

Regulatory Notice

08-23

Financial Responsibility

Proposed Consolidated FINRA Rules Governing Financial Responsibility

Comment Period Expires: June 13, 2008

Executive Summary

As part of the process to develop a new consolidated rulebook (the Consolidated FINRA Rulebook),¹ FINRA is requesting comment on a proposed set of financial responsibility rules (the proposed rules). Proposed FINRA Rules 4110, 4120, 4130, 4140 and 4521 would be new, consolidated rules based in part on existing NASD and Incorporated NYSE Rules² and would govern members' financial responsibility requirements. Proposed FINRA Rules 9557 and 9559 would revise NASD Rules 9557 and 9559, respectively, and would afford members served with a notice under the financial responsibility rules an expedited appeal process. (In addition, FINRA would make conforming revisions to Section 4(g) of Schedule A to the FINRA By-Laws.)

The text of the proposed rules is set forth in Attachment A. The chart in Attachment B summarizes the applicability of the proposed rules to member firms.

Questions regarding this *Notice* should be directed to:

- Kris Dailey, Vice President, Risk Oversight & Operational Regulation, at (646) 315-8434;
- Susan M. DeMando, Associate Vice President, Financial Operations Policy, at (202) 728-8411; or
- Adam H. Arkel, Assistant General Counsel, Office of General Counsel, at (202) 728-6961.

May 2008

Notice Type

- Request for Comment
- Consolidated FINRA Rulebook

Suggested Routing

- Compliance
- Legal
- Senior Management

Key Topic(s)

- Financial Responsibility
- Capital Compliance

Referenced Rules & Notices

- NASD Rule 3130
- NASD IM-3130
- NASD Rule 3131
- NASD Rule 9557
- NASD Rule 9559
- NYSE Rule 312
- NYSE Rule 313
- NYSE Rule 325
- NYSE Rule 326
- NYSE Rule 328
- NYSE Rule 416
- NYSE Rule 418
- NYSE Rule 420
- NYSE Rule 421(2)
- SEA Rule 15c3-1
- SEA Rule 15c3-3
- Section 4(g) of Schedule A to FINRA By-Laws



Financial Industry Regulatory Authority

Action Requested

FINRA encourages all interested parties to comment on the proposed rules. Comments must be received by June 13, 2008. Comments received after the close of the comment period will not be considered, although interested parties will have further opportunity to comment when the proposals resulting from this *Notice* process are filed with the SEC for approval.

Member firms and other interested parties can submit their comments using the following methods:

- Emailing comments to pubcom@finra.org; or
- Mailing comments in hard copy to:

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

To help FINRA process and review comments more efficiently, persons should only use one method to comment on the proposal.

Important Notes: The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA Web site. Generally, FINRA will post comments on its site one week after the end of the comment period.³

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the FINRA Board of Governors, and then must be approved by the SEC, following publication for public comment in the Federal Register.⁴

Background

The financial responsibility rules play a crucial role in achieving member firms' compliance with their capital requirements. For that reason, FINRA has placed high priority on expeditiously developing the unified set of proposed rules for inclusion in the Consolidated FINRA Rulebook. Currently, both NASD and NYSE Rules contain provisions governing financial responsibility. The proposed rules would incorporate many of these provisions but would streamline and reorganize the provisions. In addition, many provisions have been tiered to apply only to those firms that clear or carry customer accounts or that operate pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) (referred to as "(k)(2)(i) members").⁵ The more significant changes are described below.

Discussion

A. Proposed FINRA Rule 4110 (Capital Compliance)⁶

1. Authority to Increase Capital Requirements

Proposed FINRA Rule 4110(a), based primarily on NYSE Rule 325(d), would enable FINRA to prescribe greater net capital requirements for carrying, clearing and (k)(2)(i) member firms, or require any such member to restore or increase its net capital or net worth, when deemed necessary for the protection of investors or in the public interest. The authority to act under the proposed rule would reside with FINRA's executive vice president charged with oversight for financial responsibility (or his or her written officer delegate) (referred to as "FINRA's EVP"). To execute such authority, FINRA would be required to issue a notice pursuant to Proposed FINRA Rule 9557 (referred to as a "Rule 9557 notice"). Proposed FINRA Rule 9557, much like NASD Rule 9557, would afford a member opportunity for an expedited hearing pursuant to Proposed FINRA Rule 9559. (See Section F of this Notice, below.)

Proposed FINRA Rule 4110(a) would be a new provision for FINRA members that are not Dual Members (referred to as "non-NYSE members") that are carrying, clearing or (k)(2)(i) member firms. However, it would not apply to introducing firms or to firms with limited business models (together, referred to as "non-clearing firms"). (For example, introducing firms and firms that engage exclusively in subscription-basis mutual fund transactions, direct participation programs, or mergers and acquisitions activities would not be subject to the provision.) In this regard, certain Dual Members that currently are subject to NYSE Rule 325(d)—namely those NYSE member firms that are not carrying, clearing or (k)(2)(i) members (referred to as "NYSE non-clearing firms")—would no longer be subject to the provision. All member firms that are subject to the provision would have an opportunity to request an expedited hearing if they receive a Rule 9557 notice, which would be a new procedural right not available under NYSE Rule 325(d).

The NYSE staff historically has employed NYSE Rule 325(d) in limited circumstances, and FINRA anticipates that it would apply Proposed FINRA Rule 4110(a) in similar fashion. Under the proposed rule, FINRA's EVP could require a carrying, clearing or (k)(2)(i) member firm to comply with increased capital requirements in extraordinary circumstances, such as where unanticipated systemic market events (*e.g.*, recent events that have caused stress in the credit markets) threaten the member firm's capital, or where the member firm maintains an undue concentration in illiquid products. In such instances, FINRA's EVP may, for example, find it appropriate, in the public interest, to raise the applicable "haircut" (that is, to increase the percentage of the market value of certain securities or commodities positions by which the member must reduce its net worth) or treat certain assets as non-allowable in computing net capital.

2. *Suspension of Business Operations*

Proposed FINRA Rule 4110(b)(1) is based in part on NASD Rule 3130(e) and would provide that, unless otherwise permitted by FINRA, a member firm must suspend all business operations during any period of time in which it is not in compliance with Securities Exchange Act (SEA) Rule 15c3-1. This requirement is consistent with current law. However, the proposed rule would expressly permit a member to effect liquidating transactions upon customer direction and proprietary transactions in circumstances where the subject transactions are reasonably expected to increase the member's net capital or reduce its risk.

As with NASD Rule 3130(e), Proposed FINRA Rule 4110(b)(1) is self-operative (that is, a firm would automatically be required to comply with the provision without any direction from FINRA). Notwithstanding that the proposed provision is self-operative, FINRA may issue a Rule 9557 notice directing a member that is not in compliance with SEA Rule 15c3-1 to suspend all or a portion of its business. Upon receipt of a Rule 9557 notice, the firm would have the right to request an expedited hearing. Neither the fact that FINRA may issue a Rule 9557 notice nor the right to an expedited hearing would be a defense in any subsequent disciplinary proceeding with respect to a member firm's non-compliance with Proposed FINRA Rule 4110(b)(1).

3. *Withdrawal of Equity Capital*

To further the goal of financial stability, Proposed FINRA Rule 4110(c)(1) would prohibit a member from withdrawing equity capital for a period of one year, unless otherwise permitted by FINRA in writing. FINRA anticipates that approvals for the early withdrawal of equity capital would be granted on a limited basis.

Proposed FINRA Rule 4110(c)(2) would apply only to carrying, clearing and (k)(2)(i) member firms and would prohibit any such member, without the prior written approval of FINRA, from withdrawing capital, paying a dividend or effecting a similar distribution that would reduce the member's equity, where such withdrawals, payments or reductions in the aggregate, in any rolling 35-calendar-day period, on a net basis, would exceed 10 percent of the member's excess net capital. This provision is based in part on NYSE Rule 312(h) and SEA Rule 15c3-1(e). While it would be a new requirement for non-NYSE members that are carrying, clearing or (k)(2)(i) members, it would not apply to non-clearing firms. In this regard, NYSE non-clearing firms that currently are subject to NYSE Rule 312(h) would no longer be required to comply with the provision. FINRA further notes that the 10 percent limit set forth in Proposed FINRA Rule 4110(c)(2) is intended as a *de minimis* exception; NYSE Rule 312(h) does not include such an exception.

