



**Michael Garawski**  
Associate General Counsel  
Office of General Counsel

Direct: (202) 728-8835  
Fax: (202) 728-8264

September 15, 2022

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

**Re: File No. SR-FINRA-2022-015 (Proposed Rule Change to Amend FINRA Rule 9312 (FINRA BrokerCheck Disclosure) to Release Information on BrokerCheck Relating to Firm Designation as a Restricted Firm)**

Dear Ms. Countryman:

This letter is being submitted by the Financial Industry Regulatory Authority (“FINRA”) in response to comments received by the Securities and Exchange Commission (“SEC” or “Commission”) regarding the above-referenced rule filing. The proposed rule change would amend Rule 8312 (FINRA BrokerCheck Disclosure) to release information on BrokerCheck® as to whether a particular member firm or former member firm is currently designated as a “Restricted Firm” pursuant to Rule 4111 (Restricted Firm Obligations) and Rule 9561 (Procedures for Regulating Activities Under Rule 4111).

The Commission published the proposed rule change for public comment in the Federal Register on June 17, 2022.<sup>1</sup> The Commission received four comment letters directed to the rule filing.<sup>2</sup> The following are FINRA’s responses to the commenters’ material concerns.

---

<sup>1</sup> See Securities Exchange Act Release No. 95092 (June 13, 2022), 87 FR 36551 (June 17, 2022) (Notice of Filing of File No. SR-FINRA-2022-015) (“Filing”).

<sup>2</sup> See Letter from Francis J. Skinner, Esq., CLO, CoastalOne, to SEC, dated July 6, 2022 (“Skinner”); Letter from Nicole G. Iannarone, Assistant Professor of Law, Drexel University, Thomas R. Kline School of Law & Christine Lazaro, Professor of Clinical Legal Education and Director of the Securities Arbitration Clinic, St. John’s University School of Law, to Vanessa Countryman, Secretary, SEC, dated July 7, 2022 (“Iannarone and Lazaro”); Letter from Michael Edmiston, President, Public Investors Advocate Bar Association, to J. Matthew DeLesDernier, Assistant Secretary, SEC, dated July 8, 2022 (“PIABA”); and Letter from Mark Quinn,

### General Support for the Proposal

Two commenters generally support the proposal. Iannarone and Lazaro comment that disclosure of Restricted Firm status on BrokerCheck “would further improve BrokerCheck and allow retail investors to make more informed choices and ask pertinent questions to financial professionals before engaging them.” They also recommend adopting the proposal as written “so as not to delay the increased investor protection that will result from it.” PIABA believes that “making this information about firms publicly available on BrokerCheck is the common-sense next step to the newly adopted FINRA Rule 4111 and comports with that rule’s intended investor protection goal.” FINRA appreciates, and agrees with, these comments.

### Opposition to the Proposal

Cetera and Skinner do not support the proposal. Both point to potential adverse economic impacts that may result from disclosing Restricted Firm designations on BrokerCheck. For example, Cetera comments that any firm designated as a Restricted Firm “will have an immediate stigma” that is “significant enough to increase the likelihood that the firm will fail,” which “would make it less able to meet its obligations to customers, . . . increase the possibility of disorderly failure or closure,” and potentially make customers “worse off than had the restricted status of the firm not been disclosed.” Cetera adds that while “[p]ublic disclosure of Restricted Firm status adds to the information available to the public,” “the potential for negative consequences to the firm militates in favor of avoiding disclosure on the BrokerCheck system.” Similarly, Skinner contends that the proposed BrokerCheck disclosure would be a “scarlet letter” that could cause severe economic impact on, and harm to, the firm, with a high probability that it would put firms (especially small firms) out of business and would hinder the future employment prospects of employees who are “guilty by association.”

As FINRA explained in the Filing, the proposed disclosure on BrokerCheck of a firm’s designation as a Restricted Firm may have a range of economic impacts. Most importantly, it would enhance the investor-protection benefits of Rule 4111. It may prompt investors to learn more about Restricted Firms, engage with them more cautiously, or, for investors currently using the services of Restricted Firms, critically review their experiences with these firms.<sup>3</sup> It may help some investors avoid harms associated with future misconduct.<sup>4</sup> The disclosure, and the additional investor caution, may prompt firms

---

Director of Regulatory Affairs, Cetera Financial Group, to Secretary, SEC, dated July 8, 2022 (“Cetera”).

