

OMB APPROVAL

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Required fields are shown with yellow backgrounds and asterisks.

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SECURITIES AND EXCHANGE COMMISSION
 WASHINGTON, D.C. 20549
 Form 19b-4

File No.* SR - 2011 - * 013

Amendment No. (req. for Amendments *)

Proposed Rule Change by Financial Industry Regulatory Authority
 Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * ☒ Amendment * ☐ Withdrawal ☐

Section 19(b)(2) * ☒ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Rule

Pilot ☐ Extension of Time Period
 for Commission Action * ☐ Date Expires *

☐ 19b-4(f)(1) ☐ 19b-4(f)(4)
☐ 19b-4(f)(2) ☐ 19b-4(f)(5)
☐ 19b-4(f)(3) ☐ 19b-4(f)(6)

Exhibit 2 Sent As Paper Document ☐

Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the proposed rule change (limit 250 characters, required when Initial is checked *).

Proposed Rule Change to Establish a Registration Category, Qualification Examination and Continuing Education Requirements for Certain Operations Personnel, and Adopt FINRA Rule 1250 (Continuing Education Requirements) in the Consolidated FINRA Rulebook

Contact Information

Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name * Erika Last Name * Lazar
 Title * Counsel
 E-mail * erika.lazar@finra.org
 Telephone * (202) 728-8013 Fax (202) 728-8264

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date 03/04/2011

By Patrice Gliniecki
 (Name *)

Senior Vice President and Deputy General Counsel

(Title *)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Patrice Gliniecki,

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EDFS website.

Form 19b-4 Information (required)

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change (required)

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

☐

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

☐

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”),¹ Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to adopt FINRA Rule 1230(b)(6) to establish a registration category and qualification examination requirement for certain operations personnel. The proposed rule change also would adopt continuing education requirements for such operations personnel and adopt NASD Rule 1120 (Continuing Education Requirements) as FINRA Rule 1250 (Continuing Education Requirements) in the consolidated FINRA rulebook with minor changes.

The text of the proposed rule change is attached as Exhibit 5 to this rule filing.

(b) Upon Commission approval and implementation by FINRA of the proposed rule change, NASD Rule 1120 will be eliminated from the current FINRA rulebook.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

At its meetings on February 11, 2009 and April 14, 2010, the FINRA Board of Governors authorized the filing of the proposed rule change with the SEC. No other action by FINRA is necessary for the filing of the proposed rule change.

FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 90 days following Commission approval. The implementation date will be no later than 240 days following Commission approval.

¹ 15 U.S.C. 78s(b)(1).

3. **Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

(a) Purpose

Background

Given the growing complexity of the financial services industry and the importance of services provided by personnel in operations departments, FINRA is concerned about the potential for regulatory gaps in the area of registration and education requirements for individuals performing and overseeing member operations functions. Historically, federal and state law and self-regulatory organization ("SRO") rules, including NASD Rules 1021 and 1031, have required that individuals engaged in or supervising the securities or investment banking business of a member firm be qualified and registered persons. These requirements generally have applied to, among others, individuals with customer contact providing advice (sales persons and investment bankers) or effecting securities transactions (traders) and their supervisors. However, unregistered individuals who perform and oversee member operations functions also play an integral role in the business of the firm, and their activities often have a meaningful connection to client funds, accounts and transactions. FINRA believes registration and education requirements for certain operations personnel are needed to help ensure that investor protection mechanisms are in place in all areas of a member's business that could harm the member, a customer, the integrity of the marketplace, or the public.

Proposal

As described in detail below, FINRA is proposing to expand its registration provisions to require registration of certain individuals ("covered persons") who are engaged in, responsible for or supervising certain member operations functions ("covered

functions”) to enhance the regulatory structure surrounding these areas. The proposed rule change would amend proposed FINRA Rule 1230 (Registration Categories) to adopt a new representative registration category and qualification examination for such individuals (“Operations Professionals”)² and would expand FINRA’s continuing education requirements to require that Operations Professionals be subject to Regulatory Element and Firm Element training.

Generally, covered persons would be those persons who are directly responsible for overseeing that tasks within the covered functions are performed correctly in accordance with industry rules, firm protocols, policies and procedures, and who are charged with protecting the functional and control integrity of the covered functions for a member. Only persons who are both “covered persons” (i.e., meet the depth of personnel criteria as discussed in Section A. below) and conduct activities or functions in one or more of the “covered functions” (discussed in Section B. below) would be subject to the new Operations Professional registration category.

A. Covered Persons for Inclusion in the New Registration Category

The proposed rule change would require the following covered persons to register with FINRA as an Operations Professional:

- (1) Senior management with responsibility over the covered functions;
- (2) Supervisors, managers or other persons responsible for approving or authorizing work, including work of other persons, in direct furtherance of the covered functions; and

² See Regulatory Notice 09-70 (December 2009) (FINRA Requests Comment on Proposed Consolidated FINRA Rules Governing Registration and Qualification Requirements). The proposed amendments discussed in this Notice would be included in proposed FINRA Rule 1230 (Registration Categories).

- (3) Persons with the authority or discretion materially to commit a member's capital in direct furtherance of the covered functions or to commit a member to any material contract or agreement (written or oral) in direct furtherance of the covered functions.

Persons who perform a covered function, but whose responsibilities are below these specified levels, would not be required to register as Operations Professionals. Members must determine, based on a person's activities and responsibilities, whether such person would be considered a covered person and subject to the proposed requirements for Operations Professionals. A person's job title may not be clearly indicative of his or her obligation to register as an Operations Professional.

For the purpose of the proposed third category of covered persons, any person who has the authority or discretion materially to commit firm capital in direct furtherance of the covered functions or commit a firm to a material contract or agreement in direct furtherance of the covered functions would be required to register as an Operations Professional. As proposed in supplementary material .06 (Scope of Operations Professional Requirement), the determination as to what constitutes "materially" or "material" would be based on a member's pre-established spending guidelines and risk management policies. Generally, persons who do not have the authority or discretion to commit a member's capital, or to commit a member to a contract or agreement, above such pre-established spending guidelines and risk management policies would not be subject to registration as an Operations Professional under this provision.

Additionally, proposed supplementary material .06 would provide that any person whose activities are limited to performing a function ancillary to a covered function, or

whose function is to serve a role that can be viewed as supportive of or advisory to the performance of a covered function, or who engages solely in clerical or ministerial activities in a covered function would not be required to register as an Operations Professional pursuant to paragraph (b)(6)(A) of the proposed rule. For example, internal audit, legal or compliance personnel who review but do not have primary responsibility for any covered function would not be required to register as an Operations Professional.

Consistent with FINRA guidance, persons subject to the new Operations Professional registration category would be considered associated persons of a member irrespective of their employing entity, and would be subject to all FINRA rules applicable to associated persons and/or registered persons.³ Moreover, any person who meets the depth of personnel criteria described above in Section A. and is engaged in one or more covered functions would be required to register as an Operations Professional. The proposed rule change does not alter the status of covered persons as associated persons of a member insofar as they are performing regulated broker-dealer functions on behalf of the member. Rather, the proposed rule change explicitly imposes registration, qualification examination and continuing education requirements on such persons.

³ See Notice to Members 05-48 (July 2005) (Members' Responsibilities When Outsourcing Activities to Third-Party Service Providers). The Notice reminds members that "in the absence of specific NASD [or FINRA] rules, MSRB rules, or federal securities laws or regulations that contemplate an arrangement between members and other registered broker-dealers with respect to such activities or functions (e.g., clearing agreements executed pursuant to NASD Rule 3230), any third-party service providers conducting activities or functions that require registration and qualification under NASD [or FINRA] rules will generally be considered associated persons of the member and be required to have all necessary registrations and qualifications."

B. Covered Functions for Inclusion in the New Registration Category

Any person who meets the threshold in one of the three categories of covered persons identified above in Section A. who conducts activities or functions for a member in one or more of the following covered functions would be required to register as an Operations Professional:

- (1) Client on-boarding (customer account data and document maintenance);
- (2) Collection, maintenance, re-investment (i.e., sweeps) and disbursement of funds;
- (3) Receipt and delivery of securities and funds, account transfers;
- (4) Bank, custody, depository and firm account management and reconciliation;
- (5) Settlement, fail control, buy ins, segregation, possession and control;
- (6) Trade confirmation and account statements;
- (7) Margin;
- (8) Stock loan/securities lending;
- (9) Prime brokerage (services to other broker-dealers and financial institutions);
- (10) Approval of pricing models used for valuations;
- (11) Financial control, including general ledger and treasury;
- (12) Contributing to the process of preparing and filing financial regulatory reports;
- (13) Defining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements;
- (14) Defining and approving business security requirements and policies for information technology, including, but not limited to, systems and data, in connection with the covered functions;

(15) Defining and approving information entitlement policies in connection with the covered functions; and

(16) Posting entries to a member's books and records in connection with the covered functions to ensure integrity and compliance with the federal securities laws and regulations and FINRA rules.

The proposed rule change would include persons engaged in or supervising stock loan/securities lending activities that meet the depth of personnel as a covered person in Section A. above. FINRA also is proposing separate registration categories for a "Securities Lending Representative" and a "Securities Lending Supervisor."⁴

C. Operations Professional Qualification Examination

The proposed rule change would establish a new qualification examination for Operations Professionals that would provide reasonable assurance that such individuals understand their professional responsibilities, including key regulatory and control themes, as well as the importance of identifying and escalating red flags that may harm a member, a customer, the integrity of the marketplace, or the public.⁵ So that applicants

⁴ In Regulatory Notice 09-70, FINRA generally proposes to adopt the NYSE registration requirements for Securities Lending Representatives and Securities Lending Supervisors, requiring an associated person who has discretion to commit a member to any contract or agreement (written or oral) involving securities lending or borrowing activities with any other person, and the direct supervisor of the associated person to register as a Securities Lending Representative and Securities Lending Supervisor, respectively. These individuals would be required to register as such for tracking and oversight purposes, regardless of whether they are registered in other categories. However, solely for purposes of registering as a Securities Lending Representative or Securities Lending Supervisor, an individual will not be subject to a qualification examination at this time.

⁵ Any individual whose activities go beyond those proposed for the Operations Professional registration category would be required to separately qualify and

understand that they are functioning in a heavily regulated industry, the proposed Operations Professional qualification examination would test applicants on general securities industry knowledge and its associated regulations and rules. Subject to the proposed exception in Section D. below, any person required to register as an Operations Professional would be required to pass the Operations Professional qualification examination before such registration may become effective.

In general, given the diversity of functions performed by covered persons, the proposed Operations Professional qualification examination would be a principles-based qualification examination with a regulatory focus to test for a broad understanding of a broker-dealer's business at a basic level, a basic understanding of the operations functions that support a broker-dealer's business and the regulations designed to achieve investor protection and market integrity that drive the operations processes and procedures conducted at a broker-dealer. As further detailed in Section E. below, the continuing education components associated with the Operations Professional registration category would provide competency training specific to the covered functions, as applicable.

The breadth and depth of coverage of the qualification examination would be determined through the use of testing industry standards used to develop examinations, and would include input and advice from covered persons active in the securities industry. The following are the proposed key content themes of the new Operations Professional qualification examination:

register in the appropriate category or categories of registration attendant to such activities.