4. *Sale-and-Leasebacks, Factoring, Financing, Loans and Similar Arrangements*

To ensure the permanency of net capital in contemplated sale-and-leaseback, factoring, financing and similar arrangements, Proposed FINRA Rule 4110(d)(1)(A) would provide that no carrying, clearing or (k)(2)(i) member may consummate a sale-and-leaseback arrangement with respect to any of its assets, or a sale, factoring or financing arrangement with respect to any unsecured accounts receivable, where any such arrangement would increase the member's tentative net capital by 10 percent or more, without the prior written authorization of FINRA.

Proposed FINRA Rule 4110(d)(1)(A) is based on NYSE Rule 328(a), but would apply only to carrying, clearing and (k)(2)(i) members. While the provision would be new for non-NYSE members that are carrying, clearing or (k)(2)(i) members, it would not apply to non-clearing firms. In this regard, NYSE non-clearing firms that currently are subject to NYSE Rule 328(a) would no longer be required to comply with the provision. Moreover, unlike NYSE Rule 328(a), Proposed FINRA Rule 4110(d)(1)(A) includes a *de minimis* exception by permitting a member to consummate, without FINRA's prior authorization, a sale-and-leaseback arrangement with respect to any of its assets, or a sale, factoring or financing arrangement with respect to any unsecured accounts receivable where the arrangement would not increase the member firm's tentative net capital by 10 percent or more.

Proposed FINRA Rule 4110(d)(1)(B), which is also based on NYSE Rule 328(a), would provide that no carrying member may consummate any arrangement concerning the sale or factoring of customer debit balances, irrespective of amount, without the prior written authorization of FINRA. The provision would be new for non-NYSE members that are carrying members.

Proposed FINRA Rule 4110(d)(2) is based on NYSE Rule 328(b), but also would apply only to carrying, clearing and (k)(2)(i) members. The provision would require FINRA's prior approval for any loan agreement entered into by such a member, the proceeds of which exceed 10 percent of the member's tentative net capital and that is intended to reduce the deduction in computing net capital for fixed assets and other assets that cannot be readily converted into cash under SEA Rule 15c3-1(c)(2)(iv). Because the provision would apply only to carrying, clearing and (k)(2)(i) members, NYSE non-clearing firms would be relieved from current requirements under NYSE Rule 328(b). In addition, unlike NYSE Rule 328(b), the proposed rule would include a *de minimis* exception.

Proposed FINRA Rule 4110(d)(3) provides that any member that is subject to paragraphs (d)(1)(A), (d)(1)(B) or (d)(2) of Proposed FINRA Rule 4110 would be prohibited from consummating, without FINRA's prior written authorization, any arrangement pursuant to those paragraphs if the aggregate of all such arrangements would exceed 20 percent of the member's tentative net capital.

Proposed FINRA Rule 4110(d)(4) implements a requirement of the SEC's net capital rule and therefore would apply to all members. It provides that any agreement relating to a determination of a "ready market" for securities based upon the securities being accepted as collateral for a loan by a bank under SEA Rule 15c3-1(c)(11)(ii) must be submitted to, and be acceptable to, FINRA before the securities may be deemed to have a "ready market."

5. *Subordinated Loans, Notes Collateralized by Securities and Capital Borrowings*

Proposed FINRA Rule 4110(e) is based in part on current NYSE Rule 420 and would address the requirements for subordinated loans and loans made to general partners of members that are partnerships or to LLC participants of certain members that are LLCs.

- Proposed FINRA Rule 4110(e)(1) would implement Appendix D of SEA Rule 15c3-1 and require that all subordinated loans or notes collateralized by securities must meet such standards as FINRA may require to ensure the continued financial stability and operational capability of a member, in addition to meeting those standards specified in Appendix D of SEA Rule 15c3-1.⁷ Appendix D of SEA Rule 15c3-1 requires that all subordination agreements must be found acceptable by the Examining Authority before they can become effective.
- Proposed FINRA Rule 4110(e)(2) would require that, unless otherwise permitted by FINRA, each member whose general partner or LLC participant (whose LLC agreement has provisions that operate to grant the LLC participant rights analogous to those of a general partner in a partnership) enters into any secured or unsecured borrowing, the proceeds of which will be contributed directly to the capital of the member, must, in order for the proceeds to qualify as capital acceptable for inclusion in computation of the member's net capital, submit to FINRA for approval a signed copy of the loan agreement. The loan agreement must have at least a 12-month duration and provide non-recourse to the assets of the member firm. Moreover, because a general partner's interest or certain LLC participant's interest may allow the lender to reach into the assets of the broker-dealer, FINRA is requiring a provision in the loan agreement that will estop the lender from having that right.

B. Proposed FINRA Rule 4120 (Regulatory Notification and Business Curtailment)

1. Regulatory Notification

Proposed FINRA Rule 4120(a) is based on current NYSE Rule 325(b), but would apply only to carrying, clearing and (k)(2)(i) members. The proposed rule would require any such member promptly, but in any event within 24 hours, to notify FINRA when certain specified financial triggers are reached. This would be a new notification requirement for non-NYSE members that are carrying, clearing or (k)(2)(i) members; it would not, however, apply to non-clearing firms. Accordingly, NYSE non-clearing firms would no longer be subject to the requirements.

2. Restrictions on Business Expansion

Proposed FINRA Rule 4120(b) is based on NASD Rule 3130(c) and NYSE Rule 326(a) and addresses circumstances under which a member would be prohibited from expanding its business.

Proposed FINRA Rule 4120(b)(1), which is self-operative, would apply only to carrying, clearing and (k)(2)(i) members, and requires any such member, unless otherwise permitted by FINRA, to refrain from expanding its business during any period in which any of the conditions described in Proposed FINRA Rule 4120(a)(1) continue to exist for the specified time period. While NASD Rule 3130(c) includes comparable provisions, the requirement would now be self-operative for non-NYSE members that are carrying, clearing or (k)(2)(i) members. Proposed FINRA Rule 4120(b) also provides that FINRA may issue a Rule 9557 notice directing any such member not to expand its business, in which case the member would have the right to request an expedited hearing. Neither the fact that FINRA may issue a Rule 9557 notice nor the right to an expedited hearing would be a defense in any subsequent disciplinary proceeding with respect to a member's non-compliance with Proposed FINRA Rule 4120(b)(1).

Unlike the self-operative nature of paragraph (b)(1), Proposed FINRA Rule 4120(b)(2) authorizes FINRA, for any financial or operational reason, to restrict any member's ability to expand its business by the issuance of a Rule 9557 notice. In all such cases, the member would have the right to request an expedited hearing. This same provision currently exists in NASD Rule 3130(c)(2).

3. *Reduction of Business*

Proposed FINRA Rule 4120(c) is based on NASD Rule 3130(d) and NYSE Rule 326(b) and addresses circumstances under which a member would be required to reduce its business.

Proposed FINRA Rule 4120(c)(1), which is self-operative, would apply only to carrying, clearing and (k)(2)(i) members, requiring that any such member, unless otherwise permitted by FINRA in writing, to reduce its business to a point enabling its available capital to exceed the standards set forth in Proposed FINRA Rule 4120(a)(1) when any of the enumerated conditions continue to exist for the specified time period. While NASD Rule 3130(d) includes comparable provisions, the requirement would now be self-operative for non-NYSE members that are carrying, clearing or (k)(2)(i) members. Proposed FINRA Rule 4120(c)(1) also provides that FINRA may issue a Rule 9557 notice directing any such member to reduce its business, in which case the member would have the right to an expedited hearing. Neither the fact that FINRA may issue a Rule 9557 notice nor the right to an expedited hearing would be a defense in any subsequent disciplinary proceeding with respect to a member's non-compliance with Proposed FINRA Rule 4120(c)(1).

Unlike the self-operative nature of paragraph (c)(1), proposed FINRA Rule 4120(c)(2) authorizes FINRA, for any financial or operational reason, to require any member firm to reduce its business by the issuance of a notice in accordance with Rule 9557. In all such cases, the member firm would have the right to request an expedited hearing. This same provision currently exists in NASD Rule 3130(d)(2).