<sup>3</sup> See Filing, 87 FR 36551, 36554.

<sup>4</sup> See Filing, 87 FR 36551, 36554.

designated as Restricted Firms to offer more competitive pricing, improve customer service, and act to improve internal controls to avoid additional reputation harm and being re-designated as a Restricted Firm in subsequent years.<sup>5</sup>

As FINRA also explained in the Filing, the additional investor caution and potential reactions by third parties (i.e., a Restricted Firm’s clearing firms and trading partners) may cause pressures and, if significant enough, financial distress at Restricted Firms.<sup>6</sup> While the magnitude of those reactions cannot be quantified, it is possible, as FINRA previously acknowledged, that the proposed BrokerCheck disclosure may result in some Restricted Firms going out of business.<sup>7</sup> FINRA believes, however, that these potential impacts on Restricted Firms would be mitigated by how the Rule 4111 multi-step process includes numerous features designed to narrowly focus the new obligations on the firms most of concern,<sup>8</sup> and by the proposed rule change’s effective date.<sup>9</sup> On this latter point, FINRA expects that the effective date of the proposed rule change would be a date after FINRA completes the first annual Rule 4111 cycle,<sup>10</sup> but no later than the “Evaluation Date” for the second annual Rule 4111 cycle.<sup>11</sup> FINRA would make the relevant disclosures on BrokerCheck beginning with the firms that are designated or re-designated

---

<sup>5</sup> See Filing, 87 FR 36551, 36554.

<sup>6</sup> See Filing, 87 FR 36551, 36554.

<sup>7</sup> See Filing, 87 FR 36551, 36554.

<sup>8</sup> See Securities Exchange Act Release No. 90527 (November 27, 2020), 85 FR 78540, 78542 (December 4, 2020) (Notice of Filing of SR-FINRA-2020-041) (“Notice”).

<sup>9</sup> See Filing, 87 FR 36551, 36553.

<sup>10</sup> FINRA began the first annual Rule 4111 cycle in early July 2022, when it conducted the first Rule 4111 annual calculation of which firms meet the “Preliminary Criteria for Identification.” See Rule 4111(b); see also Rule 4111(i)(9) (defining “Preliminary Criteria for Identification”).

<sup>11</sup> See Rule 4111(i)(5) (defining “Evaluation Date”). The Evaluation Date for the first annual Rule 4111 cycle was June 1, 2022. FINRA has previously stated that it expects that the Evaluation Dates in subsequent years also will be on June 1, but that it will evaluate whether future adjustments of the annual Evaluation Date are warranted and announce any changes in such date sufficiently in advance. See Information Notice, February 1, 2022 (FINRA Announces Rule 4111 (Restricted Firm Obligations) Evaluation Date).

as Restricted Firms in the second annual Rule 4111 cycle.<sup>12</sup> This would allow FINRA to gain meaningful experience with Rule 4111, including any operational shortcomings, before FINRA begins disclosing Restricted Firms on BrokerCheck.<sup>13</sup>

With respect to the potential impacts on employees of Restricted Firms, FINRA noted in the Filing that the proposed rule change is expected to affect individuals associated with Restricted Firms indirectly.<sup>14</sup> For example, employees with clean disciplinary records who work for a Restricted Firm, or who anticipate that their firm will be designated as a Restricted Firm, may have an incentive to leave, which would add to the potential pressures on the firm as discussed in the Filing and above. Moreover, the extent to which Rule 4111

---

<sup>12</sup> The second annual Rule 4111 cycle will commence when FINRA conducts the second annual calculation of the Preliminary Criteria for Identification, which FINRA expects will be in July 2023.

<sup>13</sup> As noted above, Skinner comments that the potential harms would especially affect small firms. The proposed BrokerCheck disclosure, however, would impact only those firms designated as Restricted Firms pursuant to Rule 4111, a rule that the Commission previously found “takes a reasonable approach to identifying firms that pose the greatest risk to investors, without being unduly burdensome towards smaller firms.” See Securities Exchange Act Release No. 92525 (July 30, 2021), 86 FR 42925, 42941 (August 5, 2021) (Order Approving File No. SR-FINRA-2020-041), see also Securities Exchange Act Release No. 92525 (July 30, 2021), 86 FR 49589 (September 3, 2021) (Order Approving File No. SR-FINRA-2020-041) (Correction).

