Regulatory Notice 11-13

Sanction Guidelines

FINRA Revises Sanction Guidelines

Effective Immediately

March 2011

Executive Summary

FINRA has revised two sections of its *Sanction Guidelines*—the General Principles Applicable to All Sanctions Determinations and the Principal Considerations in Determining Sanctions—to reflect recent developments in FINRA disciplinary cases. Specifically, the revisions:

- clarify the causation standard for when FINRA adjudicators order restitution;
- recognize that FINRA adjudicators may order that a respondent's ill-gotten gains be paid to those injured by the respondent's misconduct, where appropriate;
- reflect that not every factor listed in the principal considerations has the potential to be aggravating and mitigating; and
- direct adjudicators to consider sanctions imposed by another regulator for the same misconduct when determining a sanction.

The revised *Sanction Guidelines* are effective immediately and available on FINRA's website at *www.finra.org/Industry/Enforcement/SanctionGuidelines*.

You may direct questions concerning this *Notice* to:

- Gary Dernelle, Office of General Counsel, at (202) 728-8255, and
- Jennifer Brooks, Office of General Counsel, at (202) 728-8083.

Notice Type

- Guidance

Key Topics

- FINRA Sanction Guidelines

Suggested Routing

- Legal
- Registered Representatives
- Senior Management

Financial Industry Regulatory Authority

Background & Discussion

The *FINRA Sanction Guidelines* address a wide variety of potential violations of FINRA's rules and provide fact-specific guidance for crafting sanctions. FINRA adjudicators rely on the guidelines to determine appropriate remedial sanctions, and FINRA's Departments of Market Regulation and Enforcement and the defense bar rely on them when negotiating settlements in disciplinary matters. In order to promote consistency in their application, the *Sanction Guidelines* outline certain General Principles Applicable to All Sanctions Determinations and the Principal Considerations in Determining Sanctions. These general principles and principal considerations enumerate certain factors for consideration in all cases. The National Adjudicatory Council approved the revisions to the general principles and principal considerations discussed below.

Revisions to General Principles Applicable to All Sanction Determinations

To address federal court, SEC and NAC precedent in recent FINRA disciplinary cases, FINRA amended the general principles concerning the use of restitution and disgorgement to remediate misconduct.

General Principle 5 of the *Sanction Guidelines* recognizes that FINRA adjudicators may order restitution where necessary to remediate misconduct. Restitution is a traditional remedy used to restore the status quo ante where a respondent's victim would otherwise unjustly suffer loss. General Principle 5 instructs adjudicators to calculate orders of restitution based on the actual amount of the loss sustained because of a respondent's misconduct. Such orders may thus exceed the amount of a respondent's ill-gotten gain.

As a result of a recent FINRA disciplinary matter, the SEC, upon remand from the United States Court of Appeals for the District of Columbia Circuit, requested that FINRA articulate the causation standard required under General Principle 5 when its adjudicators order restitution.[1] Revised General Principle 5 makes clear that "proximate causation" is the causation standard required for restitution orders in FINRA disciplinary proceedings.

General Principle 6 of the *Sanction Guidelines* instructs FINRA adjudicators to consider the disgorgement of a respondent's ill-gotten gain where the respondent has obtained a financial benefit from his wrongdoing. Disgorgement seeks to remediate misconduct by depriving a respondent of his or her unlawful profits irrespective of the actual losses suffered by the respondent's victims.

General Principle 6 traditionally recognized the ability of adjudicators to require the disgorgement of ill-gotten gains by fining away the amount of some or all of the financial benefit derived, directly or indirectly, through a respondent's misconduct. Although compensation of injured victims is not a primary purpose of disgorgement, the NAC and the SEC recognized that it nevertheless is a valid secondary purpose.[2] The amendments to General Principle 6 therefore reflect that FINRA adjudicators may order, where appropriate, the use of disgorged funds to remedy harms suffered by customers, rather than adding that amount of money as a fine payable to FINRA.

Revisions to Principal Considerations in Determining Sanctions

FINRA amended the introductory section of the Principal Considerations in Determining Sanctions to reflect that not every enumerated factor has the potential to be aggravating and mitigating.[3] The relevancy and characterization of a factor depends on the facts and circumstances of a case and the type of violation.[4]

Principal Consideration 14 directs adjudicators to consider whether individual respondents were disciplined by their firms for the misconduct before regulatory detection. FINRA amended Principal Consideration 14 to direct adjudicators also to consider sanctions imposed by another regulator, such as a state regulator, for the same misconduct and determine whether that sanction was sufficiently remedial.

Endnotes

1 *See Michael Frederick Siegel*, Exchange Act Rel. No. 62324, 2010 SEC LEXIS 2015, at *3 (June 18, 2010).

2 *See Dep't of Enforcement v. Mission Secs. Corp.,* Complaint No. 200600378501, 2010 FINRA Discip. LEXIS 1, at *47-48 (FINRA NAC Feb. 4, 2010), *aff'd,* Exchange Act Rel. No. 63453, 2010 SEC LEXIS 4053, at *54-55 (Dec. 7, 2010).

3 *See, e.g., Siegel v. SEC*, 592 F.3d 147, 157 (D.C. Cir. 2010) ("[N]ot every consideration listed in the [G]uidelines has the potential to be mitigating…" (internal quotation omitted)).

4 *See, e.g., Rooms v. SEC*, 444 F.3d 1208, 1214-15 (10th Cir. 2006) (explaining that while the existence of a disciplinary history is an aggravating factor when determining the appropriate sanction, its absence is not mitigating).