of or pleaded no contest to, any felony or misdemeanor in a domestic or foreign court;

[(7)] (G) is a defendant or respondent in any securities- or commodities-related civil litigation or arbitration, is a defendant or respondent in any financial-related insurance civil litigation or arbitration, or is the subject of any claim for damages by a customer, broker or dealer that relates to the provision of financial services or relates to a financial transaction, [which] and such civil litigation, arbitration or claim for damages has been disposed of by judgment, award or settlement for an amount exceeding \$15,000. However, when the member is the defendant or respondent or is the subject of any claim for damages by a customer, broker or dealer, then the reporting to [the Association] FINRA shall be required only when such judgment, award[,] or settlement is for an amount exceeding \$25,000; or

[(8) is the subject of any claim for damages by a customer, broker, or dealer which is settled for an amount exceeding \$15,000. However, when the claim for damages is against a member, then the reporting to the Association shall be required only when such claim is settled for an amount exceeding \$25,000;]

[(9) (H) is, or is involved [associated] in the sale of any [business or] financial [activity] instrument, the provision of any investment advice or the financing of any such activities with any person who is, subject to a “statutory disqualification” as that term is defined in the Exchange Act[, and the member knows or should have known of the association]. The report shall include the name of the person subject to the statutory disqualification and details concerning the disqualification; or

[(10) (2) an associated person of the member is the subject of any disciplinary action taken by the member [against any person associated with the member] involving suspension, termination, the withholding of [commissions] compensation or of any other remuneration in excess of \$2,500, [or] the imposition of fines in excess of \$2,500[,] or is otherwise disciplined in any manner [which] that would have a significant limitation on the individual’s activities on a temporary or permanent basis.

(b) Each member shall promptly report to FINRA, but in any event not later than 30 calendar days, after the member has concluded or reasonably should have concluded that an associated person of the member or the member itself has violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or

standards of conduct of any domestic or foreign regulatory body or self-regulatory organization.

[(b)] (c) Each person associated with a member shall promptly report to the member the existence of any of the [conditions] events set forth in paragraph (a)(1) of this Rule. [Each member shall report to the Association not later than 10 business days after the member knows or should have known of the existence of any of the conditions set forth in paragraph (a) of this rule.]

[(c)] (d) Each member shall report to [the Association] FINRA statistical and summary information regarding written customer complaints in such detail as [the Association] FINRA shall specify by the 15th day of the month following the calendar quarter in which customer complaints are received by the member. [For the purposes of this paragraph, “customer” includes any person other than a broker or dealer with whom the member has engaged, or has sought to engage, in securities activities, and “complaint” includes any written grievance by a customer involving the member or person associated with a member.]

[(d)] (e) Nothing contained in this Rule shall eliminate, reduce[,] or otherwise abrogate the responsibilities of a member or person associated with a member to promptly [file with full disclosure,] disclose required [amendments to] information on the Forms BD, [Forms] U[-]4 [and] or U[-]5, as applicable, [or] to make any other required filings[, and] or to respond to [NASD] FINRA with respect to any customer complaint, examination[,] or inquiry. In addition, members are required to comply with the reporting obligations under paragraphs (a), (b) and (d) of this Rule, regardless of whether the information is reported or disclosed pursuant to any other rule or requirement, including

the requirements of the Forms BD or U4. However, a member need not report an event otherwise required to be reported under paragraphs (a) or (b) of this Rule if the member discloses the event on the Form U5, consistent with the requirements of that form.

[(e) Any member subject to substantially similar reporting requirements of another self-regulatory organization of which it is a member is exempt from paragraphs (a), (b) and (c) of this Rule.]

(f) Each member shall promptly file with [NASD] FINRA copies of:

(1) any indictment, information or other criminal complaint or plea agreement for conduct reportable under paragraph (a)[(5)](1)(E) of this Rule;

(2) any complaint in which a member is named as a defendant or respondent in any securities- or commodities-related private civil litigation, or is named as a defendant or respondent in any financial-related insurance private civil litigation;

(3) any securities- or commodities-related arbitration claim, or financial-related insurance arbitration claim, filed against a member in any forum other than the [NASD] FINRA Dispute Resolution forum;

(4) any indictment, information or other criminal complaint, any plea agreement, or any private civil complaint or arbitration claim against a person associated with a member that is reportable under question 14 on Form U[-]4, irrespective of any dollar thresholds Form U[-]4 imposes for notification, unless, in the case of an arbitration claim, the claim has been filed in the [NASD] FINRA Dispute Resolution forum.