As also noted above, Cetera comments that the potential harms may include the disorderly failure or closure of a firm that makes customers worse off. However, in the event the public disclosure of a firm’s Restricted Firm designation leads to financial distress that is significant enough to cause the firm to cease operations, “multiple layers of protection [would] safeguard investor assets.” See Investor Alert, If a Brokerage Firm Closes Its Doors, available at <https://www.finra.org/investors/alerts/if-brokerage-firm-closes-its-doors> (explaining, among other things, the customer protections provided by the Net Capital Rule, the Customer Protection Rule, and the Securities Industry Protection Corporation (SIPC), and how, when a brokerage firm liquidates, securities regulators “work with the firm to make sure that customer accounts are protected and that customer assets are transferred in an orderly fashion to one or more SIPC-protected brokerage firms”). To the extent there are any residual risks to customers, FINRA believes they would be outweighed by the investor-protection benefits from publicly disclosing a firm’s designation as a Restricted Firm.

<sup>14</sup> See Filing, 87 FR 36551, 36553.

may impact the employment prospects of Restricted Firms' registered persons, including ones with relevant disclosures, is expected to be limited,<sup>15</sup> and FINRA does not expect the proposed BrokerCheck disclosure of a firm's designation as a Restricted Firm would change that significantly, given that none of the Rule 4111 metrics are based on prior associations with Restricted Firms. Further, most of the underlying events included in the metrics employed in Rule 4111 are already in BrokerCheck. FINRA believes the disclosure history of individual registered persons seeking new employment will be appropriately considered by a prospective firm, including in determining if the individual's disclosures impact the firm's Rule 4111 metrics. While there is some possible risk that a person's association or prior association with a Restricted Firm may potentially impact future employment prospects in ways unrelated to Rule 4111, FINRA believes that these risks are outweighed by the investor protection benefits of the proposed rule change.

Skinner also writes that the disclosure on BrokerCheck of a firm's designation as a Restricted Firm would be confusing and misleading. FINRA disagrees with these comments. As explained in the Filing, information that a firm is currently a Restricted Firm would be displayed in BrokerCheck on both a firm's summary report and detailed report. Specifically, those reports would include the text, "This firm is currently designated as a Restricted Firm pursuant to FINRA Rule 4111 (Restricted Firm Obligations)," in a color or font that is prominent, and contain a hyperlink to Rule 4111. They also would include the text, "Click here for more information," with a hyperlink to a page on FINRA's website that provides for the investing public a clear explanation of Rule 4111 and what it means to be a Restricted Firm. FINRA believes this will provide investors with clear and accurate information about Restricted Firms. Further, FINRA believes the specific display of a firm's Restricted Firm designation on BrokerCheck will make this status more readily apparent to investors and could prompt investors to ask the firm about the firm's status. FINRA further notes that this is the same way that FINRA publicly discloses information that a firm is a "taping firm" and provides for the public a clear explanation of the Taping Rule.<sup>16</sup>

---

<sup>15</sup> See Notice, 85 FR 78540, 78553 & n.62 (explaining that that the economic impact from Rule 4111 on individuals' employment prospects is expected to be limited to a small proportion of registered persons, specifically those with a significant number of disciplinary and other disclosure events on their records, and that the vast majority of member firms would likely be able to employ most of the individuals seeking employment in the industry, including ones who have some disclosures, without coming close to meeting the Rule 4111 Preliminary Criteria for Identification).

<sup>16</sup> See Filing, 87 FR 36551, 36552 & n.19; Regulatory Notice 21-09 (March 2021). The description of the Taping Rule that is hyperlinked in taping firms'

Likewise, the proposed disclosure would not, as Skinner claims, be redundant. Although a Restricted Firm designation is based on events already disclosed on BrokerCheck—such as certain events that are reported on the Uniform Registration Forms—the disclosure of a firm’s designation as a Restricted Firm would provide additional information to investors. It would convey that FINRA has designated the firm as a Restricted Firm after determining that the firm meets the Preliminary Criteria for Identification, conducting an initial evaluation, and having a consultation with the member; that the firm has significantly higher levels of risk-related disclosures than other similarly sized peers and presents a high degree of risk to investors; and that the firm may be subject to a “Restricted Deposit Requirement” and other conditions or restrictions.<sup>17</sup> This is not information that an investor could gather today from reviewing a firm’s BrokerCheck report.