➤ Professional Conduct and Ethical Considerations: This section of the examination would assess a candidate's core knowledge addressed on other FINRA examinations that are appropriate for an Operations Professional. The questions would assess knowledge of what are considered serious violations of securities industry rules. This section would include ethics-based questions that address issues such as data integrity, escalation of regulatory red flags and separation of duties.

➤ Essential Product and Market Knowledge for an Operations Professional: This section of the examination would assess a candidate's basic product and market knowledge, including definitions and characteristics of major product categories (i.e., equities, debt, packaged securities, options and markets). An Operations Professional would not be expected to know the same level of detail about the products and markets as a product specialist or a representative selling products to customers.

➤ Knowledge Associated with Operations Activities: This section of the examination would assess a candidate's broad-based knowledge regarding the covered functions outlined above that support a broker-dealer's business and the underlying rules that drive the processes associated with these activities (i.e., customer account set-up and transfers, recordkeeping requirements, rules associated with the protection of customer assets and transaction processing, uniform practices associated with making good delivery of securities, making payments for securities and meeting settlement requirements, and credit and margin rules). This section of the examination also would include ethics-based questions in the context of operations activities.

D. Exception to Operations Professional Examination Requirement

The proposed rule change would include an exception to the Operations Professional qualification examination requirement for persons who currently hold certain registrations (each an “eligible registration”) or have held one during the two years immediately prior to registering as an Operations Professional. The proposed exception also would apply to persons who do not hold an eligible registration, but prefer an alternative to taking the Operations Professional examination. Such persons would be permitted to register in an eligible registration category (subject to passing the corresponding qualification examination or obtaining a waiver) and use such registration to qualify for Operations Professional registration.

A person who wishes to obtain Operations Professional registration under the proposed exception would not be automatically waived-in, but would have to opt-in by requesting Operations Professional registration via Form U4 (the Uniform Application for Securities Industry Registration or Transfer) in the Central Registration Depository (“CRD®”).⁶ If there are no other deficiencies (e.g., fingerprints), the Operations Professional registration would be approved automatically at the time such request is made. Information regarding the proposed implementation period is discussed in detail in Section F. below. FINRA would not assess a separate registration fee for persons relying on the proposed exception to register as Operations Professionals.

FINRA conducted a review of the content outlines for each qualification examination it recognizes and identified examinations with broad content coverage that

⁶ A person who qualifies for the proposed exception based on their having held an eligible registration within the two years immediately prior to registering as an Operations Professional would be required to first re-activate such eligible registration prior to requesting Operations Professional registration.

would be eligible for an exception to the Operations Professional examination requirement. Accordingly, persons who hold the following representative-level registration categories, or who have held such registration categories within the two years immediately prior to registering as an Operations Professional, would be qualified to register as an Operations Professional without passing the Operations Professional qualification examination:

- Investment Company Products/Variable Contracts Representative (Series 6)
- General Securities Representative (Series 7)
- United Kingdom Securities Representative (Series 17) or Canada Securities Representative (Series 37 or 38)

Additionally, persons who hold (or have held) certain principal-level registration categories would be qualified to register as an Operations Professional without passing the Operations Professional examination. Most principal-level qualification examinations have a prerequisite examination requirement that is satisfied with one of the representative qualification examinations listed above; however, FINRA also proposes to include principal-level qualification examinations that do not have a prerequisite, or have a prerequisite that can be met with a qualification examination not on the above list (e.g., Series 62), because it is likely such principals are familiar with the content to be covered in the Operations Professional qualification examination as a result of the requirements of their positions. Specifically, persons who hold the following principal-level registration categories, or who have held such registration categories within the two years immediately prior to registering as an Operations Professional, would be qualified to

register as an Operations Professional without passing the Operations Professional qualification examination:

- Registered Options Principal (Series 4)
- General Securities Sales Supervisor (Series 9/10)
- Compliance Officer (Series 14)
- Supervisory Analyst (Series 16)
- General Securities Principal (Series 24)
- Investment Company Products/Variable Products Principal (Series 26)
- Financial and Operations Principal (Series 27)
- Introducing Broker-Dealer Financial and Operations Principal (Series 28)
- Municipal Fund Securities Limited Principal (Series 51)
- Municipal Securities Principal (Series 53)

The proposed exception would not apply to persons whose eligible registrations are revoked pursuant to FINRA Rules 8310 (Sanctions for Violation of the Rules) or 8320 (Payment of Fines, Other Monetary Sanctions, or Costs; Summary Action for Failure to Pay), suspended or otherwise deemed inactive.⁷

FINRA notes that covered persons are generally acting in a supervisory position, so many persons will already hold one of the eligible registrations that would qualify for

⁷ If a person's registration in an eligible registration category was revoked within the prior two years, but such person re-qualifies and re-registers in such eligible registration category, he or she may rely on this eligible registration to qualify for the exception to the Operations Professional qualification examination requirement. Further, a suspended registration may not be relied upon as an eligible registration during the suspension period. Similarly, a registration deemed inactive for any reason (e.g., failure to complete continuing education requirements) may not be relied upon as an eligible registration during such inactive period. See also FINRA Rule 8311 (Effect of a Suspension, Revocation, Cancellation, or Bar).

the exception to the Operations Professional examination requirement. As noted in Section A. above, entry-level operations personnel would not typically be subject to the proposed requirements for Operations Professionals.

E. Continuing Education Requirements for Operations Professionals

The proposed rule change would require that individuals registered as Operations Professionals be subject to FINRA's Regulatory Element and Firm Element continuing education requirements as set forth in proposed FINRA Rule 1250 (Continuing Education Requirements).⁸ The continuing education elements for this registration category would provide more specific learning materials appropriate for an Operations Professional, given the breadth of functions that are covered by this registration requirement.

The Regulatory Element program for Operations Professionals would provide instruction for Operations Professionals to: (1) maintain and improve understanding of the regulatory and ethical aspects associated with the covered functions; (2) identify suspicious activities and/or red flags that could harm a customer, a firm, issuers of securities or the integrity of the marketplace; (3) maintain and improve knowledge and understanding of the covered functions; and (4) assist the Operations Professionals in keeping up with changes in the industry and regulations that impact their work.

Operations Professionals would be required to complete scenario-based modules based on the key content themes of the Operations Professional qualification examination, as described in Section C. above. The breadth and depth of coverage of the modules would be determined through the use of existing industry standards currently used to develop continuing education content and would include input and advice from

⁸ See Section G. for further discussion of the adoption of NASD Rule 1120 (Continuing Education Requirements) as FINRA Rule 1250.

operations professionals active in the securities industry. Individuals would be expected to complete the Regulatory Element continuing education requirement two years after passing the qualification examination and then every three years thereafter.

Individuals who avail themselves of the proposed exception to the Operations Professional qualification examination requirement with an eligible registration described above would be subject to the Regulatory Element program appropriate for such other registration category. For example, a person who registers as an Operations Professional by holding a General Securities Representative registration (Series 7) under the exception would be subject to the S101 continuing education program in lieu of the Operations Professional Regulatory Element training, and a person who registers by holding a General Securities Principal registration (Series 24) would be subject to the S201 continuing education program in lieu of the Operations Professional Regulatory Element training.

Operations Professionals also would be subject to Firm Element training. To implement this change, as further discussed in Section G. below, the proposed rule change would include Operations Professionals in the definition of “covered registered persons” in proposed FINRA Rule 1250, and would require that firms deliver Firm Element training to Operations Professionals subject to the new registration and qualification requirements.⁹

⁹ NASD Rule 1120(b) (Continuing Education Requirements) is currently limited to registered persons who have direct contact with customers in the conduct of the firm’s securities sales, trading and investment banking activities, any person registered as a research analyst pursuant to NASD Rule 1050, and to the immediate supervisors of such persons. The proposed amendments are reflected in the new FINRA rule governing continuing education, FINRA Rule 1250, which is being proposed as part of this rule change. See Section G. below.

F. Implementation of the Proposed Rule Change

As noted above, any person who meets the depth of personnel criteria described in Section A. and is engaged in one or more covered functions described in Section B. would be required to register with FINRA as an Operations Professional. Such persons would be required to register by doing one of the following, as applicable: (1) requesting Operations Professional registration via Form U4 in CRD and passing the Operations Professional qualification examination; (2) requesting Operations Professional registration via Form U4 in CRD and opting in to such registration based on their holding, or having held within the past two years, an eligible registration;¹⁰ or (3) requesting Operations Professional registration via Form U4 in CRD, registering with FINRA in an eligible registration category and opting in to Operations Professional registration based on such eligible registration.¹¹

Members must identify persons required to register as an Operations Professional as of the effective date of the proposed rule change (“Day-One Professionals”) (i.e.,

¹⁰ Persons with an active eligible registration who request Operations Professional registration will be automatically granted Operations Professional registration once they submit such request via Form U4 in CRD, regardless of when such persons apply for Operations Professional registration (provided there are no existing deficiencies). See also supra note 6.

¹¹ If a person elects to register with FINRA as an Operations Professional by newly qualifying in an eligible registration (i.e., does not have an active eligible registration when he or she requests Operations Professional registration via Form U4 in CRD), such person must contact FINRA upon passing the alternative examination to request that the eligible registration be applied to the request for Operations Professional registration. This would include, for example, a person who requests both the Operations Professional and General Securities Representative registrations via Form U4 in CRD and passes the Series 7 examination. Such person would be required to contact FINRA to alert FINRA staff that the General Securities Representative registration will be used as an eligible registration to qualify as an Operations Professional.

persons who meet the depth of personnel criteria and are engaged in one or more covered functions as of the effective date of the proposed rule change). FINRA is proposing a 60-day identification period beginning on the effective date of the proposed rule change during which Day-One Professionals must request registration as an Operations Professional via Form U4 in CRD. During this 60-day period, a Day-One Professional may function in the capacity of an Operations Professional. Day-One Professionals who are identified during the 60-day period and must pass the Operations Professional examination (or an eligible qualification examination) to qualify (i.e., persons who do not hold, and have not within the past two years held, an eligible registration) would be granted 12 months beginning on the effective date of the proposed rule change to pass such qualifying examination, during which time such persons may function as an Operations Professional.¹² To be eligible to function as an Operations Professional for the 12-month transition period, Day-One Professionals subject to an examination requirement must request Operations Professional registration via Form U4 in CRD during the 60-day identification period and pass the Operations Professional examination (or an eligible qualification examination) before the expiration of 12 months from the effective date of the proposed rule change.¹³ If a Day-One Professional does not pass an

¹² When a person requests Operations Professional registration via Form U4 in CRD during the 60-day identification period, an examination window for the Operations Professional qualification examination will open in CRD that expires 12 months from the effective date of the proposed rule change. After the 60-day identification period, the examination window for the Operations Professional qualification examination will open for the standard 120 days.

¹³ Members should note that the standard examination window in CRD applicable to a particular registration category will apply notwithstanding the 12-month examination window established for purposes of the transition period. The 12-month examination window is only for the Operations Professional qualification examination. Thus, a person who elects to qualify, for example, by passing the

acceptable examination by the expiration of the 12-month transition period, such person must cease functioning as an Operations Professional.