C. Proposed FINRA Rule 4130 (Regulation of Activities of Section 15C Members Experiencing Financial and/or Operational Difficulties)

Proposed FINRA Rule 4130 would be substantially identical to NASD Rule 3131 except that the proposed rule would reflect FINRA as the designated examining authority and make other conforming revisions. The proposed rule would apply only to certain firms that are subject to the Treasury Department's liquid capital requirements.

D. Proposed FINRA Rule 4521 (Notifications, Questionnaires and Reports)

Drawing in part on NASD IM-3130 and Rule 3150 and NYSE Rules 325(b)(2), 416 and 421(2), Proposed FINRA Rule 4521 would address FINRA's authority to request certain information from members to carry out its surveillance and examination responsibilities. As further described below, many of the provisions would apply only to carrying, clearing and (k)(2)(i) members.

- Proposed FINRA Rule 4521(a) would provide that each carrying, clearing or (k)(2)(i) member must submit to FINRA such financial and operational information regarding the member or any of its correspondents as FINRA deems essential for the protection of investors and the public interest. The provisions would be new for certain non-NYSE members that are carrying, clearing or (k)(2)(i) members. (FINRA notes that NASD Rule 3150 (Reporting Requirements for Clearing Firms) currently requires most carrying and clearing members to submit such data to FINRA.) The proposed rule would impose a late fee of \$100 for each day that a requested report is not timely filed, up to a maximum of 10 business days.
- Proposed FINRA Rule 4521(e) would require each carrying, clearing or (k)(2)(i) member to notify FINRA in writing no more than 48 hours after its tentative net capital, as computed pursuant to SEA Rule 15c3-1, has declined 20 percent or more from the amount reported in its most recent FOCUS Report or, if later, the most recent such notification filed with FINRA. This would be a new requirement for non-NYSE members that are carrying, clearing or (k)(2)(i) members.
- Proposed FINRA Rule 4521(f) would require that, unless otherwise permitted by FINRA in writing, member firms carrying margin accounts for customers must submit, on a settlement-date basis: (1) the total of all debit balances in securities margin accounts; and (2) the total of all free credit balances contained in cash or margin accounts. This would be a new requirement for non-NYSE member firms that carry margin accounts.

E. Proposed FINRA Rule 4140 (Audit)

The proposed rules would incorporate FINRA's existing authority under NASD Rule 3130 and NASD IM-3130 and NYSE Rule 418 to request an audit or an agreed-upon procedures review under certain circumstances. The proposed rule would impose a late fee of \$100 for each day that a requested report is not timely filed, up to a maximum of 10 business days.

F. Proposed FINRA Rule 9557 (Procedures for Regulating Activities Under Rules 4110, 4120 and 4130 Regarding a Member Experiencing Financial or Operational Difficulties) and Proposed FINRA Rule 9559 (Hearing Procedures for Expedited Proceedings Under the Rule 9550 Series)

NASD Rules 9557 and 9559 address service of notice to member firms that are experiencing financial or operational difficulties and the related hearing procedures. The proposed rules would make a number of conforming revisions to NASD Rules 9557 and 9559 in light of several of the proposed financial responsibility rules (Proposed FINRA Rules 4110, 4120 and 4130). The proposed rules also would set forth new provisions to afford members with an appeals process that is more expedited than that currently provided under NASD Rules 9557 and 9559. For instance:

- Proposed FINRA Rule 9557(d) would provide that the requirements referenced in a Rule 9557 notice served upon a member are immediately effective. Under the proposed rule, a timely request for a hearing would *stay the effective date for 10 business days* after the service of the notice or until a written order is issued (whichever period is less), unless it is determined that such a stay cannot be permitted with safety to investors, creditors or other member firms;
- to ensure an expedited process, Proposed FINRA Rule 9557(e) would require a member to file with the Office of Hearing Officers any written request for a hearing *within two business days* after service of the Rule 9557 notice;
- Proposed FINRA Rule 9559(d)(2) would provide that the Chief Hearing Officer must select as panelists current or former members of the FINRA Financial Responsibility Committee;
- Proposed FINRA Rule 9559(f)(1) would provide that, after a respondent subject to a Rule 9557 notice files a written request for a hearing with the Office of Hearing Officers, the hearing must be held *within five business days of such filing*; and
- Proposed FINRA Rule 9559(o)(4) would provide that, *within two business days of the date of the close of the hearing*, the Office of Hearing Officers must issue a written order that reflects the Hearing Panel's summary determinations. The Hearing Panel's written order would be effective when issued. The Office of Hearing Officers would be required to issue a written decision in connection with its order *within seven days* of the issuance of the Hearing Panel's written order.

Endnotes

- 1 The current FINRA rulebook consists of two sets of rules: (1) NASD Rules and (2) rules incorporated from NYSE (Incorporated NYSE Rules). The Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (Dual Members). Dual Members also must comply with NASD Rules. For more information about the rulebook consolidation process, *see FINRA Information Notice, March 12, 2008* (Rulebook Consolidation Process).
- 2 For convenience, the Incorporated NYSE Rules are referred to as the “NYSE Rules.”
- 3 FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. *See NASD Notice to Members 03-73* (November 2003) (NASD Announces Online Availability of Comments) for more information.
- 4 Section 19 of the Securities Exchange Act of 1934 (SEA or Exchange Act) permits certain limited types of proposed rule changes to take effect upon filing with the SEC. The SEC has the authority to summarily abrogate these types of rule changes within 60 days of filing. *See* SEA Section 19 and rules thereunder.
- 5 For purposes of this *Notice* and the proposed rules, firms “operating” pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) is not meant to include firms that have *elected* the exemption but do not operate as such. FINRA’s records currently indicate that approximately seventy firms would be considered (k)(2)(i) members for purposes of the proposed rules.
- 6 The proposed rules may be renumbered as part of the final Consolidated FINRA Rulebook.
- 7 *See* SEA Rule 15c3-1d. Note that the proposed Supplementary Material would require that, for purposes of Proposed FINRA Rule 4110(e)(1), the member must assure itself that any applicable provisions of the Securities Act of 1933 and/or state Blue Sky laws have been satisfied, and may be required to submit evidence thereof to FINRA prior to approval of the subordinated loan agreement. *See* Proposed FINRA Rule 4110.01.

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ATTACHMENT A

Below is the text of Proposed FINRA Rules 4110, 4120, 4130, 4140, 4521, 9557 and 9559, and FINRA By-Laws Schedule A, Section 4. With respect to Proposed FINRA Rules 9557 and 9559 and FINRA By-Laws Schedule A, Section 4, new language is underlined; deletions are in brackets.

Rule 4110. Capital Compliance

(a) When necessary for the protection of investors or in the public interest, FINRA may, at any time or from time to time with respect to a particular carrying or clearing member or all carrying or clearing members or a member or members operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i), pursuant to authority exercised by FINRA's Executive Vice President charged with oversight for financial responsibility, or his or her written officer delegate, prescribe greater net capital or net worth requirements than those otherwise applicable, including more stringent treatment of items in computing net capital or net worth, or require such member to restore or increase its net capital or net worth. In any such instance, FINRA shall issue a notice pursuant to FINRA Rule 9557.

(b) (1) Unless otherwise permitted by FINRA, a member shall suspend all business operations during any period in which it is not in compliance with applicable net capital requirements set forth in SEA Rule 15c3-1, provided however, that such member may effect:

(A) liquidating transactions upon customer direction; and/or

(B) proprietary transactions in circumstances where the subject transactions are reasonably expected to increase the member's net capital or reduce its risk.

(2) FINRA may issue a notice pursuant to FINRA Rule 9557 directing a member that is not in compliance with applicable net capital requirements set forth in SEA Rule 15c3-1 to suspend all or a portion of its business.

(c) (1) Any equity capital contributed by a member may not be withdrawn for a period of one year, unless otherwise permitted by FINRA in writing.

(2) A carrying or clearing member or a member operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) shall not, without the prior written approval of FINRA, withdraw capital, pay a dividend or effect a similar distribution that would reduce such member's equity, where such withdrawals, payments or reductions in the aggregate, in any 35 rolling calendar day period, on a net basis, exceeds 10% of its excess net capital.