Skinner also comments that FINRA’s purpose for Rule 4111 was “to provide some assurances that if a firm is levied with a large arbitration award, it does not simply fold the tents and disappear, leaving wronged investors with unpaid arbitration awards,” and that a display on BrokerCheck of a Restricted Firm designation “adds nothing to further that purpose.” FINRA disagrees with this assertion and, as explained in the Filing, FINRA is proposing changes to Rule 8312 to enhance the investor-protection benefits of Rule 4111.<sup>18</sup> The primary goal of Rule 4111 is to incentivize members with a significant history of misconduct relative to their peers to change behavior.<sup>19</sup> Such incentives would only be strengthened by the disclosure on BrokerCheck of a firm’s Restricted Firm designation, because it would further motivate a firm to change behavior so as to avoid or lose such a designation. Moreover, just as Rule 4111 may have important ancillary effects on addressing unpaid arbitration awards,<sup>20</sup> so too would the proposed BrokerCheck disclosure. By strengthening the incentives to reduce firms’ risk profile and violative conduct, the

---

BrokerCheck reports is available at <https://www.finra.org/rules-guidance/guidance/taping-rule>.

<sup>17</sup> See generally Rule 4111; see Rule 4111(i)(15) (defining “Restricted Deposit Requirement”); Regulatory Notice 21-34 (September 2021) (describing the Preliminary Criteria for Identification and the annual Rule 4111 process).

<sup>18</sup> See Filing, 87 FR 36551, 36552.

<sup>19</sup> See Notice, 85 FR 78540, 78558.

<sup>20</sup> See Notice, 85 FR 78540, 78565.

proposed disclosure may further deter behavior that could otherwise result in unpaid arbitration awards.<sup>21</sup>

Skinner also comments that the proposal has not provided “objective statistical evidence” that the proposal will be helpful. FINRA included in the Filing, however, an economic impact analysis that is consistent with FINRA’s approach to economic impact assessments for proposed rulemakings.<sup>22</sup>

### Design and Scope of Disclosure

While Iannarone and Lazaro recommend that the proposal be adopted as written, they also recommend two future changes. First, they suggest that a plain-English explanation of what a Restricted Firm designation means should be provided on the BrokerCheck report itself, because they “do not believe a link to the rule on its own would be enough.” As explained above, the proposed BrokerCheck disclosure would include hyperlinks not just to Rule 4111, but also to a page on FINRA’s website that provides for the investing public a clear explanation of Rule 4111 and what it means to be a Restricted Firm. FINRA would provide such an explanation on a separate webpage, rather than on the BrokerCheck reports, because of considerations related to BrokerCheck usability. The overall BrokerCheck design approach is user-centric and involves a significant number of considerations when determining how to display information. FINRA expects the explanation of what it means to be a Restricted Firm would be several paragraphs long.<sup>23</sup> Were a description of such length to be included at the top of the relevant BrokerCheck reports, space constraints would necessitate using a font that is too small to be easily readable. FINRA also believes, based on its general user testing of BrokerCheck, that including the explanation on the BrokerCheck reports would create a cluttered presentation that has a detrimental impact on the user’s experience. Nonetheless, FINRA appreciates

---

<sup>21</sup> Cf. Notice, 85 FR 78540, 78565 (explaining that Rule 4111 “may deter behavior that could otherwise result in unpaid arbitration awards, by incentivizing firms to reduce their risk profile and violative conduct in order to avoid being deemed a Restricted Firm and becoming subject to the Restricted Deposit Requirement (or other conditions or restrictions)”).

<sup>22</sup> See Framework Regarding FINRA’s Approach to Economic Impact Assessment for Proposed Rulemaking, available at [https://www.finra.org/sites/default/files/Economic%20Impact%20Assessment\\_0\\_0.pdf](https://www.finra.org/sites/default/files/Economic%20Impact%20Assessment_0_0.pdf).

<sup>23</sup> By comparison, the description of the Taping Rule that is hyperlinked from Taping Firms’ BrokerCheck reports is several paragraphs long. See <https://www.finra.org/rules-guidance/guidance/taping-rule>.

the commenters' suggestion and, if the proposed rule change is approved, will revisit this presentation choice as part of its routine monitoring of BrokerCheck information design.