The 12-month transition period to pass a qualification examination would only apply to Day-One Professionals. Any person who is not subject to the registration requirements for Operations Professionals as of the effective date of the proposed rule change (i.e., a person who does not meet the depth of personnel criteria and/or is not engaged in one or more covered functions as of the effective date, or persons hired after the effective date of the proposed rule change who will be placed in such roles) (“non-Day-One Professionals”) would be required to register as an Operations Professional and, if applicable, pass the Operations Professional qualification examination (or an eligible qualification examination), prior to engaging in any activities that would require such registration. The 60-day identification period and the 12-month transition period do not affect the obligations of non-Day-One Professionals to register as an Operations Professional prior to engaging in functions that would require such registration. However, any non-Day-One Professional associated with a non-clearing member who must pass the Operations Professional qualification examination (or an eligible qualification examination) to obtain registration would be granted a grace period of 120 days beginning on the date such person requests Operations Professional registration via Form U4 in CRD to pass such qualifying examination, during which time such person may function as an Operations Professional. FINRA believes that allowing a person

Series 7 examination would have only 120 days to take and pass the Series 7 examination once the window for such examination is opened in CRD. Members should plan accordingly so that associated persons are prepared to take the requisite examination within the prescribed window for that registration category, and that any requisite examination is passed before the expiration of the 12-month transition period for Day-One Professionals.

associated with a non-clearing member to function as an Operations Professional for a 120-day period will enable these firms to manage their more limited staffs to comply with the proposed registration requirements without disrupting those firms' obligations to customers. Non-Day-One Professionals associated with a self-clearing or clearing member would not have the benefit of the 120-day grace period and would be required to register as an Operations Professional prior to engaging in activities that would require such registration.

Members would be responsible for tracking and monitoring their associated persons to ensure that such persons are registered, and conducting their activities, in compliance with the time frames described above.

G. FINRA Continuing Education Rule

The proposed rule change would adopt NASD Rule 1120 (Continuing Education Requirements) as new FINRA Rule 1250 (Continuing Education Requirements). In addition to the proposed change noted in Section E., which would expand the scope of "covered registered persons" subject to the Firm Element to include persons registered as Operations Professionals, the proposed rule change would make additional minor changes to NASD Rule 1120 to update cross-references and reflect the conventions of the consolidated FINRA Rulebook.

NASD Rule 1120 and Incorporated NYSE Rule 345A were adopted in 1995 in response to the recommendation of a task force, which subsequently became the Securities Industry Regulatory Council on Continuing Education (the "Council"),¹⁴ to

¹⁴ The Council is comprised of up to 16 industry members from broker-dealers, representing a broad cross section of industry firms, and representatives from SROs as well as liaisons from the SEC and the North American Securities Administrators Association ("NASAA").

create uniform continuing education requirements in the securities industry. As advised by the Council, the continuing education requirements include a Regulatory Element and a Firm Element. The NASD and Incorporated NYSE rules are nearly identical in keeping with the goals of the Council to create uniform continuing education requirements.¹⁵

The Regulatory Element consists of periodic computer-based training on regulatory, compliance, ethical, supervisory subjects and sales practice standards. A registered person is required to participate and complete a designated Regulatory Element within a 120-day period that commences with the second anniversary of such person's initial securities registration, and reoccurs every three years thereafter for as long as such person remains in the securities business. Failure to complete the Regulatory Element will result in a registered person's registration becoming inactive and such person cannot conduct a securities business on behalf of the member until the requirement is met.¹⁶

The Firm Element requirements currently apply to any person registered with a member who has direct contact with customers in the conduct of the member's securities sales, trading and investment banking activities, any person registered as a research analyst pursuant to NASD Rule 1050, and to the immediate supervisors of such persons (collectively, "covered registered persons"). However, as noted above, the proposed rule

¹⁵ The proposed rule change would not delete Incorporated NYSE Rule 345A (and its Interpretation). Rather, FINRA expects to address Incorporated NYSE Rule 345A (and its Interpretation) and propose additional changes to proposed FINRA Rule 1250 as part of the consolidated registration and qualification rules. See Regulatory Notice 09-70 (December 2009).

¹⁶ A registered person will be required to retake the Regulatory Element in the event such person is: (1) subject to a statutory disqualification as defined by Section 3(a)(39) of the Exchange Act; (2) subject to a suspension or imposition of a fine of \$5,000 or more by an SRO or other securities governmental agency; or (3) ordered to do so as a sanction in a disciplinary action by an SRO or other securities governmental agency.

change would expand the scope of “covered registered persons” subject to the Firm Element to include persons registered as Operations Professionals. The Firm Element consists of annual, member-developed and administered training programs designed to keep covered registered persons current regarding securities products, services and strategies offered by the member. The Firm Element requires members to annually evaluate and prioritize their training needs (i.e., conduct a Needs Analysis and develop a written plan). In planning, developing and implementing the Firm Element training, each member must take into consideration its size, organizational structure, scope of business, types of products and services it offers, as well as regulatory developments and the performance of its covered registered persons in the Regulatory Element. FINRA may require a member to provide specific training to a member’s covered registered persons as FINRA deems appropriate. Each member must administer its Firm Element Continuing Education Program in accordance with its annual Needs Analysis and written plan, and must maintain records documenting the content of the program and completion of the program by covered registered persons.

As noted in Item 2 of this filing, FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 90 days following Commission approval. The implementation date will be no later than 240 days following Commission approval.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹⁷ which requires, among other things, that FINRA rules

¹⁷ 15 U.S.C. 78o-3(b)(6).

must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes the proposed rule change to expand FINRA's registration and continuing education requirements to Operations Professionals will help ensure that investor protection mechanisms are in place in all areas of a member's business that could harm the member, a customer, the integrity of the marketplace, or the public.

4. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The proposed rule change was published for comment in Regulatory Notice 10-25 (May 2010) (the "Notice"). Forty-nine comment letters were received in response to the Notice.¹⁸ A copy of the Notice is attached as Exhibit 2a. A list of the comment letters received in response to the Notice is attached as Exhibit 2b. Copies of the comment letters received in response to the Notice are attached as Exhibit 2c. Below is a summary of the comments and FINRA's responses.

General Concerns Regarding the Scope of the New Registration Category

Certain commenters generally opposed the proposed rule change stating that it is overly broad and ambiguous, poorly defined, imposes requirements that are unnecessary

¹⁸ All references to the commenters under this Item are to the commenters as listed in Exhibit 2b.

to meet FINRA’s stated objectives and may have unintended consequences.¹⁹ Other commenters argued that licensing requirements do not make people honest or increase their efficiency or proficiency²⁰ and that no amount of licensing will change failures of human character.²¹ Two commenters noted that frauds are almost always committed on the frontlines by individuals who are already licensed.²² Additionally, certain commenters opposed registration requirements for covered persons because their work is already supervised and approved by a firm principal²³ and holding principals accountable for failures in these areas would be more cost effective.²⁴ Numerous commenters proposed an alternative approach under which firms would delegate each of the covered functions to existing registered principals of the firm and reflect such assignments in the firm’s written supervisory procedures (“WSPs”).²⁵ Other commenters noted the proposed rule change is unnecessary because people who handle customer funds go through background checks and fingerprinting.²⁶

¹⁹ ACLI, AIC, Bank of America, Crowell, ESI, Horace Mann, IPA, IRI, Modern Woodmen, Navidar, NSCP, PSD, Quasar, UPFS, Scottrade, SIFMA, Sutherland, TIAA, Wellington and Wells Fargo.

²⁰ Mutual Trust.

²¹ AIC and Wells Fargo.

²² AIC and PSD.

²³ Crowell, IRI, M. Griffith, PSD and RiverStone.

²⁴ Crowell and Wellington.

²⁵ IRI, Nationwide, PSD and Sutherland.

²⁶ PSD, RiverStone and Wells Fargo.

In response, FINRA notes that covered persons are performing regulated broker-dealer functions on behalf of a member, and believes such persons should be subject to registration, examination and continuing education requirements to ensure that they attain and maintain specified levels of competence and knowledge to properly carry out their responsibilities to the member and its customers. FINRA does not agree that principal approval or background checks and fingerprinting are sufficient safeguards to ensure members' operations departments are functioning in a manner that will promote investor protection to the highest level possible. The proposed rule change is intended, among other things, to increase covered persons' awareness and knowledge that they are operating in a regulated environment designed to protect investors' interests and the integrity of the operations of a broker-dealer. In addition, the proposed rule will help to ensure that any fraudulent activity that may start in the front office of a firm cannot be processed without passing through a properly registered and trained Operations Professional. Requiring registration, testing and training for Operations Professionals should further strengthen members' compliance with securities laws, rules and regulations.

Certain commenters expressed concern that requiring registration of covered persons will dramatically limit the pool of candidates that may be considered for hiring when personnel changes occur in operations departments.²⁷ As an initial matter, FINRA notes that it is always correct to state that conduct once regulated becomes constrained by that regulation, but that observation by itself is not a credible reason not to engage in the regulation. The proper test is whether that regulation is appropriately tailored and needed

²⁷ NPB and RiverStone.

in furtherance of the interests of investors and the securities markets. The immediate prior paragraph restates those interests, and the depth of personnel as set forth in Section A. of the Purpose section demonstrates the appropriate tailoring of the proposed regulation. Finally, Section D. of the Purpose section indicates that many candidates for positions that would require registration may possess an eligible registration and qualify for an exception from the requirement to take the Operations Professional qualification examination.

Two commenters suggested FINRA reduce the obligations for Operations Professionals and specify that not all of the rules applicable to associated persons apply to such persons since they are generally not customer-facing personnel.²⁸ Certain other commenters sought clarification that the proposed rule change does not eliminate or limit the ability of a securities issuer and its associated persons to rely on the issuer exemption under Exchange Act Rule 3a4-1²⁹ to avoid broker-dealer registration requirements.³⁰ Another commenter requested that FINRA provide guidance on the impact of the proposed rule change on FINRA Rule 2310 (Direct Participation Programs) and clearly state that the salaries of Operations Professionals be categorized as “non-transaction-based-compensation” and that there is a blanket exception from “underwriting compensation” for Operations Professionals.³¹

²⁸ TIAA and Wells Fargo.

²⁹ 17 CFR § 240.3a4-1.

³⁰ PSD, Sutherland and TIAA.

³¹ IPA.

FINRA does not agree that Operations Professionals should be subject to a limited set of rules. Covered persons are not only associated persons of a member but their activities are crucial enough to the business of a member to require registration with FINRA. The proposed rule change does not alter a person's status as an associated person under Exchange Act Rule 3a4-1 or otherwise, nor does it address the definitions of certain types of compensation under FINRA rules. However, FINRA recognizes that additional guidance may be needed following the adoption of the proposed rule change and will address interpretive questions as needed, similar to FINRA's approach to other regulatory initiatives with wide-ranging and novel impacts.

Covered Persons for Inclusion in the New Registration Category

Certain commenters requested clarification with respect to proposed FINRA Rule 1230(b)(6)(A)(i) regarding scope of the term senior management and whether this provision applies beyond senior managers with primary or direct responsibility over the covered functions.³² Two commenters advocated limiting the depth of personnel for the proposed rule change to a single category for senior management with responsibility over the covered functions, and requiring firms to maintain policies and procedures reasonably designed to ensure that operations personnel have an awareness of investor protection mechanisms in place at a firm.³³

FINRA believes this provision is clear as originally proposed and, while FINRA understands titles may differ between firms, members should be able to identify operations personnel that would be subject to proposed Rule 1230(b)(6)(A)(i) based on

³² IRI, Nationwide, NSCP and TIAA.