(g) Members shall not be required to comply separately with paragraph (f) in the event that any of the documents required by paragraph (f) have been the subject of a request by [NASD] FINRA's Registration and Disclosure staff, provided that the member produces those requested documents to the Registration and Disclosure staff not later than 30 days after receipt of such request. This paragraph does not supersede any [NASD] FINRA rule or policy that requires production of documents specified in paragraph (f) sooner than 30 days after receipt of a request by the Registration and Disclosure staff.

• • • Supplementary Material: -----

.01 Reporting of Firms' Conclusions of Violations. For purposes of paragraph (b) of this Rule, with respect to violative conduct by a member, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, or conduct that arises from a material failure of the member's systems, policies or practices involving numerous customers, multiple errors or significant dollar amounts. With respect to violative conduct by an associated person, FINRA expects a member to report only conduct that has widespread or potential widespread impact to the member, its customers or the markets, conduct that has a significant monetary result with respect to a member(s), customer(s) or market(s), or multiple instances of any violative conduct. In addition, with respect to violative conduct by an associated person, the reporting obligation under paragraph (b) must be read in conjunction with the reporting obligation under paragraph (a)(2) of this Rule. If a member has concluded that an associated person has engaged in violative conduct and imposes the discipline set forth under paragraph (a)(2) of this Rule, then the member is

required to report the event under paragraph (a)(2), and it need not report the event under paragraph (b).

.02 Firms' Conclusions of Violations versus External Findings. Members should be aware that paragraph (b) of this Rule is limited to situations where the member has concluded or reasonably should have concluded on its own that violative conduct has occurred. Paragraph (a)(1)(A) of this Rule is limited to situations where there has been a finding of violative conduct by an external body, such as a court, domestic or foreign regulatory body, self-regulatory organization or business or professional organization.

.03 Meaning of "Found." The term "found" as used in paragraph (a)(1)(A) of this Rule includes among other formal findings, adverse final actions, including consent decrees in which the respondent has neither admitted nor denied the findings, but does not include informal agreements, deficiency letters, examination reports, memoranda of understanding, cautionary actions, admonishments and similar informal resolutions of matters. For example, a Letter of Acceptance, Waiver and Consent or an Offer of Settlement is considered an adverse final action. The term "found" also includes any formal finding, regardless of whether the finding will be appealed. The term "found" does not include a violation of a self-regulatory organization rule that has been designated as "minor" pursuant to a plan approved by the SEC, if the sanction imposed consists of a fine of \$2,500 or less, and if the sanctioned person does not contest the fine.

.04 Meaning of "Regulatory Body." For purposes of this Rule, the term "regulatory body" refers to governmental regulatory bodies and authorized non-governmental regulatory bodies, such as the Financial Services Authority.

.05 Reporting of Individual and Related Events. With respect to a reportable event under paragraphs (a) or (b) of this Rule, members should not report the same event under more than one paragraph or subparagraph. Members should report the event under the most appropriate paragraph or subparagraph. However, members should be aware that they may be required to report related events under more than one paragraph or subparagraph. For instance, if a member is named as a respondent in a proceeding brought by a self-regulatory organization alleging the violation of the self-regulatory organization's rules, the member would be required to report that event under paragraph (a)(1)(C) of this Rule. In addition, if the member subsequently is found to have violated the self-regulatory organization's rules, the member would be required to report that finding under paragraph (a)(1)(A) of this Rule.

.06 Calculation of Monetary Thresholds. For purposes of paragraph (a)(1)(G) of this Rule, when determining the dollar amount that would require a report, members must include any attorneys fees and interest in the total amount. In addition if the parties are subject to "joint and several" liability, the amount for each party must be aggregated and reported, if above the dollar thresholds under paragraph (a)(1)(G), as if each party is separately liable for the aggregated amount. For instance, if two parties have "joint and several" liability for \$40,000, the amount reported would be \$40,000 for each party.

.07 Former Associated Persons. For purposes of paragraphs (a), (b) and (d) of this Rule, members should report an event relating to a former associated person if the event occurred while the individual was associated with the member. A member is not required to report such an event where, based on its records, the member cannot determine that the

person was an associated person of the member, provided that the member's records were preserved for the period of time and accessibility specified in SEA Rule 17a-4(e)(1).

.08 Customer Complaints. For purposes of paragraph (a)(1)(B) of this Rule, a "customer" includes any person, other than a broker or dealer, with whom the member has engaged, or has sought to engage, in securities activities. Any written customer complaint reported under paragraph (a)(1)(B) of this Rule also must be reported pursuant to paragraph (d) of this Rule. For purposes of paragraph (d) of this Rule, with respect to a person, other than a broker or dealer, with whom the member has engaged in securities activities, the member must report any written grievance by such person involving the member or a person associated with the member. In addition, with respect to a person, other than a broker or dealer, with whom the member has sought to engage in securities activities, the member must report any securities-related written grievance by such person involving the member or a person associated with the member and any written complaint reportable under paragraph (a)(1)(B) of this Rule.