(d) Sale-And-Leasebacks, Factoring, Financing, Loans and Similar Arrangements

(1) (A) No carrying or clearing member or member operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) shall consummate a sale-and-leaseback arrangement with respect to any of its assets, or a sale, factoring, or financing arrangement with respect to any unsecured accounts receivable, where any such arrangement would increase the member's tentative net capital by 10% or more, without the prior written authorization of FINRA.

(B) No carrying member shall consummate any arrangement concerning the sale or factoring of customer debit balances, irrespective of amount, without the prior written authorization of FINRA.

(2) Any loan agreement entered into by a carrying or clearing member or a member operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i), the proceeds of which exceed 10% of such member's tentative net capital and which is intended to reduce the deduction in computing net capital for fixed assets and other assets which cannot be readily converted into cash under SEA Rule 15c3-1(c)(2)(iv), must be submitted to and be acceptable to FINRA, prior to such reduction becoming effective.

(3) Members subject to paragraphs (d)(1)(A), (d)(1)(B) or (d)(2), shall not consummate any arrangement pursuant to such paragraph(s) if the aggregate of all such arrangements outstanding would exceed 20% of such member's tentative net capital, without the prior written authorization of FINRA.

(4) Any agreement relating to a determination of a "ready market" for securities based upon the securities being accepted as collateral for a loan by a bank under SEA Rule 15c3-1(c)(11)(ii), must be submitted to and be acceptable to FINRA before the securities may be deemed to have a "ready market."

(e) Subordinated Loans, Notes Collateralized by Securities and Capital Borrowings

(1) All subordinated loans or notes collateralized by securities shall meet such standards as FINRA may require to ensure the continued financial stability and operational capability of the member, in addition to those specified in Appendix D of SEA Rule 15c3-1.

(2) Unless otherwise permitted by FINRA, each member partnership whose general partner, or each member LLC whose LLC participant is granted rights analogous to those of a general partner in a partnership, enters into any secured or unsecured borrowing, the proceeds of which will be contributed directly to the capital of the member, shall submit the following for approval in order for such proceeds to qualify as capital acceptable for inclusion in computation of the net capital of the member:

A signed copy of the loan agreement which must:

- (A) have at least a 12 month duration; and
- (B) provide non-recourse to the assets of the member.

Additional documents may be required, the nature of which will vary, depending upon the legal status of the lender e.g. an individual, bank, estate, trust, corporation, partnership, etc.

• • • **Supplementary Material:** — — — — —

.01. For purposes of paragraph (e)(1), the member shall assure itself that any applicable provisions of the Securities Act of 1933 and/or State Blue Sky laws have been satisfied and may be required to submit evidence thereof to FINRA prior to approval of the subordinated loan agreement.

Rule 4120. Regulatory Notification and Business Curtailment

(a) Notification

(1) Each carrying or clearing member or a member operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i), shall promptly, but in any event within 24 hours, notify FINRA in writing if its net capital falls below the following percentages:

(A) the member's net capital is less than 150 percent of its minimum dollar net capital requirement or such greater percentage thereof as may from time to time be designated by FINRA;

(B) the member is subject to the aggregate indebtedness requirement of SEA Rule 15c3-1, and its aggregate indebtedness is more than 1,000 percent of its net capital;

(C) the member elects to use the alternative method of computing net capital pursuant to SEA Rule 15c3-1(a)(1)(ii), and its net capital is less than the level specified in SEA Rule 17a-11(c)(2);

(D) the member is approved to use the alternative method of computing net capital pursuant to SEA Rule 15c3-1e, and

(i) its tentative net capital as defined in SEA Rule 15c3-1(c)(15) is less than 50 percent of the early warning notification amount required by SEA Rule 15c3-1(a)(7)(ii), or

(ii) its net capital is less than \$1.25 billion;

(E) the member is registered as a Futures Commission Merchant pursuant to the Commodity Exchange Act, and its net capital is less than 120% of the minimum risk-based capital requirements of Commodity Exchange Act Rule 1.17; or

(F) the member's deduction of capital withdrawals, which it anticipates making, whether voluntarily or as a result of a commitment, including maturities of subordinated liabilities entered into pursuant to Appendix D of SEA Rule 15c3-1, during the next six months, would result in any one of the conditions described in paragraph (a)(1)(A)-(E) of this Rule.

(b) Restrictions on Business Expansion

(1) Except as otherwise permitted by FINRA in writing, a member that carries customer accounts, clears transactions, or operates pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) shall not expand its business during any period in which any of the conditions described in paragraph (a)(1) continue to exist for more than 15 consecutive business days, provided that such condition(s) has been known to FINRA or the member for at least five consecutive business days. FINRA may issue a notice pursuant to FINRA Rule 9557 directing any such member not to expand its business; however, FINRA's authority to issue such notice does not negate the member's obligation not to expand its business in accordance with this paragraph (b)(1).

(2) No member may expand its business during any period in which FINRA restricts the member from expanding its business for any financial or operational reason. In any such instance, FINRA shall issue a notice pursuant to FINRA Rule 9557.

(3) For purposes of paragraph (b) of this Rule, the term "expansion of business" may include:

- (A) net increase in the number of registered representatives or other producing personnel;
- (B) exceeding average capital commitments over the previous three months for market making or block positioning;
- (C) initiation of market making in new securities or any new proprietary trading or other commitment in securities or commodities in which a market is not made (other than riskless trades associated with customer orders);
- (D) exceeding average commitments over the previous three months for underwritings;
- (E) opening of new branch offices;
- (F) entering any new line of business or deliberately promoting or expanding any present lines of business;
- (G) making unsecured or partially secured loans, advances, drawings, guarantees or other similar receivables; and

(H) such other activities as FINRA deems appropriate under the circumstances, in the public interest or for the protection of investors.

(c) Reduction of Business

(1) Except as otherwise permitted by FINRA in writing, a member that carries customer accounts, clears transactions, or operates pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) is obligated to reduce its business to a point enabling its available capital to exceed the standards set forth in paragraph (a)(1)(A)-(F) of this Rule, when any of the following conditions continue to exist for more than 15 consecutive business days, provided that such condition(s) has been known to FINRA or the member for at least five consecutive business days:

(A) the member's net capital is less than 125 percent of its minimum dollar net capital requirement or such greater percentage thereof as may from time to time be designated by FINRA;

(B) the member is subject to the aggregate indebtedness requirement of SEA Rule 15c3-1, and its aggregate indebtedness is more than 1,200 percent of its net capital;

(C) the member elects to use the alternative method of computing net capital pursuant to SEA Rule 15c3-1(a)(1)(ii), and its net capital is less than one percentage point below the level specified in SEA Rule 17a-11(c)(2);

(D) the member is approved to use the alternative method of computing net capital pursuant to SEA Rule 15c3-1e, and

(i) its tentative net capital as defined in SEA Rule 15c3-1(c)(15) is less than 40 percent of the early warning notification amount required by SEA Rule 15c3-1(a)(7)(ii), or

(ii) its net capital is less than \$1 billion;

(E) the member is registered as a Futures Commission Merchant pursuant to the Commodity Exchange Act, and its net capital is less than 110% of the minimum risk-based capital requirements of Commodity Exchange Act Rule 1.17; or

(F) the member's deduction of capital withdrawals, including maturities of subordinated liabilities entered into pursuant to Appendix D of SEA Rule 15c3-1, scheduled during the next six months, would result in any one of the conditions described in paragraph (c)(1)(A)-(E) of this Rule.

FINRA may issue a notice pursuant to FINRA Rule 9557 directing any such member to reduce its business to a point enabling its available capital to exceed the standards set forth in paragraph (a)(1)(A)-(F) of this Rule; however, FINRA's authority to issue such notice does not negate the member's obligation to reduce its business in accordance with this paragraph (c)(1).

(2) A member must reduce its business as directed by FINRA for any financial or operational reason. In any such instance, FINRA shall issue a notice pursuant to FINRA Rule 9557.

