



July 1, 2019

By Electronic Email (pubcom@finra.org)

Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

RE: Regulatory Notice 19-17: FINRA Requests Comment on Proposed New Rule 4111 (Restricted Firm Obligations) Imposing Additional Obligations on Firms with a Significant History of Misconduct.

Dear Ms. Mitchell,

Thank you for the opportunity to submit these comments on the proposed new rule to the Financial Industry Regulatory Authority (“FINRA”) Financial and Operational Rules, Rule 4000 Series (FINRA Proposed Rule 4111) on behalf of HLBS Law.

HLBS Law appreciates FINRA’s goal of enforcing measures to protect investors and maintaining an accurate and meaningful regulatory platform to inform the investing public. HLBS Law advocates for removal of meritless customer disclosures for Registered Representatives. HLBS utilizes FINRA’s dispute resolution forum and follows FINRA Rules promulgated to provide a path to expunge false and misleading U4 and U5 disclosures, of which there are many. This common goal of making sure the public can make informed decisions is why Proposed FINRA Rule 4111 cannot be enacted.

FINRA has created 6 categories of events or conditions that will flag a registered member and potentially increase the risk a member firm will be designated as restricted:

1. Registered Person Adjudicated Events;
2. Registered Person Pending Events;
3. Registered Person Termination and Internal Review Events;
4. Member Firm Adjudicated Events;
5. Member Firm Pending Events; and
6. Registered Persons Associated with Previously Expelled Firms (also referred to as the Expelled Firm Association category).

To avoid designation, Proposed FINRA Rule 4111 has a one-time option to terminate Registered Persons to reduce staffing levels to below numeric thresholds. Proposed FINRA Rule 4111 is overbroad and violates the trust the public has placed in FINRA to report accurate and



meaningful information. Rule 4111 would create the designation of a Restricted Firm when numeric thresholds of disclosures proposed by FINRA are met.

If a firm meets the restrictive status, the member firm is required to deposit a large sum of money pursuant to a grid created by FINRA. The purpose of FINRA Rule 4111 according to Regulatory Notice 19-17 is to protect investors from misconduct. In reality, FINRA Rule 4111 is a punitive measure without due process constraints. It is designed to punish Registered Persons and Registered Firms and does little more than spread unverified accusations and inhibit free trade.

1. A restricted status designation under Proposed Rule 4111 misleads the public because it is based on unverified misconduct.

Proposed Rule 4111 is not crafted to inform the public when misconduct occurs for several reasons:

- A Member firm's decision to settle is a business decision, not an admission of misconduct. In the vast majority of FINRA arbitrations, the costs to fully litigate a matter to conclusion far outweighs the costs to simply settle the case for pennies on the dollar, regardless of the merits of the case.
- A presumption of guilt is an anathema to fundamental principles of justice. FINRA has provided no evidence or support that shows pending claims are related to misconduct. FINRA is essentially adopting presumed guilty standard. As it stands, the Rule is a blanket measure that does not differentiate between meritorious and unmeritorious claims.
- Proposed FINRA Rule 4111 attempts to undermine what historically has been a business decision whether or not to terminate someone's employment or contractual relationship. The rule throws out a blanket category without addressing what language is on the registered member's Form U-5. FINRA has not tailored the designation to ensure a nexus between firm attrition and investor protection.

As drafted, this rule punishes mere suspicion of misconduct. It results in a disservice to the public, and a chilling effect on Member firms and Registered Persons. Why waste resources on anything more than a cursory investigation when the punishment is the same whether there is any wrongful conduct found or not? This rule does not result in a truthful disclosure to the public, only the branding of a scarlet letter on the chest of Member firms and Representatives.

2. The proposed rule inhibits free trade by allowing FINRA to insert itself in Member firms' day-to-day business decisions.

A fundamental principle of the American workforce economy is that business and people are free to choose with whom to associate in their employment relationship. With rare exception, States have acknowledged that an employer/employee relationship is at-will. The Proposed Rule allows FINRA to substantially influence Member firms' recruiting and termination decisions.



Proposed Rule 4111 is aimed at only small to mid-sized firms. These firms do not have the same resources for attracting and keeping experienced representatives as large firms do. To be blunt, there is significant business value in attracting experienced Registered Representatives who, but for a U4 or U5 disclosure, would not consider aligning with a smaller firm. Proposed Rule 4111 forces Member firms to prioritize disclosures over candidate attributes. In order to stay competitive, a Member firm must now factor in whether to retain a 30-year veteran with a 20-year old disclosure, or an untested recruit with a clean record. This is a gross intrusion on onboarding and retention decisions.

The most alarming and punitive measure of Proposed FINRA Rule 4111 is the one-time option to terminate Registered Persons to reduce staffing levels to below numeric thresholds. Layoffs are a regular occurrence on the employment landscape. However, under Rule 4111, Member firms would conduct a mass termination not because of independent business decision, but because the practical result of failing to do so is a regulatory designation that would essentially result in financial ruin.

Conclusion

FINRA has the privilege and burden of making sure the investing public is protected and informed. Proposed Rule 4111 does not align with this objective. 4111 is overbroad and employs strong-arm tactics that rely on the BrokerCheck public reporting system that is itself indisputably flawed. It is our hope that the SEC once again steps in like it did with Regulatory Notice 17-42 and object to this overbroad rule with sweeping consequences.

Once again, HLBS Law thanks you for the opportunity to submit these comments. If there is any further information or other assistance that we may be able to provide, or if there are any questions we may be able to answer, please contact me at owen.harnett@hlbslaw.com or 720-515-9069.

Respectfully,

Owen Harnett
Managing Attorney