³³ Wellington and Wells Fargo.

their functions and responsibilities as senior managers overseeing the covered functions. FINRA would consider any senior manager in the chain of command responsible for a covered function to be subject to the proposed rule, up to and including the Principal Operations Officer.³⁴ FINRA does not agree that “covered persons” should be limited to senior management with responsibility over the covered functions because the proposed registration category is intended to include other individuals who exercise supervisory and discretionary authority in direct furtherance of the covered functions. Accordingly, FINRA has not proposed changes to proposed FINRA Rule 1230(b)(6)(A)(i).

Proposed FINRA Rule 1230(b)(6)(A)(ii) would include as covered persons supervisors, managers or other persons responsible for approving or authorizing work, including work of other persons, in direct furtherance of the covered functions. One commenter suggested the proposed rule explicitly state that covered persons are limited to those persons with decision-making and/or oversight authority.³⁵ Certain commenters requested that FINRA clarify what is meant by the phrase “approve or authorize work.”³⁶ Other commenters stated that this provision is written too broadly;³⁷ creates potential for misinterpretation in determining how far up or down the reporting chain this registration requirement would apply;³⁸ could sweep in affiliate employees, mid or low level

³⁴ See Regulatory Notice 09-70 (December 2009) for a discussion of the Principal Operations Officer registration category. See also infra note 60 and accompanying text.

³⁵ Morgan Stanley.

³⁶ ESI, NFP, TIAA and UPFS.

³⁷ ACLI, NSCP, Quasar and Wells Fargo.

³⁸ ACLI.

employees,³⁹ third-party vendors⁴⁰ and margin clerks;⁴¹ and that it should be limited to supervisors, managers or other persons responsible for primary oversight of covered functions, including managers for dual hat employees.⁴² One commenter suggested that FINRA revise this provision to clarify that supervisors and managers be senior members of their respective departments or units.⁴³ Numerous commenters recommended deleting the phrase “work of other persons” because it is unclear.⁴⁴

FINRA believes proposed FINRA Rule 1230(b)(6)(A)(ii) is clear as proposed and notes that it consulted with industry representatives in developing the proposed rule change, including the definition and appropriate depth of personnel to be subject to the Operations Professional registration category. As noted above, FINRA believes members will be able to identify supervisors, managers or other persons responsible for approving or authorizing work in direct furtherance of the covered functions based on their functions and responsibilities. The phrases “approve or authorize work” and “work of other persons” are not legal terms of art but, rather, comport with commercially understood operating terms and do not require clarification. Accordingly, FINRA has not revised this provision as suggested by the commenters; however, FINRA proposes a minor modification to the original proposal by re-locating the phrase “including the work

³⁹ Morgan Stanley.

⁴⁰ Schwab.

⁴¹ Scottrade.

⁴² ARM, TIAA and Wells Fargo.

⁴³ Bank of America.

⁴⁴ Bank of America, IPA, SIFMA and Wells Fargo.

of other persons” to streamline the provision, as reflected in Section A. of the Purpose section.

As originally proposed in the Notice, FINRA Rule 1230(b)(6)(A)(iii) required registration as an Operations Professional for persons with the authority or discretion to commit the member’s capital in direct furtherance of the covered functions or to commit the member to any contract or agreement (written or oral) in direct furtherance of the covered functions. Certain commenters stated this provision is unclear and too far-reaching⁴⁵ and noted it would capture persons who perform routine, daily activities, or enter into agreements consistent with firm policies that have no material impact on firm operations (including margin clerks, who often have flexibility to obligate firm capital up to certain limits).⁴⁶ Two commenters noted that the provision should only be triggered if the contracts are sufficiently material to the firm.⁴⁷ One commenter noted that it may be so broad as to require registration of junior associates if they sign or approve contracts, retain vendors or make clerical postings to the books of a member.⁴⁸ Another commenter noted that this provision is inconsistent with the first two categories of covered persons, which focus on senior managers, supervisors and those who approve work in the covered functions.⁴⁹ Another commenter requested clarification with respect to the term “firm capital” because it could sweep in persons who approve the payment of vendor invoices

⁴⁵ Bank of America, TIAA and NSCP.

⁴⁶ T. Rowe Price and Wells Fargo.

⁴⁷ Bank of America and TIAA.

⁴⁸ Bank of America.

⁴⁹ SIFMA.

for services related to some aspect of a covered function.⁵⁰ Two commenters noted it is unclear what individuals, other than those engaged in or supervising securities lending activities, the proposed third category of covered persons intends to cover and suggested certain amendments to clarify the proposal with respect to such persons.⁵¹

Based on the comments, FINRA has revised the third category of covered persons from the original proposal in the Notice, as discussed in Section A. of the Purpose section. Under the revised proposal, FINRA Rule 1230(b)(6)(A)(iii) would require persons with the authority or discretion materially to commit a member's capital in direct furtherance of the covered functions or to commit a member to any material contract or agreement (written or oral) in direct furtherance of the covered functions to register as an Operations Professional. FINRA purposefully did not limit the third category of covered persons to supervisors and managers because the capacity to make material discretionary decisions above a member's pre-established spending guidelines and risk management policies under this provision is not confined to senior or supervisory personnel.

Numerous commenters suggested that FINRA add language to the proposed rule to clarify, as stated in the Notice, that the proposed rule does not apply to persons who perform functions ancillary to a covered function or whose function is to serve a role that can be viewed as supportive of, or advisory to, the performance of a covered function, such as internal audit, legal or compliance personnel.⁵² One commenter further urged FINRA to add rule language to note that individuals performing quality assurance and

⁵⁰ Scottrade.

⁵¹ Morgan Stanley and SIFMA.

⁵² Bank of America, FSI, NSCP, Scottrade, SIFMA and TIAA.

quality control functions in direct furtherance of a covered function are similarly excluded.⁵³ One commenter noted that registering clerical personnel only increases costs unnecessarily and creates hiring barriers for new applicants.⁵⁴ One commenter requested that FINRA provide specific examples of activities it deems ministerial or clerical in nature, especially when such activities require Financial and Operations Principal review and control procedures.⁵⁵

Based on the comments, and as noted in Section A. of the Purpose section of this rule filing, FINRA is proposing supplementary material .06 to the proposed rule to clarify that any person whose activities are limited to performing a function ancillary to a covered function, or whose function is to serve a role that can be viewed as supportive of or advisory to the performance of a covered function (e.g., internal audit, legal or compliance personnel who review but do not have primary responsibility for any covered function), or who engages solely in clerical or ministerial activities in a covered function would not be required to register as an Operations Professional. FINRA declines to provide examples of clerical and ministerial activities at this time, believing the term to be well understood in the industry;⁵⁶ however, as noted above, FINRA will consider issuing additional guidance as needed regarding the categories of persons subject to the Operations Professional registration category.

⁵³ TIAA.

⁵⁴ Martin Nelson.

⁵⁵ Quasar.

⁵⁶ See, e.g., NASD Rule 1060 (Persons Exempt from Registration).

One commenter encouraged FINRA to clarify whether an Operations Professional must be supervised by a qualified supervisory principal.⁵⁷ Another commenter requested clarification regarding whether a firm must assign or designate an Operations Professional and whether a person who is already a registered principal must register as an Operations Professional.⁵⁸

As noted above, as registered persons, Operations Professionals will be subject to all FINRA rules applicable to associated persons and/or registered persons. Accordingly, pursuant to NASD Rule 3010(a)(5), each Operations Professional must be assigned to an appropriately registered representative(s) and/or principal(s) who shall be responsible for supervising that person's activities. Additionally, FINRA expects that each member would have at least one registered Operations Professional, who often may be the member's Financial and Operations Principal and/or the Principal Operations Officer. In this regard, neither principal registration, nor representative registration in another category, obviates the requirement for a covered person to register as an Operations Professional. As noted in Section D. of the Purpose section, there are numerous eligible registrations that would except such registered persons from the requirement to pass the Operations Professional qualification examination.

Certain commenters inquired as to the proposed rule change's relationship to, and consistency with, the proposals set forth in Regulatory Notice 09-70⁵⁹ and two commenters requested clarification regarding how the proposed requirement under

⁵⁷ Pershing.

⁵⁸ Crowell.

⁵⁹ PSD, Sutherland and Wells Fargo.

Regulatory Notice 09-70 that firms appoint a distinct Principal Operations Officer and a distinct Principal Financial Officer intersects with the proposed Operations Professional designation.⁶⁰

The proposed rule change does not conflict with the proposals set forth in Regulatory Notice 09-70. The proposed rule change should be read as a separate registration requirement that will be added to the consolidated FINRA registration rules. To note, the proposed rule change would include persons engaged in or supervising stock loan/securities lending activities that meet the depth of personnel as a covered person in Section A. above. FINRA also is proposing separate registration requirements for a “Securities Lending Representative” and a “Securities Lending Supervisor” in Regulatory Notice 09-70; consequently, firms should be aware of both sets of proposed requirements.⁶¹ With respect to the proposed requirements in Regulatory Notice 09-70 for Principal Operations Officers and Principal Financial Officers, such persons likely would be required to register as an Operations Professional, depending on whether they meet the criteria of a covered person as described in Section A. of the Purpose section. The requirement for a covered person to register as an Operations Professional applies regardless of any other, separate registration requirements; however, such other registration may be used as an eligible registration to qualify a covered person for an exception from the requirement to take the Operations Professional qualification examination.

⁶⁰ IRI and TIAA.

⁶¹ See supra note 4.

One commenter noted the proposed rule change could have costly and burdensome implications regarding state registration and licensing so FINRA should be as clear as possible in defining who is covered under the proposed rule change.⁶² As noted above, FINRA believes the definitions of covered persons are sufficiently clear and will provide additional guidance as needed regarding the scope of persons subject to the new requirements.

Covered Functions for Inclusion in the New Registration Category

Numerous commenters stated that the covered functions as proposed in the Notice are too broad, unclear and inconsistent, and will incur unnecessary costs for firms.⁶³ The commenters requested more precise descriptions of the covered functions.⁶⁴ One commenter requested that FINRA clarify that the covered functions apply only to activities performed by or on behalf of a firm's securities and investment banking business.⁶⁵ Two commenters urged FINRA to group dependent technology-related covered functions into a single entry.⁶⁶ Another commenter suggested that certain

⁶² NSCP.

⁶³ Commonwealth, Crowell, ESI, FSI, IPA, IRI, Modern Woodmen, Morgan Stanley, NFP, Northwestern Mutual, NSCP, PSD, TIAA, SIFMA, Sutherland, UPFS and WSFG.

⁶⁴ Commonwealth, Crowell, ESI, FSI, IPA, IRI, Modern Woodmen, Morgan Stanley, NFP, Northwestern Mutual, NSCP, PSD, TIAA, SIFMA, Sutherland, UPFS and WSFG.

⁶⁵ TIAA.

⁶⁶ Morgan Stanley and NSCP.

functions be deleted because they are roles that support other covered functions and are not stand-alone functions.⁶⁷

Based on the comments, FINRA has made certain changes to the covered functions as originally proposed in the Notice to clarify and streamline the proposed rule. As a general matter, FINRA has revised the list of covered functions, as reflected in Section B. of the Purpose section, to group related functions together. Substantive revisions to the covered functions are described in detail below.

To clarify the proposed rule change, FINRA has revised Rule 1230(b)(6)(B)(i) (as originally proposed in the Notice) by limiting this covered function to the “[a]pproval of pricing models used for valuations,” instead of the “[d]evelopment and approval of pricing models used for valuations.” FINRA also moved this provision to proposed Rule 1230(b)(6)(B)(x).