The second future change suggested by Iannarone and Lazaro is to also disclose on BrokerCheck a firm's *prior* Restricted Firm designations. At the present time, however, FINRA believes that the potential for a Restricted Firm disclosure to be removed from BrokerCheck would serve as a strong incentive for firms designated as Restricted Firms to improve their behavior and, thus, would further the primary purpose of Rule 4111 itself.<sup>24</sup> That said, FINRA appreciates this suggestion and, if the proposed rule change is approved, will revisit it after gaining experience with disclosing Restricted Firm designations on BrokerCheck.

#### Public Awareness of BrokerCheck

PIABA comments that FINRA should couple this proposed rule change with an investor outreach program or marketing effort that draws attention to the importance of BrokerCheck and the types of information that can be found there. FINRA appreciates PIABA's comment, and notes that FINRA has taken, and continues to take, various measures to increase investor awareness of BrokerCheck. For example, FINRA has adopted Rule 2210(d)(8), which requires that each of a member's websites include a readily apparent reference and hyperlink to BrokerCheck on the initial webpage that the member intends to be viewed by retail investors and any other webpage that includes a professional profile of one or more registered persons who conduct business with retail investors.<sup>25</sup> Likewise, Rule 2267 requires members to provide to customers the FINRA BrokerCheck Hotline Number and a statement as to the availability to the customer of an investor brochure that includes information describing BrokerCheck. In addition, for the purpose of educating investors about BrokerCheck, FINRA regularly raises awareness about BrokerCheck in the media, across FINRA's social media channels, and at investor-focused events including investor forums and other engagements.

---

<sup>24</sup> See Notice, 85 FR 78540, 78550 (explaining that Rule 4111 would "create incentives for firms to change behaviors and activities, either to avoid being designated as a Restricted Firm or lose an existing Restricted Firm designation").

<sup>25</sup> See also Regulatory Notice 15-50 (December 2015) (explaining that "FINRA believes that greater investor awareness of and access to BrokerCheck continues to be important to protect investors" and that Rule 2210(d)(8) will "help increase investor awareness and make it easier for investors to find BrokerCheck by requiring references and hyperlinks to BrokerCheck on member firms' websites").



Timing of Disclosure on BrokerCheck in the Event of a Hearing

In the Filing, FINRA explained that information that a firm is a Restricted Firm would display on BrokerCheck while that firm is designated as a Restricted Firm. FINRA also explained that this would include during the pendency of a Rule 9561 expedited proceeding to review a Department of Member Regulation (“Department”) decision that designates a firm as a Restricted Firm, because such a decision is not stayed during a Rule 9561 proceeding.<sup>26</sup> Cetera suggests, however, that if Restricted Firms are to be identified on BrokerCheck, such disclosure “should be delayed until the entire adjudicatory process has been completed.”

FINRA appreciates the comment, but continues to believe that displaying information on BrokerCheck that a firm is a Restricted Firm while that firm is designated as a Restricted Firm—including during the pendency of a Rule 9561 expedited proceeding—strikes the right balance in support of investor protection. During the pendency of a Rule 9561 expedited proceeding, a firm’s obligations under Rule 4111 are not stayed; a designated Restricted Firm will still be required to comply with any conditions and restrictions imposed on the firm and deposit a portion of any Restricted Deposit Requirement. Displaying the firm’s Restricted Firm status on BrokerCheck while the Rule 9561 expedited proceeding is pending could prompt investors to ask the firm about the firm’s status. However, in light of the comment, FINRA will work to include in the display on BrokerCheck, in situations where the firm has requested a hearing in a Rule 9561 expedited proceeding,<sup>27</sup> information that a Restricted Firm designation is on appeal.

\* \* \* \* \*

FINRA believes that the foregoing responds to the material issues raised by the commenters to the rule filing. If you have any questions, please contact me at (202) 728-8835, email: [michael.garawski@finra.org](mailto:michael.garawski@finra.org).

Best regards,

/s/ Michael Garawski

Michael Garawski  
Associate General Counsel  
FINRA Office of General Counsel

---

<sup>26</sup> See Filing, 87 FR 36551, 36552 & n.15.

<sup>27</sup> See Rule 9561(a)(5).