(3) For purposes of paragraph (c) of this Rule, the term "business reduction" shall mean reducing or eliminating parts of a member's business in order to reduce the amount of capital required, which may include:

- (A) promptly paying all or a portion of free credit balances to customers;
- (B) promptly effecting delivery to customers of all or a portion of fully paid securities in the member's possession or control;
- (C) introducing all or a portion of its business to another member on a fully disclosed basis;
- (D) reducing the size or modifying the composition of its inventory and reducing or ceasing market making;
- (E) closing of one or more existing branch offices;
- (F) collecting unsecured or partially secured loans, advances, drawings, guarantees or other similar receivables;
- (G) accepting no new customer accounts;
- (H) restricting the payment of salaries or other sums to partners, officers, directors, shareholders, or associated persons of the member;
- (I) effecting liquidating transactions only;
- (J) accepting only unsolicited customer orders; and
- (K) such other activities as FINRA deems appropriate under the circumstances in the public interest or for the protection of investors.

• • • **Supplementary Material:** — — — — —

.01. The following are examples of the conditions under which FINRA may exercise its discretion pursuant to paragraphs (b)(2) or (c)(2) above:

(a) The member has experienced a substantial change in the manner in which it processes its business, which, in the view of FINRA, increases the potential risk of loss to customers and other members;

(b) The member's books and records are not maintained in accordance with the provisions of SEA Rules 17a-3 and 17a-4;

(c) The member is not in compliance, or is unable to demonstrate compliance, with applicable net capital requirements;

(d) The member is not in compliance, or is unable to demonstrate compliance, with SEA Rule 15c3-3 (Customer Protection – Reserves and Custody of Securities);

(e) The member is unable to clear and settle transactions promptly; or

(f) The member's overall business operations are in such a condition, given the nature of its business that, notwithstanding the absence of any of the conditions enumerated in paragraphs (a) through (e), a determination of financial or operational difficulty should be made.

.02. The rule contemplates that any restrictions or conditions imposed on a carrying or clearing member's business under this Rule may require that member to restrict the business activities of one or more correspondent firms for which the member clears, insofar as such business would be handled by such carrying or clearing member.

Rule 4130. Regulation of Activities of Section 15C Members Experiencing Financial and/or Operational Difficulties

(a) Application — For purposes of this Rule, the term “member” shall be limited to any member of FINRA registered with the Commission pursuant to Section 15C of the Exchange Act that is not designated to another self-regulatory organization by the Commission for financial responsibility pursuant to Section 17 of the Exchange Act and SEA Rule 17d-1. Further, the term shall not be applicable to any member that is subject to Section 402.2(c) of the rules of the Treasury Department, or is otherwise exempt from the provisions of said rule.

(b) Each member subject to Section 402.2 of the rules of the Treasury Department shall comply with the capital requirements prescribed therein and with the provisions of this Rule.

(c) A member, when so directed by FINRA shall not expand its business during any period in which:

(1) Any of the following conditions continue to exist for more than 15 consecutive business days:

(A) the member’s liquid capital is less than 150 percent of the total haircuts or such greater percentage thereof as may from time to time be prescribed by FINRA;

(B) the member’s liquid capital minus total haircuts is less than 150 percent of its minimum dollar capital requirement; or

(C) the deduction of ownership equity and maturities of subordinated debt scheduled during the next six months would result in any one of the conditions described in (A) or (B) of this subparagraph (1); or

(2) FINRA restricts the member for any other financial or operational reason.

(d) A member, when so directed by FINRA, shall forthwith reduce its business:

(1) To a point at which the member would not be subject to a prohibition against expansion of its business as set forth in paragraphs (c)(1)(A), (B), or (C) of this Rule if any of the following conditions continue to exist for more than 15 consecutive business days:

(A) the member's liquid capital is less than 125 percent of total haircuts or such greater percentage thereof as may from time to time be prescribed by FINRA;

(B) the member's liquid capital minus total haircuts is less than 125 percent of its minimum dollar capital requirement; or

(C) the deduction of ownership equity and maturities of subordinated debt scheduled during the next six months would result in any one of the conditions described in (A) or (B) of this subparagraph (1); and

(2) As required by FINRA when it restricts a member for any other financial or operational reason.

(e) A member shall suspend all business operations during any period of time when the member is not in compliance with applicable liquid capital requirements as set forth in Section 402.2 of the rules of the Treasury Department. FINRA staff may issue a notice to such member directing it to suspend all business operations; however, the member's obligation to suspend all business operations arises from its obligations under Section 402.2 of the rules of the Treasury Department and is not dependent on any notice that may be issued by FINRA staff.

(f) Any notice directing a member to limit or suspend its business operations shall be issued by FINRA staff pursuant to FINRA Rule 9557.

Rule 4140. Audit

(a) FINRA's Executive Vice President charged with oversight for financial responsibility, or his or her written officer delegate, may at any time, due to concerns regarding the accuracy or integrity of a member's financial statements, books and records or prior audited financial statements, direct any member to cause an audit to be made by an independent public accountant of its accounts, or cause an examination to be made in accordance with attestation, review or consultation standards prescribed by the AICPA. Such audit or examination shall be made in accordance with such requirements as FINRA may prescribe.

(b) Any member failing to file an audited financial and/or operational report or examination report under this Rule in the prescribed time shall be subject to a late fee as set forth in Schedule A to the By-Laws.

* * * * *

Rule 4521. Notifications, Questionnaires and Reports

(a) Each carrying or clearing member or a member operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) shall submit to FINRA, or its designated agent, at such times as may be designated, or on an ongoing basis, in such form and within such time period as may be prescribed, such financial and operational information regarding the member or any of its correspondents as FINRA deems essential for the protection of investors and the public interest.

(b) Unless a specific temporary extension of time has been granted, there shall be imposed upon each member required to file reports pursuant to paragraph (a) of this Rule, a late fee as set forth in Schedule A to the By-Laws.

(c) For purposes of this Rule, any report filed pursuant to this Rule containing material inaccuracies shall be deemed not to have been filed until a corrected copy of the report has been resubmitted.

(d) Every member approved by the SEC pursuant to SEA Rule 15c3-1 to use the alternative method of computing net capital contained in Appendix E to that Rule shall file such supplemental and alternative reports as may be prescribed by FINRA.

(e) Each carrying or clearing member or a member operating pursuant to the exemptive provisions of SEA Rule 15c3-3(k)(2)(i) shall notify FINRA in writing, no more than 48 hours after its tentative net capital as computed pursuant to SEA Rule 15c3-1, has declined 20 percent or more from the amount reported in its most recent FOCUS Report or, if later, the most recent such notification filed with FINRA. For purposes of this paragraph, “tentative net capital as computed pursuant to SEA Rule 15c3-1” shall exclude withdrawals of capital previously approved by FINRA.

(f) (1) Unless otherwise permitted by FINRA in writing, members carrying margin accounts for customers are required to submit, on a settlement date basis, the information specified in paragraphs (f)(2)(A) and (f)(2)(B) of this Rule as of the last business day of the month. If a member has no information to submit, a report should be filed with a notation thereon to that effect. Reports are due as promptly as possible after the last business day of the month, but in no event later than the sixth business day of the following month. Members shall use such form as FINRA may prescribe for these reporting purposes.

(2) Each member carrying margin accounts for customers shall submit reports containing the following customer information:

(A) Total of all debit balances in securities margin accounts; and

(B) Total of all free credit balances in all cash accounts and all margin accounts.

(3) For purposes of this Rule:

(A) Only free credit balances in cash and margin accounts shall be included in the member's report. Balances in short accounts and in Special Memorandum Accounts (as defined in Section 2.2 of Regulation T under the Exchange Act) shall not be considered as free credit balances.

(B) Reported debit or credit balance information shall not include the accounts of other organizations that are FINRA members, or of the associated persons of the member submitting the report where such associated person's account is excluded from the definition of customer pursuant to SEA Rule 15c3-3.

* * * * *

9557. Procedures for Regulating Activities Under Rules 4110, [3130] 4120 and 4130 [3131] Regarding a Member Experiencing Financial or Operational Difficulties¹

(a) Notice of Requirements and/or Restrictions

FINRA [NASD] staff may issue a notice directing a member to comply with the provisions of Rule 4110, 4120 or 4130 or restrict its business activities, either by limiting or ceasing to conduct those activities consistent with Rule 4110, 4120 or 4130, if FINRA [NASD] staff has reason to believe that a condition specified in Rule 4110, 4120 [3130] or 4130 [Rule 3131] exists.