Two commenters requested a definition for the term “client on-boarding” in proposed FINRA Rule 1230(b)(6)(B)(v) (as originally proposed in the Notice).⁶⁸ FINRA notes from its consultation with industry representatives in the rule development process that this is a term commonly used for this covered function and believes the proposed rule text provides sufficient clarity (*i.e.*, “[c]lient on-boarding (customer account data and document maintenance)”).

Numerous commenters requested clarification with respect to the scope of proposed FINRA Rule 1230(b)(6)(B)(vi) (as originally proposed in the Notice), the covered function addressing the “[c]apturing of business requirements for sales and

⁶⁷ Schwab.

⁶⁸ PSD and Sutherland.

trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements.”⁶⁹ One commenter noted that this provision should apply only to individuals who “define and approve” business requirements, rather than individuals who “capture” such requirements.⁷⁰ Similarly, to reduce the likelihood of inadvertently capturing personnel who merely prepare initial drafts of business requirements documents and who perform routine quality assurance or quality control testing, two commenters suggested incorporating the concepts of “accepting” and “approving” in lieu of “capturing” and “defining” for the covered functions that include these terms.⁷¹

Based on the comments, FINRA has revised the original proposal to eliminate the concept of “capturing” in proposed FINRA Rule 1230(b)(6)(B)(vi). The proposed rule change renumbers this provision as proposed FINRA Rule 1230(b)(6)(B)(xiii) and includes as a covered function, “[d]efining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements.” FINRA has not eliminated the concept of “defining” from the covered functions because it believes covered persons who are responsible for defining and approving business system requirements are professional level staff that should be subject to registration with FINRA. The covered functions generally would not include a person who engages in administrative responsibilities, such as an initial drafter or a code developer. However, a

⁶⁹ ESI, FSI, Horace Mann, Modern Woodmen, NFP, Scottrade, TIAA and UPFS.

⁷⁰ Northwestern Mutual.

⁷¹ Bank of America and SIFMA.

person who supervises or approves such activities generally would be required to register as an Operations Professional.

Additionally, certain commenters requested clarification with respect to proposed Rule 1230(b)(6)(B)(vii) (as originally proposed in the Notice), which includes as a covered function, “[w]ith respect to the covered functions, defining and approving business security requirements and policies for information technology (including, but not limited to, systems and data).”⁷² One commenter noted that this function should only require persons who “approve” business requirements for systems and information technology to register so that the final approvals for technology requirements are performed by licensed Operations Professionals.⁷³

FINRA has made minor changes to the original proposal with respect to Rule 1230(b)(6)(B)(vii). The proposed rule change renumbers this provision as proposed FINRA Rule 1230(b)(6)(B)(xiv) and includes as a covered function, “[d]efining and approving business security requirements and policies for information technology, including, but not limited to, systems and data, in connection with the covered functions.” As noted above, FINRA believes that covered persons engaged in defining and approving business security requirements and policies for information technology should be registered as Operations Professionals.

One commenter requested clarification with respect to proposed Rule 1230(b)(6)(B)(viii) (as originally proposed in the Notice), which includes as a covered

⁷² ESI, FSI, Horace Mann, Modern Woodmen, NFP, Scottrade and UPFS.

⁷³ Morgan Stanley.

function, “[d]efining information entitlement policy in connection with the covered functions.”⁷⁴

Based on the comments and in line with the changes noted above, FINRA has revised Rule 1230(b)(6)(B)(viii). The proposed rule change renumbers this provision as proposed FINRA Rule 1230(b)(6)(B)(xv) and includes as a covered function, “[d]efining and approving information entitlement policies in connection with the covered functions.”

One commenter recommended that FINRA combine paragraphs (b)(6)(B)(vii) and (viii) (as originally proposed in the Notice) since both sections cover overlapping sets of supervisors in the Information Management area.⁷⁵ Another commenter noted that proposed FINRA Rules 1230(b)(6)(B)(vi), (vii), (viii) and (xv) are not separate functions but are ancillary to other covered functions and may require managers from both the actual covered functions and these ancillary areas to register.⁷⁶ One commenter requested clarification that FINRA Rules 1230(b)(6)(B)(vi), (vii) and (viii) (as originally proposed in the Notice) are limited to only those individuals directly employed by the FINRA member.⁷⁷ Another commenter suggested limiting these provisions to individuals responsible for ensuring that systems related to sales and trading and to covered functions meet business and regulatory requirements and “information security”

⁷⁴ Scottrade.

⁷⁵ Bank of America.

⁷⁶ NSCP.

⁷⁷ IPA.

(firewalls, data access, and system entitlements in connection with the covered functions).⁷⁸

FINRA believes that the proposed revisions to these provisions noted above clarify the proposed rule and is not proposing further changes at this time. FINRA notes that these covered functions should remain as separate items since they address different activities (e.g., defining, approving and validating business requirements for sales and trading systems or other systems relating to the covered functions vs. defining and approving entitlement policies in connection with the covered functions) and firms may have different internal reporting structures so that these activities are not part of the same area or subject to the same supervisory scheme.

Certain commenters suggested deleting proposed Rule 1230(b)(6)(B)(xv) (as originally proposed in the Notice), which includes as a covered function, “[p]osting entries to the books and records of a member in connection with the covered functions,” because it is ambiguous, too broad⁷⁹ and may sweep in clerical staff.⁸⁰ Another commenter requested clarification regarding the term “books and records” and requested that FINRA add a reference to Exchange Act Rule 17a-3⁸¹ or MSRB Rule G-8.⁸² Two

⁷⁸ SIFMA.

⁷⁹ Bank of America and SIFMA.

⁸⁰ Crowell and SIFMA.

⁸¹ 17 CFR § 240.17a-3.

⁸² Rockfleet.

commenters recommended that FINRA revise this provision to tailor it to separate regulatory issues such as customer protection or financial responsibility concerns.⁸³

FINRA has revised Rule 1230(b)(6)(B)(xv) to clarify this covered function. The proposed rule change renumbers this provision as FINRA Rule 1230(b)(6)(B)(xvi) and includes as a covered function, “[p]osting to a member’s books and records in connection with the covered functions to ensure integrity and compliance with the federal securities laws and regulations and FINRA rules.”

One commenter noted that some of the covered functions may cause confusion with respect to other registration categories, including proposed FINRA Rules 1230(b)(6)(B)(ix) and (xiv) (as originally proposed in the Notice), the covered functions for “[f]inancial controller (including general ledger)” and “[f]inancial regulatory reporting,” respectively, and the functions supervised by the financial and operations principal, and may overlap with the proposed designation of the Principal Operations Officer under Regulatory Notice 09-70.⁸⁴ Based on the comment, FINRA has revised these items. The proposed rule change renumbers these items as proposed FINRA Rules 1230(b)(6)(B)(xi) and (xii), respectively, and includes as covered functions, “[f]inancial control, including general ledger and treasury” and “[c]ontributing to the process of preparing and filing financial regulatory reports.” FINRA does not agree that the proposed rule change causes confusion with respect to other registration requirements. Members must determine whether the proposed registration requirements for Operations

⁸³ Morgan Stanley and SIFMA.

⁸⁴ IRI.

Professionals would apply to an associated person based on his or her functions and responsibilities notwithstanding any other, separate registration requirements.

One commenter noted that the title of the proposed registration category is too narrow and not reflective of the covered functions. Alternatively, the commenter suggested that the registration category should be titled “Operations, Support or Securities Lending Professionals.”⁸⁵ FINRA believes that the proposed title for the new registration category, Operations Professionals, is appropriate and succinctly captures the individuals to which the proposed requirements would apply given the breadth of activities covered under the proposed rule change.

Certain commenters requested clarification that ongoing insurance company functions relating to variable annuity contracts as well as other functions performed by insurance company staff are not included in the covered functions.⁸⁶ FINRA does not intend to make any categorical exclusions from the covered functions. The proposed requirements will apply if a person meets the depth of personnel criteria and engages in one or more covered function on behalf of a member regardless of where they are employed.

Operations Professional Qualification Examination

One commenter noted that elements of the qualification examination and continuing education requirements have no relevance to the products and operations of limited purpose broker-dealers that comprise more than 50% of FINRA’s membership.⁸⁷

⁸⁵ SIFMA.

⁸⁶ IRI, PSD and Sutherland.

⁸⁷ ACLI.

Other commenters noted that the two areas of proposed examination coverage, “essential product and market knowledge for an Operations Professional” and “knowledge associated with operations activities,” should be eliminated from the examination curriculum because they undercut FINRA’s premise that it will not be a “competency” examination and render the test extremely challenging for many operations personnel since they lack the background and experience to pass the examination and have little testing experience.⁸⁸ Another commenter similarly noted that the proposed examination requirement could result in well-qualified employees losing their jobs and firms’ operations departments could have compromised functionality, and supervision (i.e., a “brain drain”) of qualified operations personnel, thus undermining the goals of the proposal.⁸⁹

Numerous commenters stated that an examination is unnecessary because training and education for operations personnel should be addressed in a member’s WSPs⁹⁰ and registered principals are responsible for training operations personnel.⁹¹ To reduce cost burdens on firms, certain commenters recommended ongoing training requirements as an alternative to registration and testing of operations personnel.⁹² Certain other commenters noted that FINRA can address operations personnel through registration and

⁸⁸ NSCP and ACLI.

⁸⁹ NSCP.

⁹⁰ FSI, M. Griffith, Navidar and PSD.

⁹¹ Modern Woodmen and Martin Nelson.

⁹² Harrison, NSCP, RMOA and Wells Fargo.

continuing education⁹³ and an examination not based on competency serves no essential function.⁹⁴ One commenter stated that the Series 27 and 28 examinations already test for the covered functions, so a new exam is a poor use of member firm fees and will unnecessarily delay implementation of the proposal.⁹⁵

One commenter noted that based on the definition of a covered person, the Operations Professional qualification examination should be a principal-level examination with corresponding continuing education requirements.⁹⁶ One commenter requested that FINRA publish a study outline for notice and comment prior to making the test effective.⁹⁷ Another commenter recommended that FINRA offer the proposed examination as an optional test for people who want to learn about back-office, but not as a mandatory examination for Operations Professional registration.⁹⁸

FINRA believes the qualification examination requirement is appropriate as proposed. The proposed examination is being tailored to test for basic securities industry knowledge and ethics. Although the examination will not test for proficiency with respect to the specific covered functions, FINRA believes there is value in an examination that tests for general knowledge about the securities industry. The proposed examination will be appropriately tailored to individuals subject to the proposed

⁹³ Commonwealth, ESI, FSI, Horace Mann, NFP, UFPS and WSFG.

⁹⁴ Horace Mann, JRCO, Modern Woodmen, NSCP, RMOA, Rockfleet, UPFS and WSFG.

⁹⁵ Rockfleet.

⁹⁶ Rockfleet.

⁹⁷ NSCP.

⁹⁸ M. Griffith.

registration requirements. It is crucial for covered persons to understand their professional responsibilities, including key regulatory and control themes, as well as the importance of identifying and escalating red flags that may harm a firm, its customers, the integrity of the marketplace, or the public.

Additionally, FINRA believes a representative-level examination is appropriate for Operations Professionals because the proposed registration category is based on functions performed by operations personnel and is not limited to supervisory or managerial staff (e.g., persons who fall within proposed FINRA Rule 1230(b)(6)(A)(ii) and (iii)).