.09 Financial Related. For purposes of this Rule, the term "financial related" means related to the provision of financial services.

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

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Rule 351. Reporting Requirements

(a) **Reserved.** [Each member not associated with a member organization and each member organization shall promptly report to the Exchange whenever such member

or member organization, or any member or registered or non-registered employee associated with such member or member organization:]

[(1) has violated any provision of any securities law or regulation, or any agreement with or rule or standards of conduct of any governmental agency, self-regulatory organization, or business or professional organization, or engaged in conduct which is inconsistent with just and equitable principles of trade or detrimental to the interests or welfare of the Exchange;]

[(2) is the subject of any written customer complaint involving allegations of theft or misappropriation of funds or securities or of forgery;]

[(3) is named as a defendant or respondent in any proceeding brought by a regulatory or self-regulatory body alleging the violation of any provision of the Securities Exchange Act of 1934, or of any other Federal or state securities, insurance, or commodities statute, or of any rule or regulation thereunder, or of any agreement with, or of any provision of the constitution, rules or similar governing instruments of, any securities, insurance or commodities regulatory or self-regulatory organization;]

[(4) is denied registration or is expelled, enjoined, directed to cease and desist, suspended or otherwise disciplined by any securities, insurance or commodities industry regulatory or self-regulatory organization or is denied membership or continued membership in any such self-regulatory organization; or is barred from becoming associated with any member or member organization of any such self-regulatory organization;]

[(5) is arrested, arraigned, indicted or convicted of, or pleads guilty to, pleads no contest to, any felony; or any misdemeanor that involves the purchase or sale of any security, the taking of a false oath, the making of a false report, bribery, perjury, burglary, larceny, theft, robbery, extortion, forgery, counterfeiting, fraudulent concealment, embezzlement, fraudulent conversion, or misappropriation of funds, or securities, or a conspiracy to commit any of these offenses, or substantially equivalent activity in a domestic, military or foreign court;]

[(6) is a director, controlling stockholder, partner, officer or sole proprietor of, or an associated person with, a broker, dealer, investment company, investment advisor, underwriter or insurance company which was suspended, expelled or had its registration denied or revoked by any agency, jurisdiction or organization or is associated in such a capacity with a bank, trust company or other financial institution which was convicted of, or pleaded no contest to, any felony or misdemeanor;]

[(7) is a defendant or respondent in any securities or commodities-related civil litigation or arbitration which has been disposed of by judgment, award or settlement for an amount exceeding \$15,000. However, when a member organization is the defendant or respondent, then the reporting to the Exchange shall be required only when such judgment, award or settlement is for an amount exceeding \$25,000;]

[(8) is the subject of any claim for damages by a customer, broker or dealer which is settled for an amount exceeding \$15,000. However, when the

claim for damages is against a member organization, then the reporting to the Exchange shall be required only when such claim is settled for an amount exceeding \$25,000;]

[(9) is, or learns that he is associated in any business or financial activity with any person who is, subject to a “statutory disqualification” as that term is defined in the Securities Exchange Act of 1934.]

[(10) is the subject of any disciplinary action taken by the member or member organization against any of its associated persons involving suspension, termination, the withholding of commissions or imposition of fines in excess of \$2,500, or any other significant limitation on activities.]

(b) **Reserved.** [Each member associated with a member organization and each registered or non-registered employee of a member or member organization shall promptly report the existence of any of the conditions set forth in paragraph (a) of this rule to the member or member organization with which such person is associated.]

(c) **Reserved.** [Each approved person shall promptly report to the member organization with which such approved person is associated, whenever such approved person becomes subject to a statutory disqualification as defined in Section 3(a)(39) of the Securities Exchange Act of 1934; and upon being so notified, or otherwise learning such fact, the member or member organization shall promptly so advise the Exchange in writing, giving the name of the person subject to the statutory disqualification and details concerning the disqualification.]

(d) **Reserved.** [At such intervals and in such detail as the Exchange shall specify, each member not associated with a member organization and each member organization

shall report to the Exchange statistical information regarding customer complaints relating to such matters as may be specified by the Exchange. For the purpose of this paragraph (d), “customer” includes any person other than a broker or dealer.]

(e) through (f) No Change.

••• **Supplementary Material:** -----

.10 Reserved. [Any report required pursuant to paragraphs (a), (b) or (d) of this Rule 351 shall be submitted to the Exchange on a form or forms prescribed by the Exchange.]

.11 through .12 No Change.

.13 Reserved. [The term “customer complaint” shall mean any written statement of a customer, or any person acting on behalf of a customer, other than a broker or dealer, alleging a grievance involving the activities of those persons under the control of a member organization.]

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