(b) Service of Notice

FINRA [NASD] staff shall serve the member subject to a notice issued under this Rule by facsimile, overnight courier or personal delivery. Papers served on a member by overnight courier or personal delivery shall conform to paragraphs (a)(1) and (3) and (b)(2) of Rule 9134. Papers served on a member by facsimile shall be sent to the facsimile number listed in the member's contact questionnaire submitted to FINRA [NASD] pursuant to Article 4, Section III of the FINRA [NASD's] By-Laws, except that, if FINRA [NASD] staff has actual knowledge that an entity's contact questionnaire facsimile number is out of date, duplicate copies shall be sent to the entity by overnight courier or personal delivery in conformity with paragraphs (a)(1) and (3) and (b)(2) of Rule 9134. Service is complete upon sending the notice by facsimile, mailing the notice by overnight courier or delivering it in person, except that, where duplicate service is required, service is complete upon sending the duplicate service.

(c) Contents of Notice

A notice issued under this Rule shall state the specific grounds and include the factual basis for the FINRA [NASD] action. The notice shall specify the nature of the requirements and/or restrictions being imposed, the effective date of the requirements and/or restrictions [state when the NASD action will take effect] and, where applicable, [explain what the respondent must do to avoid] the conditions for avoiding [such action] or terminating such requirements and/or restrictions. The notice shall state that the respondent may file a written request for a hearing with the Office of Hearing Officers pursuant to Rule 9559. The notice also shall inform the respondent of the applicable deadline for filing a request for a hearing and shall state that a request for a hearing must set forth with specificity any and all defenses to the FINRA [NASD] action.

¹ The draft text is marked to show changes between NASD Rule 9557 and proposed FINRA Rule 9557.

In addition, the notice shall explain that, pursuant to Rules 8310(a) and 9559(n), a Hearing Officer or, if applicable, Hearing Panel, may approve, modify or withdraw any and all requirements and/or restrictions [sanctions or limitations] imposed by the notice, and may impose any other fitting sanction.

(d) Effective Date of the Requirements and/or Restrictions

The requirements and/or restrictions referenced in a notice issued and served under this Rule are immediately effective. A timely request for a hearing shall stay the effective date for ten business days after service of the notice or until the Office of Hearing Officers issues a written order under Rule 9559(o)(4)(A) (whichever period is less), unless FINRA's Chief Executive Officer (or such other senior officer as the Chief Executive Officer may designate) determines that such a stay cannot be permitted with safety to investors, creditors or other members. Such a determination by the Chief Executive Officer (or such other senior officer as the Chief Executive Officer may designate) cannot be appealed. An extension of the stay period is not permitted. [The restrictions referenced in a notice issued and served under this Rule shall become effective seven days after service of the notice, unless stayed by a request for a hearing pursuant to Rule 9559.]

(e) Request for a Hearing

A member served with a notice under this Rule may file with the Office of Hearing Officers a written request for a hearing pursuant to Rule 9559. A request for a hearing shall be made within two business days after service of a notice under this Rule [before the effective date of the notice, as indicated in paragraph (d) of this Rule]. A request for a hearing must set forth with specificity any and all defenses to the FINRA [NASD] action.

(f) Failure to Request Hearing

If a member does not [timely] request a hearing within the time period specified in paragraph (e) of this Rule, [the] any requirements and/or restrictions [specified in the notice shall become effective seven days after service of the notice. The restrictions] specified in the notice shall remain in effect until the head of the FINRA [NASD] department or office that issued the notice or, if another FINRA [NASD] department or office is named as the party handling the matter on behalf of the issuing department or office, the head of the FINRA [NASD] department or office that is so designated, reduces or removes the requirements and/or restrictions pursuant to paragraph (h) of this Rule.

(g) [Order to] Enforcement of [Sanctions] Notice or Decision

[If NASD staff determines that a] A member that has failed to comply with any requirements and/or restrictions imposed by a decision or an effective notice under this Rule shall be automatically and immediately suspended [that have not been stayed, NASD staff shall issue an order imposing the sanctions set forth in the decision or notice and specifying the effective date and time of such sanctions]. The [order shall inform the] member [that it] may apply for relief from the suspension [sanctions imposed by the order] by filing a written request for a hearing before the Office of Hearing Officers under Rule 9559. The procedures delineated in this Rule shall be applicable, except that a request for a hearing regarding a suspension under this paragraph does not stay the effectiveness of the suspension.

(h) Additional Requirements and/or Restrictions or the Reduction or Removal of Requirements and/or Restrictions

(1) Additional Requirements and/or Restrictions

If a member continues to experience financial or operational difficulty specified in Rule 4110 or 4120 [3130] or 4130 [3131], notwithstanding an effective notice[, order] or decision under this Rule, FINRA [NASD] [S]staff may impose additional requirements and/or restrictions by [issuing] serving an additional notice under paragraph (b) of this Rule. The additional notice shall inform the member that it may apply for relief from the additional requirements and/or restrictions by filing a written request for a hearing before the Office of Hearing Officers under Rule 9559. The procedures delineated in this Rule shall be applicable to such [a] additional notice.

(2) Reduction or Removal of Requirements and/or Restrictions

If FINRA [NASD] staff determines that any requirements and/or restrictions previously imposed under this Rule should be reduced or removed, FINRA [NASD] staff shall serve a written notice on the member pursuant to Rule 9134.

(i) Notice to Membership

FINRA [NASD] shall provide notice of any final FINRA [NASD] action taken pursuant to this Rule in the next Regulatory Notice [to Members] Disciplinary and Other FINRA [NASD] Action Section.

* * * * *

9559. Hearing Procedures for Expedited Proceedings Under the Rule 9550 Series²

(a) Applicability

The hearing procedures under this Rule shall apply to a member, person associated with a member, person subject to FINRA's [NASD's] jurisdiction or other person who is served with a notice issued under the Rule 9550 Series and who timely requests a hearing. For purposes of this Rule, such members or persons shall be referred to as respondents.

(b) Computation of Time

Rule 9138 shall govern the computation of time in proceedings brought under the Rule 9550 Series, except that intermediate Saturdays, Sundays and Federal holidays shall be included in the computation in proceedings brought under Rules 9556 through 9558, unless otherwise specified.

(c) Stays

(1) Unless the Chief Hearing Officer or the Hearing Officer assigned to the matter orders otherwise for good cause shown, a timely request for a hearing shall stay the effectiveness of a notice issued under Rules 9551 through 9556[7], except that the effectiveness of a notice of a limitation or prohibition on access to services offered by FINRA [NASD] or a member thereof under Rule 9555 with respect to services to which the member or person does not have access shall not be stayed by a request for a hearing.

(2) A timely request for a hearing shall stay the effectiveness of a notice issued under Rule 9557 for ten business days after service of the notice or until the Office of Hearing Officers issues a written order under Rule 9559(o)(4)(A) (whichever period is less), unless FINRA's Chief Executive Officer (or such other senior officer as the Chief Executive Officer may designate) determines that a notice under Rule 9557 shall not be stayed. Where a notice under Rule 9557 is stayed by a request for a hearing, such stay shall remain in effect only for ten business days after service of the notice or until the Office of Hearing Officers issues a written order under Rule 9559(o)(4)(A) (whichever period is less) and shall not be extended.

(3) A timely request for a hearing shall not stay the effectiveness of a notice issued under Rule 9558, unless the Chief Hearing Officer or the Hearing Officer assigned to the matter orders otherwise for good cause shown.

² The draft text is marked to show changes between NASD Rule 9559 and proposed FINRA Rule 9559.

(d) Appointment and Authority of Hearing Officer and/or Hearing Panel

(1) For proceedings initiated under Rules 9553 and 9554, the Chief Hearing Officer shall appoint a Hearing Officer to preside over and act as the sole adjudicator for the matter.