One commenter suggested that FINRA modify the period for retaking the Operations Professional qualification examination if an applicant fails to 30 days like the Series 55.⁹⁹ FINRA does not intend to change its policy regarding the re-taking of qualification examinations for the proposed Operations Professional examination at this time. FINRA will reconsider the policy if it finds it to be a necessary step when the qualification examination for Operations Professionals is administered.

Exception to Operations Professional Examination Requirement

One commenter noted that the proposed exceptions are so numerous that they dilute the regulatory intent of the proposed rule change; instead, FINRA should grant a limited number of exceptions to current operations employees.¹⁰⁰ One commenter recommended FINRA incorporate an exception for certain small firms.¹⁰¹ One

⁹⁹ Schwab.

¹⁰⁰ NASAA.

¹⁰¹ Freestone.

commenter suggested that registered principals should be completely exempt from the proposed Operations Professional requirements;¹⁰² other commenters suggested that the proposed rule change should only apply to currently unregistered persons because the potential costs and burdens involved with tracking and monitoring multiple registrations outweigh the benefits.¹⁰³ One commenter suggested FINRA permit firms to identify any relied upon registration for the proposed exception in their WSPs instead of a U4 amendment, as is required currently for any person in a supervisory role.¹⁰⁴

Certain other commenters recommended a grandfather provision for experienced persons who have worked in operations areas for a certain time period (e.g., three¹⁰⁵ or five¹⁰⁶ years) prior to the implementation of the proposed rule.¹⁰⁷ Two commenters requested that FINRA extend the proposed exception to registrations held beyond the two-year look back.¹⁰⁸ One commenter noted that there are costs and burdens of a two-year look back without a concomitant benefit.¹⁰⁹ Additionally, one commenter suggested that FINRA consider incorporating standards within its Qualification Examination Waiver Guidelines that will accommodate individuals that possessed an eligible

¹⁰² NSCP.

¹⁰³ Northwestern Mutual and T. Rowe Price.

¹⁰⁴ T. Rowe Price.

¹⁰⁵ Commonwealth.

¹⁰⁶ FSI, PSD and Sutherland.

¹⁰⁷ FSI, Modern Woodmen, NFP, UPFS and WSFG.

¹⁰⁸ Nationwide and TIAA.

¹⁰⁹ IRI.

registration within a reasonably recent time period and have been performing an Operations Professional role for a reasonable period of time.¹¹⁰ This commenter also suggested that FINRA finalize the permissive registration regime contemplated in Regulatory Notice 09-70 prior to implementing a new Operations Professional designation, which would provide firms and their personnel with the option to maintain licenses while the registered person occupies a non-registered position.¹¹¹

FINRA believes the proposed rule change clearly articulates the exception to the Operations Professional qualification examination requirement.¹¹² A primary purpose of the proposed qualification examination is to assess a covered person's basic understanding of the securities industry and the requirement to take a registration examination serves to alert such person of the role he or she plays in this highly regulated environment. Thus, FINRA believes the eligible registrations (and corresponding examinations) serve as a valid proxy for the Operations Professional examination requirement.

FINRA believes the two-year look back for the eligible registrations is appropriate and has not revised the proposal to extend this time period. The proposed look back is based on the window during which an associated person remains eligible to re-activate his or her registration based on previously qualifying for and holding such

¹¹⁰ TIAA.

¹¹¹ TIAA.

¹¹² The Notice included as an eligible registration the General Securities Principal – Sales Supervisor Module (Series 23). FINRA has removed this examination from the list of eligible registrations. A person who passes the Series 9/10 and the Series 23 may obtain the General Securities Principal (Series 24) registration, but a person who passes solely the Series 23 is not considered registered in any capacity.

registration. A person who qualifies for the proposed exception based on their having held an eligible registration within the two years immediately prior to registering as an Operations Professional would be required to first re-activate such eligible registration prior to requesting Operations Professional registration.¹¹³ Under NASD Rules 1021 and 1031, members are permitted to maintain or make application for registration as a registered principal or registered representative for a person who performs back-office operations, among other things. As such, firms are not currently prohibited from carrying registrations for back-office personnel. FINRA has determined not to incorporate a grandfather provision for previously unregistered operations personnel. FINRA believes that all covered persons benefit from an examination requirement even if they have been working in the same position for an extended period. As noted above, the proposed Operations Professional examination will not test on specific job functions but will focus on general securities industry knowledge and key regulatory themes.

Continuing Education

Certain commenters encouraged FINRA to clarify whether the proposal requires currently registered principals to take both the S101 continuing education module and the S201¹¹⁴ and requested that FINRA refine the continuing education requirements to reflect FINRA's diverse membership.¹¹⁵

As stated in the Notice and Section E. of the Purpose section, individuals who avail themselves of the proposed exception to the Operations Professional qualification

¹¹³ See supra note 6.

¹¹⁴ Great Nation.

¹¹⁵ ACLI.

examination requirement with an eligible registration would be subject to the Regulatory Element program appropriate for such other registration category. FINRA believes the proposed continuing education requirements for Operations Professionals are clear and notes that such requirements will be appropriately suited for those subject to registration, similar to the continuing education training for other FINRA registration categories.

Outsourced and Shared Functions

One commenter requested confirmation that FINRA does not intend to alter indirectly the definition of “associated person” or the existing regulatory guidance on outsourcing arrangements with the proposed rule change.¹¹⁶ Numerous commenters requested clarification that covered persons are limited to persons who have been empowered by a broker-dealer to oversee the covered functions and would not include individuals who perform operations functions for affiliated entities, outsourced operations functions for a third-party service provider or supervisors within a large, diversified financial services organization who are far-removed from a member’s securities business.¹¹⁷ Certain commenters requested clarification with respect to who must register where clearing and introducing firms share responsibility for operations functions (“shared functions”)¹¹⁸ and whether such persons would be considered associated persons of both the introducing and clearing firms.¹¹⁹ Several commenters suggested that an exemption be provided when covered functions are performed by another registered

¹¹⁶ SIFMA.

¹¹⁷ ACLI, A&P, ARM, Bank of America, Horace Mann, IRI, Nationwide, PSD, Sutherland and TIAA.

¹¹⁸ ESI, FSI, NFP, UPFS, Wells Fargo and WSFG.

¹¹⁹ Northwestern Mutual, Pershing and Wells Fargo.

broker-dealer, bank, investment advisor, foreign entity¹²⁰ or affiliated insurance company.¹²¹ Given a member’s obligation to supervise any outsourced activity, numerous commenters stated that it should be sufficient for FINRA to confine application of the proposed registration and examination requirements to “employees” of the member.¹²² One commenter questioned the legal ramifications that would result from requiring the registration of vendor employees with more than one member.¹²³ Certain commenters requested clarification with respect to how the proposed rule change affects Office of Supervisory Jurisdiction (“OSJ”) requirements relating to currently outsourced activities¹²⁴ and back-office and support locations.¹²⁵ One commenter stated the proposed rule change would place an unfair burden on small firms that outsource many of the covered functions.¹²⁶

As noted above, FINRA believes anyone who meets the criteria of a covered person and engages in one or more of the covered functions on behalf of a member must register as an Operations Professional, regardless of whether such person works internally at a member, an affiliate or third-party service provider. Also as previously noted, the proposed rule change does not alter the definition of an “associated person” but rather

¹²⁰ AIC and Pershing.

¹²¹ ACLI and AIC.

¹²² NSCP, Pershing, Schwab, Scottrade and TIAA.

¹²³ Pershing.

¹²⁴ IRI.

¹²⁵ Scottrade and TIAA.

¹²⁶ Zelman.

imposes registration, qualification examination and continuing education requirements on persons who meet the depth of personnel criteria and engage in one or more of the covered functions on behalf of a member. The proposed registration category is function-based so persons are not shielded from the requirements based on their job title or employment by an entity other than a member.

Additionally, FINRA notes that the proposed rule change would apply to all members regardless of firm size. FINRA reminds members that the depth of personnel included as covered persons generally is focused on positions with higher-level responsibilities, so entry level staff will likely not be required to register.

With respect to clearing arrangements and consistent with Notice to Members 05-48, a covered person would not be considered an associated person of both the introducing and clearing firms based solely on functions performed pursuant to a carrying agreement approved under FINRA Rule 4311 (Carrying Agreements),¹²⁷ so FINRA would not expect dual registration as an Operations Professional in such cases. However, as noted above, FINRA expects each member will designate at least one Operations Professional, who often may be the Financial and Operations Principal and/or the Principal Operations Officer.¹²⁸

One commenter suggested that treating persons that fall within the covered categories as associated persons of a member will impact state law prohibitions on dual

¹²⁷ FINRA is replacing NASD Rule 3230 (Clearing Agreements) and NYSE Rule 382 (Carrying Agreements) with new consolidated FINRA Rule 4311 (Carrying Agreements). See Securities Exchange Act Release No. 63999 (March 1, 2011) (Order Approving File No. SR-FINRA-2010-061).

¹²⁸ See supra note 60 and accompanying text.

registration and vendor agreements.¹²⁹ FINRA has stated throughout this filing the need for this proposed rule change and its belief that the proposal is appropriately tailored to meet its stated objectives. FINRA believes it is therefore required additional regulation. That being the case, ill-defined collateral effects that can be avoided by a member do not serve as a reason to modify or negate such proposed rulemaking. Finally, FINRA already views the persons treated as covered persons in the covered functions, and indeed all non-clerical persons reporting to such covered persons, as associated persons irrespective of this proposed rule.

Small Firms Concerns

Numerous commenters noted the proposed rule change places an undue burden on, unnecessarily increases costs for, and is anticompetitive for small firms with no apparent benefit to the public.¹³⁰ One commenter noted the proposal is appropriate only in its application to personnel and broker-dealers that handle customer accounts, customer funds and/or securities.¹³¹

FINRA does not agree that small firms would be overly burdened by the proposed rule change since almost all other FINRA registration requirements apply to small firms and do not provide an exemption for personnel performing activities that would require registration based on a firm's limited business. FINRA also anticipates that many persons who would be subject to the new Operations Professional registration category

¹²⁹ TIAA.

¹³⁰ Crowell, Freestone, Martin Nelson, Mutual Trust, Navidar, RiverStone, Wellington and Zelman.

¹³¹ FirstBank PR.

would qualify for the proposed exception from the qualification examination based on existing registrations, and, as noted above, FINRA would not assess a separate registration fee for persons relying on the proposed exception to register as Operations Professionals. Moreover, the impact of the proposed rule change is expected to be minimal as the majority of the covered functions are generally performed by the carrying and clearing firm and, as noted above, a covered person would not be considered an associated person of both the introducing and clearing firms based solely on functions performed pursuant to a carrying agreement approved under FINRA Rule 4311 (Carrying Agreements),¹³² so FINRA would not expect dual registration as an Operations Professional in such cases. However, as further detailed in Section F. above, in light of the limitations on personnel at certain smaller firms, FINRA is proposing a 120-day grace period for covered persons associated with a non-clearing member to transition into the proposed registration category.

Implementation of the Proposed Rule Change

Numerous commenters suggested that the proposed transition period of six to nine months for persons acting as Operations Professionals as of the effective date of the proposed rule change is insufficient for firms to fully comply because a significant number of personnel will need to become registered. The commenters noted that firms will likely need to phase-in such persons' preparation for, and taking of, the qualification examination to mitigate the impact on customer service and operational functions.¹³³

¹³² See supra note 127 and accompanying text.

