

Independent Verification of Assets

SEC Approves New FINRA Rule 4160 Relating to the Verification of Assets at a Non-Member Financial Institution

Effective Date: February 1, 2011

Executive Summary

Effective February 1, 2011, new FINRA Rule 4160 (Verification of Assets) prohibits a member, when notified by FINRA, from continuing to custody or retain record ownership of assets at a non-member financial institution, which, upon FINRA staff's request, fails promptly to provide FINRA with written verification of assets maintained by the member at such financial institution.¹ The text of FINRA Rule 4160 is set forth in Attachment A of this *Notice*.

Questions concerning this *Notice* should be directed to:

- Anand Ramtahal, Senior Vice President, Risk Oversight & Operational Regulation, at (646) 315-8565; or
- Matthew E. Vitek, Counsel, Office of General Counsel, at (202) 728-8156.

Background & Discussion

FINRA has adopted a rule to strengthen its ability to independently verify assets maintained by a member at a non-member financial institution. FINRA Rule 4160 prohibits a member, when notified by FINRA, from continuing to custody or retain record ownership of assets, whether such assets are proprietary or customer assets, at a non-member financial institution, which, upon FINRA's staff's request, fails promptly to provide FINRA with written verification of assets maintained by the member at such financial institution. At this time, FINRA is not requiring members to

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Notice Type

- New Rule

Suggested Routing

- Compliance
- Finance
- Legal
- Operations
- Senior Management

Key Topics

- Asset Transfers
- Asset Verification
- Custody
- Record Ownership

Referenced Rules & Notices

- SEA Rule 15c3-1
- SEA Rule 15c3-3

enter into written contracts with non-member financial institutions maintaining their proprietary or customer assets that would obligate the institutions to comply with FINRA staff's requests for verification; however, FINRA strongly encourages members to enter into such contracts. Irrespective of whether such a contract exists, FINRA Rule 4160 precludes a member, when notified by FINRA, from continuing to maintain assets at the financial institution and requires the member to transfer the assets to another financial institution.

FINRA Rule 4160(b) provides two exemptions from the rule. The rule does not apply to:

- ▶ proprietary assets of members that are treated as non-allowable assets under SEA Rule 15c3-1; or
- ▶ instances where FINRA determines that there is no independent custody or record ownership of the assets.

Supplementary Material .01 (Asset Transfers) to the rule sets forth that in the event a member is required to transfer its assets pursuant to the rule, the member shall effect such transfer in a reasonable period of time. Supplementary Material .02 (Member Obligations Under SEA Rule 15c3-3) to the rule clarifies that nothing in the rule shall be construed as altering in any manner a member's obligations under SEA Rule 15c3-3.

Endnotes

- 1 See Exchange Act Release No. 63044 (October 5, 2010), 75 FR 62911 (October 13, 2010) (Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1; File No. SR-FINRA-2010-042). See also Exchange Act Release No. 63383 (November 29, 2010), 75 FR 75529 (December 3, 2010) (Notice of Filing and Immediate Effectiveness of File No. SR-FINRA-2010-062 to Extend the Implementation Period for SR-FINRA-2010-042).

ATTACHMENT A

The following is the text of new Rule 4160.

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4000. FINANCIAL AND OPERATIONAL RULES

4100. FINANCIAL CONDITION

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4160. Verification of Assets

(a) A member, when notified by FINRA, may not continue to custody or retain record ownership of assets, whether such assets are proprietary or customer assets, at a financial institution that is not a member of FINRA, which, upon FINRA staff's request, fails promptly to provide FINRA with written verification of assets maintained by the member at such financial institution.

(b) The Rule shall not apply:

(1) to proprietary assets of members that are treated as non-allowable assets under SEA Rule 15c3-1; or

(2) in instances where FINRA determines that there is no independent custody or record ownership of the assets.

• • • Supplementary Material: -----

.01 Asset Transfers. Any member required to transfer its proprietary and/or customer assets pursuant to this Rule shall effect such transfer within a reasonable period of time.

.02 Member Obligations Under SEA Rule 15c3-3. Nothing in this Rule shall be construed as altering in any manner a member's obligations under SEA Rule 15c3-3.