(2) For proceedings initiated under Rules 9551, 9552, 9555, 9556, 9557 and 9558, the Chief Hearing Officer shall appoint a Hearing Panel composed of a Hearing Officer and two Panelists. The Hearing Officer shall serve as the chair of the Hearing Panel. For proceedings initiated under Rules 9551, 9552, 9555, 9556 and 9558, [T]he Chief Hearing Officer shall select as Panelists persons who meet the qualifications delineated in Rules 9231 and 9232. For proceedings initiated under Rule 9557, the Chief Hearing Officer shall select as Panelists current or former members of the FINRA Financial Responsibility Committee.

(3) Rules 9231(e), 9233 and 9234 shall govern disqualification, recusal or withdrawal of a Hearing Officer or, if applicable, Hearing Panelist.

(4) A Hearing Officer appointed pursuant to this provision shall have authority to do all things necessary and appropriate to discharge his or her duties as set forth under Rules 9235 and 9280.

(5) Hearings under the Rule 9550 Series shall be held by telephone conference, unless the Hearing Officer orders otherwise for good cause shown.

(6) For good cause shown, or with the consent of all of the parties to a proceeding, the Hearing Officer or, if applicable, the Hearing Panel may extend or shorten any time limits prescribed by this Rule other than those relating to Rule 9557.

(e) Consolidation or Severance of Proceedings

Rule 9214 shall govern the consolidation or severance of proceedings, except that, where one of the notices that are the subject of consolidation under this Rule requires that a hearing be held before a Hearing Panel, the hearing of the consolidated matters shall be held before a Hearing Panel. Where two consolidated matters contain different timelines under this Rule, the Chief Hearing Officer or Hearing Officer assigned to the matter has discretion to determine which timeline is appropriate under the facts and circumstances of the case. Where one of the consolidated matters includes an action brought under a Rule [9558] that does not permit a stay of the effectiveness of the

notice or where the Chief Executive Officer (or such other senior officer as the Chief Executive Officer may designate), in the case of Rule 9557, or Hearing Officer, in the case of Rule 9558(d), determines that a request for a hearing shall not stay the effectiveness of the notice, the limitation, prohibition, condition, requirement, restriction, or suspension specified in the notice shall not be stayed pending resolution of the case [unless the Chief Hearing Officer or Hearing Officer assigned to the matter orders otherwise for good cause shown. Where one of the consolidated matters includes an action brought under Rule 9555 with respect to services to which the member or person does not have access, the effectiveness of a notice of a limitation or prohibition on access to services offered by NASD or a member thereof shall not be stayed pending resolution of the case]. Where one of the consolidated matters includes an action brought under Rule 9557 that is stayed for up to ten business days, the requirement and/or restriction specified in the notice shall not be further stayed.

(f) Time of Hearing

(1) A hearing shall be held within five business days after a respondent subject to a notice issued under Rule 9557 files a written request for a hearing with the Office of Hearing Officers.

[(1)2] A hearing shall be held within 14 days after a respondent subject to a notice issued under Rules 9556 [through] and 9558 files a written request for a hearing with the Office of Hearing Officers.

[(2)3] A hearing shall be held within 60 days after a respondent subject to a notice issued under Rules 9551 through 9555 files a written request for a hearing with the Office of Hearing Officers.

[(3)4] The timelines established by paragraphs (f)(1) [and] through (f)([2)3] confer no substantive rights on the parties.

(g) Notice of Hearing

The Hearing Officer shall issue a notice stating the date, time, and place of the hearing as follows:

(1) At least two business days prior to the hearing in the case of an action brought pursuant to Rule 9557.

[(1)2] At least seven days prior to the hearing in the case of an action brought pursuant to Rules 9556 [through] and 9558, and

([2]3) At least 21 days prior to the hearing in the case of an action brought pursuant to Rules 9551 through 9555.

(h) Transmission of Documents

(1) Not less than two business days before the hearing in an action brought under Rule 9557, not less than seven days before the hearing in an action brought under Rules 9556 [through] and 9558, and not less than 40 days before the hearing in an action brought under Rules 9551 through 9555, FINRA [NASD] staff shall provide to the respondent who requested the hearing, by facsimile or overnight courier, all documents that were considered in issuing the notice unless a document meets the criteria of Rule 9251(b)(1)(A), (B) or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by FINRA [NASD] until the date upon which FINRA [NASD] serves a final decision or, if applicable, upon the conclusion of any review by the [Securities and Exchange Commission] SEC or the federal courts.

(2) Not less than two business days before the hearing in an action brought under Rule 9557, three days before the hearing in an action brought under Rules 9556 [through] and 9558, and not less than 14 days before the hearing in an action brought under Rules 9551 through 9555, the parties shall exchange proposed exhibit and witness lists. The exhibit and witness lists shall be served by facsimile or by overnight courier.

(i) Evidence

Formal rules of evidence shall not apply to a hearing under this Rule Series. Rules 9262 and 9263 shall govern testimony and the admissibility of evidence.

(j) Additional Information

The Hearing Officer or, if applicable, the Hearing Panel may direct the Parties to submit additional information.

(k) Record of Hearing

Rule 9265 shall govern the requirements for the record of the hearing.

(l) Record of Proceeding

Rule 9267 shall govern the record of the proceeding.

(m) Failure to Appear at a Pre-Hearing Conference or Hearing or to Comply with a Hearing Officer Order Requiring the Production of Information

Failure of any respondent to appear before the Hearing Officer or, if applicable, the Hearing Panel at any status conference, pre-hearing conference or hearing, or to comply with any order of the Hearing Officer or, if applicable, Hearing Panel requiring production of information to support any defense to the notice that respondent has raised, shall be considered an abandonment of the respondent's defense and waiver of any opportunity for a hearing provided by the Rule 9550 Series. In such cases, the notice issued under the Rule 9550 Series shall be deemed to be final FINRA [NASD] action. The Hearing Officer or, if applicable, the Hearing Panel may permit the hearing to go forward as to those parties who appear and otherwise comply with this Rule.

(n) Sanctions, Costs and Remands

(1) The Hearing Officer or, if applicable, the Hearing Panel may approve, modify or withdraw any and all sanctions, requirements, restrictions or limitations imposed by the notice. The Hearing Officer or, if applicable, the Hearing Panel also may impose any other fitting sanction, pursuant to Rule 8310(a).

(2) The Hearing Officer or, if applicable, the Hearing Panel may impose costs pursuant to Rule 8330.

(3) The Hearing Officer or, if applicable, the Hearing Panel may remand the matter to the department or office that issued the notice for further consideration of specified matters.

(o) Timing of Decision

(1) Proceedings initiated under Rules 9553 and 9554

Within 60 days of the date of the close of the hearing, the Hearing Officer shall prepare a proposed written decision and provide it to the National Adjudicatory Council's Review Subcommittee.

(2) Proceedings initiated under Rules 9556 [through] and 9558

Within 21 days of the date of the close of the hearing, the Hearing Officer shall prepare a proposed written decision that reflects the views of the Hearing Panel, as determined by majority vote, and provide it to the National Adjudicatory Council's Review Subcommittee.

(3) Proceedings initiated under Rules 9551, 9552 and 9555

Within 60 days of the date of the close of the hearing, the Hearing Officer shall prepare a proposed written decision that reflects the views of the Hearing Panel, as determined by majority vote, and provide it to the National Adjudicatory Council's Review Subcommittee.

(4) Proceedings initiated under Rule 9557

(A) Written Order

Within two business days of the date of the close of the hearing, the Office of Hearing Officers shall issue a written order that reflects the Hearing Panel's summary determinations, as decided by majority vote, and shall serve the Hearing Panel's written order on the Parties and provide a copy to each FINRA member with which the respondent is associated. The Hearing Panel's written order under Rule 9557 is effective when issued. The Hearing Panel's written order will be followed by a written decision explaining the reasons for the Hearing Panel's summary determinations, as required by paragraphs (o)(4)(B) and (p) of this Rule.

(B) Written Decision

Within seven days of the issuance of the Hearing Panel's written order, the Office of Hearing Officers shall issue a written decision that complies with the requirements of paragraph (p) of this Rule and shall serve the Hearing Panel's written decision on the Parties and provide a copy to each FINRA member with which the respondent is associated.