¹³³ ARM, Bank of America, Commonwealth, ESI, FSI, Horace Mann, Modern Woodmen, M. Griffith, Morgan Stanley, NFP, NSCP, Scottrade, SIFMA and WSFG.

Also, certain commenters suggested that personnel may not pass the qualification examination on the first attempt since good test preparation services may not be available and certain operations personnel may not have test-taking skills.¹³⁴ The commenters suggested extending the transition period to between 12 to 18 months¹³⁵ or up to 24 months.¹³⁶ Other commenters noted that all persons should have the benefit of the transition period regardless of when they begin work in a covered function.¹³⁷

Certain commenters suggested that persons who begin work as Operations Professionals following the effective date of the proposed rule change (i.e., new hires or associated persons who meet the depth of personnel and transfer into a covered function) should be granted a grace period to transition into the proposed registration category.¹³⁸ According to one commenter, subjecting these persons to the proposed licensing regime immediately undercuts the purpose of the transition period and may chill hiring of operations personnel while the transition period is in effect.¹³⁹ Numerous commenters recommended a 90-day grace period for new hires or those who transition into a covered function, consistent with current NASD Rule 1021(d), which generally allows a registered representative to act in a principal capacity for 90 days while preparing for an

¹³⁴ Nationwide, UPFS and Wells Fargo.

¹³⁵ ARM, Bank of America, Commonwealth, ESI, FSI, Horace Mann, Modern Woodmen, M. Griffith, Morgan Stanley, NFP, NSCP, Scottrade, SIFMA and WSFG.

¹³⁶ Schwab.

¹³⁷ Schwab, SIFMA and TIAA.

¹³⁸ IRI, Nationwide, NSCP, Scottrade and Wells Fargo.

¹³⁹ Morgan Stanley.

applicable exam.¹⁴⁰ Two commenters suggested a 120-day grace period for personnel who transition into a covered function after the transition period has expired, conditioned on supervision by a licensed Operations Professional.¹⁴¹ One commenter suggested a 180-day grace period.¹⁴²

Based on the comments, FINRA has amended the transition period that was proposed in the Notice. As further detailed in Section F. above, FINRA is proposing a 60-day identification period beginning on the effective date of the proposed rule change during which Day-One Professionals must request registration as an Operations Professional via Form U4 in CRD. Day-One Professionals who are identified during the 60-day period and must pass the Operations Professional examination (or an eligible qualification examination) would be granted 12 months beginning on the effective date of the proposed rule change to pass such qualifying examination, during which time such persons may function as an Operations Professional.

With respect to non-Day-One Professionals, any person associated with a clearing or self-clearing member must register as an Operations Professional and, if applicable, pass the Operations Professional qualification examination (or an eligible qualification examination) prior to engaging in any activities that would require such registration. Any non-Day-One Professional associated with a non-clearing member who must pass the Operations Professional qualification examination (or an eligible qualification examination) to obtain registration would be granted a grace period of 120 days

¹⁴⁰ ARM, Bank of America, PSD, Schwab, Scottrade, Sutherland and Wells Fargo.

¹⁴¹ Morgan Stanley and SIFMA.

¹⁴² Wells Fargo.

beginning on the date such person requests Operations Professional registration via Form U4 in CRD to pass such qualifying examination, during which time such person may function as an Operations Professional.

Two commenters expressed sentiments regarding their general disagreement with FINRA spending¹⁴³ and the current regulatory structure for broker-dealers.¹⁴⁴ These comments are outside the scope of the proposed rule change.

6. Extension of Time Period for Commission Action

FINRA does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.¹⁴⁵

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibits

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 2a. Regulatory Notice 10-25 (May 2010).

Exhibit 2b. A list of the comment letters received in response to Regulatory Notice 10-25 (May 2010).

¹⁴³ Mutual Trust.

¹⁴⁴ Wellington.

¹⁴⁵ 15 U.S.C. 78s(b)(2).

Exhibit 2c. Copies of the comment letters received in response to Regulatory Notice 10-25 (May 2010).

Exhibit 5. Text of Proposed Rule Change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-FINRA-2011-013)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change to Establish a Registration Category, Qualification Examination and Continuing Education Requirements for Certain Operations Personnel, and Adopt FINRA Rule 1250 (Continuing Education Requirements) in the Consolidated FINRA Rulebook

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on , Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to adopt FINRA Rule 1230(b)(6) to establish a registration category and qualification examination requirement for certain operations personnel. The proposed rule change also would adopt continuing education requirements for such operations personnel and adopt NASD Rule 1120 (Continuing Education Requirements) as FINRA Rule 1250 (Continuing Education Requirements) in the consolidated FINRA rulebook with minor changes.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

The text of the proposed rule change is available on FINRA's Web site at <http://www.finra.org>, at the principal office of FINRA and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Background

Given the growing complexity of the financial services industry and the importance of services provided by personnel in operations departments, FINRA is concerned about the potential for regulatory gaps in the area of registration and education requirements for individuals performing and overseeing member operations functions. Historically, federal and state law and self-regulatory organization ("SRO") rules, including NASD Rules 1021 and 1031, have required that individuals engaged in or supervising the securities or investment banking business of a member firm be qualified and registered persons. These requirements generally have applied to, among others, individuals with customer contact providing advice (sales persons and investment bankers) or effecting securities transactions (traders) and their supervisors. However,

unregistered individuals who perform and oversee member operations functions also play an integral role in the business of the firm, and their activities often have a meaningful connection to client funds, accounts and transactions. FINRA believes registration and education requirements for certain operations personnel are needed to help ensure that investor protection mechanisms are in place in all areas of a member's business that could harm the member, a customer, the integrity of the marketplace, or the public.

Proposal

As described in detail below, FINRA is proposing to expand its registration provisions to require registration of certain individuals ("covered persons") who are engaged in, responsible for or supervising certain member operations functions ("covered functions") to enhance the regulatory structure surrounding these areas. The proposed rule change would amend proposed FINRA Rule 1230 (Registration Categories) to adopt a new representative registration category and qualification examination for such individuals ("Operations Professionals")³ and would expand FINRA's continuing education requirements to require that Operations Professionals be subject to Regulatory Element and Firm Element training.

Generally, covered persons would be those persons who are directly responsible for overseeing that tasks within the covered functions are performed correctly in accordance with industry rules, firm protocols, policies and procedures, and who are charged with protecting the functional and control integrity of the covered functions for a

³ See Regulatory Notice 09-70 (December 2009) (FINRA Requests Comment on Proposed Consolidated FINRA Rules Governing Registration and Qualification Requirements). The proposed amendments discussed in this Notice would be included in proposed FINRA Rule 1230 (Registration Categories).

member. Only persons who are both “covered persons” (i.e., meet the depth of personnel criteria as discussed in Section A. below) and conduct activities or functions in one or more of the “covered functions” (discussed in Section B. below) would be subject to the new Operations Professional registration category.

A. Covered Persons for Inclusion in the New Registration Category

The proposed rule change would require the following covered persons to register with FINRA as an Operations Professional:

- (1) Senior management with responsibility over the covered functions;
- (2) Supervisors, managers or other persons responsible for approving or authorizing work, including work of other persons, in direct furtherance of the covered functions; and
- (3) Persons with the authority or discretion materially to commit a member’s capital in direct furtherance of the covered functions or to commit a member to any material contract or agreement (written or oral) in direct furtherance of the covered functions.

Persons who perform a covered function, but whose responsibilities are below these specified levels, would not be required to register as Operations Professionals. Members must determine, based on a person’s activities and responsibilities, whether such person would be considered a covered person and subject to the proposed requirements for Operations Professionals. A person’s job title may not be clearly indicative of his or her obligation to register as an Operations Professional.

For the purpose of the proposed third category of covered persons, any person who has the authority or discretion materially to commit firm capital in direct furtherance

of the covered functions or commit a firm to a material contract or agreement in direct furtherance of the covered functions would be required to register as an Operations Professional. As proposed in supplementary material .06 (Scope of Operations Professional Requirement), the determination as to what constitutes “materially” or “material” would be based on a member’s pre-established spending guidelines and risk management policies. Generally, persons who do not have the authority or discretion to commit a member’s capital, or to commit a member to a contract or agreement, above such pre-established spending guidelines and risk management policies would not be subject to registration as an Operations Professional under this provision.

Additionally, proposed supplementary material .06 would provide that any person whose activities are limited to performing a function ancillary to a covered function, or whose function is to serve a role that can be viewed as supportive of or advisory to the performance of a covered function, or who engages solely in clerical or ministerial activities in a covered function would not be required to register as an Operations Professional pursuant to paragraph (b)(6)(A) of the proposed rule. For example, internal audit, legal or compliance personnel who review but do not have primary responsibility for any covered function would not be required to register as an Operations Professional.

Consistent with FINRA guidance, persons subject to the new Operations Professional registration category would be considered associated persons of a member irrespective of their employing entity, and would be subject to all FINRA rules applicable to associated persons and/or registered persons.⁴ Moreover, any person who meets the

⁴ See Notice to Members 05-48 (July 2005) (Members’ Responsibilities When Outsourcing Activities to Third-Party Service Providers). The Notice reminds members that “in the absence of specific NASD [or FINRA] rules, MSRB rules,

depth of personnel criteria described above in Section A. and is engaged in one or more covered functions would be required to register as an Operations Professional. The proposed rule change does not alter the status of covered persons as associated persons of a member insofar as they are performing regulated broker-dealer functions on behalf of the member. Rather, the proposed rule change explicitly imposes registration, qualification examination and continuing education requirements on such persons.

B. Covered Functions for Inclusion in the New Registration Category

Any person who meets the threshold in one of the three categories of covered persons identified above in Section A. who conducts activities or functions for a member in one or more of the following covered functions would be required to register as an Operations Professional:

- (1) Client on-boarding (customer account data and document maintenance);
- (2) Collection, maintenance, re-investment (i.e., sweeps) and disbursement of funds;
- (3) Receipt and delivery of securities and funds, account transfers;
- (4) Bank, custody, depository and firm account management and reconciliation;
- (5) Settlement, fail control, buy ins, segregation, possession and control;
- (6) Trade confirmation and account statements;
- (7) Margin;

or federal securities laws or regulations that contemplate an arrangement between members and other registered broker-dealers with respect to such activities or functions (e.g., clearing agreements executed pursuant to NASD Rule 3230), any third-party service providers conducting activities or functions that require registration and qualification under NASD [or FINRA] rules will generally be considered associated persons of the member and be required to have all necessary registrations and qualifications.”

- (8) Stock loan/securities lending;
- (9) Prime brokerage (services to other broker-dealers and financial institutions);
- (10) Approval of pricing models used for valuations;
- (11) Financial control, including general ledger and treasury;
- (12) Contributing to the process of preparing and filing financial regulatory reports;
- (13) Defining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements;
- (14) Defining and approving business security requirements and policies for information technology, including, but not limited to, systems and data, in connection with the covered functions;
- (15) Defining and approving information entitlement policies in connection with the covered functions; and
- (16) Posting entries to a member's books and records in connection with the covered functions to ensure integrity and compliance with the federal securities laws and regulations and FINRA rules.