(5) If not timely called for review by the National Adjudicatory Council's Review Subcommittee pursuant to paragraph (q) of this Rule, the Hearing Officer's or, if applicable, the Hearing Panel's written decision shall constitute final FINRA [NASD] action. For decisions issued under Rules 9551 through 9556 and 9558, [T]the Office of Hearing Officers shall promptly serve the decision of the Hearing Officer or, if applicable, the Hearing Panel on the Parties and provide a copy to each FINRA [NASD] member with which the respondent is associated.

([5]6) The timelines established by paragraphs (o)(1)-([4]5) confer no substantive rights on the parties.

(p) Contents of Decision

The decision, which for purposes of Rule 9557 means the written decision issued under paragraph (o)(4)(B) of this Rule, shall include:

- (1) a statement describing the investigative or other origin of the notice issued under the Rule 9550 Series;
- (2) the specific statutory or rule provision[s that were] alleged to have been violated or providing the authority for the FINRA action;
- (3) a statement setting forth the findings of fact with respect to any act or practice the respondent was alleged to have committed or omitted or any condition specified in the notice;
- (4) the conclusions of the Hearing Officer or, if applicable, Hearing Panel regarding the alleged violation or condition specified in the notice [as to whether the respondent violated any provision alleged in the notice];
- (5) a statement of the Hearing Officer or, if applicable, Hearing Panel in support of the disposition of the principal issues raised in the proceeding; and
- (6) a statement describing any sanction, requirement, restriction or limitation imposed, the reasons therefore, and the date upon which such sanction, requirement, restriction or limitation shall become effective.

(q) Call for Review by the National Adjudicatory Council

(1) For proceedings initiated under the Rule 9550 Series (other than Rule 9557), [T]he National Adjudicatory Council's Review Subcommittee may call for review a proposed decision [issued] prepared by a Hearing Officer or, if applicable, Hearing Panel [under the Rule 9550 Series] within 21 days after receipt of the decision from the Office of Hearing Officers. For proceedings initiated under Rule 9557, the National Adjudicatory Council's Review Subcommittee may call for review a written decision issued under paragraph (o)(4)(B) of this Rule by a Hearing Panel within 14 days after receipt of the written decision from the Office of Hearing Officers. Rule 9313(a) is incorporated by reference.

(2) If the Review Subcommittee calls the proceeding for review within the prescribed time, a Subcommittee of the National Adjudicatory Council shall meet and conduct a review not later than 40 days after the call for review. The Subcommittee shall be composed pursuant to Rule 9331(a)(1). The Subcommittee may elect to hold a hearing or decide the matter on the basis of the record made before the Hearing Officer or, if applicable, the Hearing Panel. Not later than 60 days after the call for review, the Subcommittee shall make its recommendation to the National Adjudicatory Council. Not later than 60 days after receipt of the Subcommittee's recommendation, the National Adjudicatory Council shall serve a final written decision on the parties via overnight courier or facsimile. The National Adjudicatory Council may affirm, modify or reverse the decision of the Hearing Officer or, if applicable, the Hearing Panel. The National Adjudicatory Council also may impose any other fitting sanction, pursuant to Rule 8310(a), and may impose costs, pursuant to 8330. In addition, the National Adjudicatory Council may remand the matter to the Office of Hearing Officers for further consideration of specified matters.

(3) For good cause shown, or with the consent of all of the parties to a proceeding, the Review Subcommittee, the National Adjudicatory Council Subcommittee or the National Adjudicatory Council may extend or shorten any time limits prescribed by this Rule other than those relating to Rule 9557.

(4) The National Adjudicatory Council's written decision shall constitute final FINRA [NASD] action.

(5) The National Adjudicatory Council shall promptly serve the decision on the Parties and provide a copy of the decision to each FINRA [NASD] member with which the respondent is associated.

(6) The timelines established by paragraphs (q)(1)-(5) confer no substantive rights on the parties.

(r) Notice to Membership

FINRA [NASD] shall provide notice of any final FINRA [NASD] action in the next Regulatory Notice [to Members] Disciplinary and Other FINRA [NASD] Action Section.

(s) Application to Commission for Review

The right to have any action pursuant to this Rule reviewed by the [Securities and Exchange Commission] SEC is governed by Section 19 of the [Securities] Exchange Act. The filing of an application for review by the [Securities and Exchange Commission] SEC shall not stay the effectiveness of final FINRA [NASD] action, unless the [Securities and Exchange Commission] SEC otherwise orders.

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FINRA By-Laws Schedule A, Section 4

Section 4 — Fees

(a) through (f) No Change.

(g) (1) Unless a specific temporary extension of time has been granted, there shall be imposed upon each member required to file reports, as designated by this paragraph ("Designated Reports"), a fee of \$100 for each day that such report is not timely filed. The fee will be assessed for a period not to exceed 10 business days. Requests for such extension of time must be submitted to FINRA at least three business days prior to the due date; and

(2) Any report filed pursuant to this Rule containing material inaccuracies or filed incompletely shall be deemed not to have been filed until a corrected copy of the report has been resubmitted.

(3) List of Designated Reports:

(A) SEC Rule 17a-5 — Monthly and quarterly FOCUS reports and annual audit reports; [and]

(B) SEC Rule 17a-10 — Schedule I[.];

(C) FINRA Rule 4140 — any audited financial and/or operational report or examination report required pursuant to FINRA Rule 4140; and

(D) FINRA Rule 4521(a) — any financial or operational information or report required pursuant to FINRA Rule 4521(a).

(h) No Change.

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ATTACHMENT B

Proposed FINRA Rule #	Proposed FINRA Rule Requirement/Topic	Applies to...
4110	Capital Compliance	
4110 (a)	Authority to increase capital requirements	Carrying, clearing and (k)(2)(i) member firms
4110(b)	Suspension of business operations	All firms
4110(c)(1)	Withdrawal of equity capital	All firms
4110(c)(2)	Withdrawal of equity capital	Carrying, clearing and (k)(2)(i) member firms
4110(d)(1)(A)	Sale-and-leasebacks, factoring, financing, loans and similar arrangements	Carrying, clearing and (k)(2)(i) member firms
4110(d)(1)(B)	Sale-and-leasebacks, factoring, financing, loans and similar arrangements	Carrying member firms
4110(d)(2)	Sale-and-leasebacks, factoring, financing, loans and similar arrangements	Carrying, clearing and (k)(2)(i) member firms
4110(d)(3)	Sale-and-leasebacks, factoring, financing, loans and similar arrangements	Member firms subject to 4110(d)(1)(A), 4110(d)(1)(B) or 4110(d)(2)
4110(d)(4)	Sale-and-leasebacks, factoring, financing, loans and similar arrangements	All firms
4110(e)(1)	Subordinated loans, notes collateralized by securities and capital borrowing	All firms
4110(e)(2)	Subordinated loans, notes collateralized by securities and capital borrowing	All firms that are partnerships or LLCs whose LLC participant is granted rights analogous to a general partner in a partnership

Proposed FINRA Rule #	Proposed FINRA Rule Requirement/Topic	Applies to...
4120	Regulatory Notification and Business Curtailment	
4120(a)	Regulatory notification	Carrying, clearing and (k)(2)(i) member firms
4120(b)(1)	Restrictions on business expansion	Carrying, clearing and (k)(2)(i) member firms
4120(b)(2)	Restrictions on business expansion	All firms
4120(c)(1)	Reduction of business	Carrying, clearing and (k)(2)(i) member firms
4120(c)(2)	Reduction of business	All firms
4130	Regulation of Activities of Section 15C Members Experiencing Financial and/or Operational Difficulties	Certain firms subject to the Treasury Department's liquid capital requirements
4140	Audit	All firms
4521	Notifications, Questionnaires and Reports	
4521(a), (b) and (e)	Notifications, questionnaires and reports	Carrying, clearing and (k)(2)(i) member firms
4521(c)	Notifications, questionnaires and reports	All firms subject to 4521(a), (b), (d), (e) and (f)
4521(d)	Notifications, questionnaires and reports	Members subject to the SEC's requirements for broker-dealers that are part of consolidated supervised entities (approved to use Appendix E of SEA Rule 15c3-1 for computing net capital)
4521(f)	Notifications, questionnaires and reports	Firms carrying margin accounts