The proposed rule change would include persons engaged in or supervising stock loan/securities lending activities that meet the depth of personnel as a covered person in Section A. above. FINRA also is proposing separate registration categories for a "Securities Lending Representative" and a "Securities Lending Supervisor."⁵

⁵ In Regulatory Notice 09-70, FINRA generally proposes to adopt the NYSE registration requirements for Securities Lending Representatives and Securities Lending Supervisors, requiring an associated person who has discretion to commit a member to any contract or agreement (written or oral) involving securities lending or borrowing activities with any other person, and the direct

C. Operations Professional Qualification Examination

The proposed rule change would establish a new qualification examination for Operations Professionals that would provide reasonable assurance that such individuals understand their professional responsibilities, including key regulatory and control themes, as well as the importance of identifying and escalating red flags that may harm a member, a customer, the integrity of the marketplace, or the public.⁶ So that applicants understand that they are functioning in a heavily regulated industry, the proposed Operations Professional qualification examination would test applicants on general securities industry knowledge and its associated regulations and rules. Subject to the proposed exception in Section D. below, any person required to register as an Operations Professional would be required to pass the Operations Professional qualification examination before such registration may become effective.

In general, given the diversity of functions performed by covered persons, the proposed Operations Professional qualification examination would be a principles-based qualification examination with a regulatory focus to test for a broad understanding of a

supervisor of the associated person to register as a Securities Lending Representative and Securities Lending Supervisor, respectively. These individuals would be required to register as such for tracking and oversight purposes, regardless of whether they are registered in other categories. However, solely for purposes of registering as a Securities Lending Representative or Securities Lending Supervisor, an individual will not be subject to a qualification examination at this time.

⁶ Any individual whose activities go beyond those proposed for the Operations Professional registration category would be required to separately qualify and register in the appropriate category or categories of registration attendant to such activities.

broker-dealer's business at a basic level, a basic understanding of the operations functions that support a broker-dealer's business and the regulations designed to achieve investor protection and market integrity that drive the operations processes and procedures conducted at a broker-dealer. As further detailed in Section E. below, the continuing education components associated with the Operations Professional registration category would provide competency training specific to the covered functions, as applicable.

The breadth and depth of coverage of the qualification examination would be determined through the use of testing industry standards used to develop examinations, and would include input and advice from covered persons active in the securities industry. The following are the proposed key content themes of the new Operations Professional qualification examination:

- Professional Conduct and Ethical Considerations: This section of the examination would assess a candidate's core knowledge addressed on other FINRA examinations that are appropriate for an Operations Professional. The questions would assess knowledge of what are considered serious violations of securities industry rules. This section would include ethics-based questions that address issues such as data integrity, escalation of regulatory red flags and separation of duties.
- Essential Product and Market Knowledge for an Operations Professional: This section of the examination would assess a candidate's basic product and market knowledge, including definitions and characteristics of major product categories (i.e., equities, debt, packaged securities, options and markets). An Operations Professional

would not be expected to know the same level of detail about the products and markets as a product specialist or a representative selling products to customers.

➤ Knowledge Associated with Operations Activities: This section of the examination would assess a candidate's broad-based knowledge regarding the covered functions outlined above that support a broker-dealer's business and the underlying rules that drive the processes associated with these activities (i.e., customer account set-up and transfers, recordkeeping requirements, rules associated with the protection of customer assets and transaction processing, uniform practices associated with making good delivery of securities, making payments for securities and meeting settlement requirements, and credit and margin rules). This section of the examination also would include ethics-based questions in the context of operations activities.

D. Exception to Operations Professional Examination Requirement

The proposed rule change would include an exception to the Operations Professional qualification examination requirement for persons who currently hold certain registrations (each an "eligible registration") or have held one during the two years immediately prior to registering as an Operations Professional. The proposed exception also would apply to persons who do not hold an eligible registration, but prefer an alternative to taking the Operations Professional examination. Such persons would be permitted to register in an eligible registration category (subject to passing the corresponding qualification examination or obtaining a waiver) and use such registration to qualify for Operations Professional registration.

A person who wishes to obtain Operations Professional registration under the proposed exception would not be automatically waived-in, but would have to opt-in by

requesting Operations Professional registration via Form U4 (the Uniform Application for Securities Industry Registration or Transfer) in the Central Registration Depository (“CRD®”).⁷ If there are no other deficiencies (e.g., fingerprints), the Operations Professional registration would be approved automatically at the time such request is made. Information regarding the proposed implementation period is discussed in detail in Section F. below. FINRA would not assess a separate registration fee for persons relying on the proposed exception to register as Operations Professionals.

FINRA conducted a review of the content outlines for each qualification examination it recognizes and identified examinations with broad content coverage that would be eligible for an exception to the Operations Professional examination requirement. Accordingly, persons who hold the following representative-level registration categories, or who have held such registration categories within the two years immediately prior to registering as an Operations Professional, would be qualified to register as an Operations Professional without passing the Operations Professional qualification examination:

- Investment Company Products/Variable Contracts Representative (Series 6)
- General Securities Representative (Series 7)
- United Kingdom Securities Representative (Series 17) or Canada Securities Representative (Series 37 or 38)

Additionally, persons who hold (or have held) certain principal-level registration categories would be qualified to register as an Operations Professional without passing

⁷ A person who qualifies for the proposed exception based on their having held an eligible registration within the two years immediately prior to registering as an Operations Professional would be required to first re-activate such eligible registration prior to requesting Operations Professional registration.

the Operations Professional examination. Most principal-level qualification examinations have a prerequisite examination requirement that is satisfied with one of the representative qualification examinations listed above; however, FINRA also proposes to include principal-level qualification examinations that do not have a prerequisite, or have a prerequisite that can be met with a qualification examination not on the above list (e.g., Series 62), because it is likely such principals are familiar with the content to be covered in the Operations Professional qualification examination as a result of the requirements of their positions. Specifically, persons who hold the following principal-level registration categories, or who have held such registration categories within the two years immediately prior to registering as an Operations Professional, would be qualified to register as an Operations Professional without passing the Operations Professional qualification examination:

- Registered Options Principal (Series 4)
- General Securities Sales Supervisor (Series 9/10)
- Compliance Officer (Series 14)
- Supervisory Analyst (Series 16)
- General Securities Principal (Series 24)
- Investment Company Products/Variable Products Principal (Series 26)
- Financial and Operations Principal (Series 27)
- Introducing Broker-Dealer Financial and Operations Principal (Series 28)
- Municipal Fund Securities Limited Principal (Series 51)
- Municipal Securities Principal (Series 53)

The proposed exception would not apply to persons whose eligible registrations are revoked pursuant to FINRA Rules 8310 (Sanctions for Violation of the Rules) or 8320 (Payment of Fines, Other Monetary Sanctions, or Costs; Summary Action for Failure to Pay), suspended or otherwise deemed inactive.⁸

FINRA notes that covered persons are generally acting in a supervisory position, so many persons will already hold one of the eligible registrations that would qualify for the exception to the Operations Professional examination requirement. As noted in Section A. above, entry-level operations personnel would not typically be subject to the proposed requirements for Operations Professionals.

E. Continuing Education Requirements for Operations Professionals

The proposed rule change would require that individuals registered as Operations Professionals be subject to FINRA's Regulatory Element and Firm Element continuing education requirements as set forth in proposed FINRA Rule 1250 (Continuing Education Requirements).⁹ The continuing education elements for this registration category would provide more specific learning materials appropriate for an Operations Professional, given the breadth of functions that are covered by this registration requirement.

⁸ If a person's registration in an eligible registration category was revoked within the prior two years, but such person re-qualifies and re-registers in such eligible registration category, he or she may rely on this eligible registration to qualify for the exception to the Operations Professional qualification examination requirement. Further, a suspended registration may not be relied upon as an eligible registration during the suspension period. Similarly, a registration deemed inactive for any reason (e.g., failure to complete continuing education requirements) may not be relied upon as an eligible registration during such inactive period. See also FINRA Rule 8311 (Effect of a Suspension, Revocation, Cancellation, or Bar).

⁹ See Section G. for further discussion of the adoption of NASD Rule 1120 (Continuing Education Requirements) as FINRA Rule 1250.

The Regulatory Element program for Operations Professionals would provide instruction for Operations Professionals to: (1) maintain and improve understanding of the regulatory and ethical aspects associated with the covered functions; (2) identify suspicious activities and/or red flags that could harm a customer, a firm, issuers of securities or the integrity of the marketplace; (3) maintain and improve knowledge and understanding of the covered functions; and (4) assist the Operations Professionals in keeping up with changes in the industry and regulations that impact their work.

Operations Professionals would be required to complete scenario-based modules based on the key content themes of the Operations Professional qualification examination, as described in Section C. above. The breadth and depth of coverage of the modules would be determined through the use of existing industry standards currently used to develop continuing education content and would include input and advice from operations professionals active in the securities industry. Individuals would be expected to complete the Regulatory Element continuing education requirement two years after passing the qualification examination and then every three years thereafter.

Individuals who avail themselves of the proposed exception to the Operations Professional qualification examination requirement with an eligible registration described above would be subject to the Regulatory Element program appropriate for such other registration category. For example, a person who registers as an Operations Professional by holding a General Securities Representative registration (Series 7) under the exception would be subject to the S101 continuing education program in lieu of the Operations Professional Regulatory Element training, and a person who registers by holding a General Securities Principal registration (Series 24) would be subject to the S201

continuing education program in lieu of the Operations Professional Regulatory Element training.

Operations Professionals also would be subject to Firm Element training. To implement this change, as further discussed in Section G. below, the proposed rule change would include Operations Professionals in the definition of “covered registered persons” in proposed FINRA Rule 1250, and would require that firms deliver Firm Element training to Operations Professionals subject to the new registration and qualification requirements.¹⁰

F. Implementation of the Proposed Rule Change

As noted above, any person who meets the depth of personnel criteria described in Section A. and is engaged in one or more covered functions described in Section B. would be required to register with FINRA as an Operations Professional. Such persons would be required to register by doing one of the following, as applicable: (1) requesting Operations Professional registration via Form U4 in CRD and passing the Operations Professional qualification examination; (2) requesting Operations Professional registration via Form U4 in CRD and opting in to such registration based on their holding, or having held within the past two years, an eligible registration;¹¹ or (3)

¹⁰ NASD Rule 1120(b) (Continuing Education Requirements) is currently limited to registered persons who have direct contact with customers in the conduct of the firm’s securities sales, trading and investment banking activities, any person registered as a research analyst pursuant to NASD Rule 1050, and to the immediate supervisors of such persons. The proposed amendments are reflected in the new FINRA rule governing continuing education, FINRA Rule 1250, which is being proposed as part of this rule change. See Section G. below.

¹¹ Persons with an active eligible registration who request Operations Professional registration will be automatically granted Operations Professional registration once they submit such request via Form U4 in CRD, regardless of when such

requesting Operations Professional registration via Form U4 in CRD, registering with FINRA in an eligible registration category and opting in to Operations Professional registration based on such eligible registration.¹²

Members must identify persons required to register as an Operations Professional as of the effective date of the proposed rule change (“Day-One Professionals”) (i.e., persons who meet the depth of personnel criteria and are engaged in one or more covered functions as of the effective date of the proposed rule change). FINRA is proposing a 60-day identification period beginning on the effective date of the proposed rule change during which Day-One Professionals must request registration as an Operations Professional via Form U4 in CRD. During this 60-day period, a Day-One Professional may function in the capacity of an Operations Professional. Day-One Professionals who are identified during the 60-day period and must pass the Operations Professional examination (or an eligible qualification examination) to qualify (i.e., persons who do not hold, and have not within the past two years held, an eligible registration) would be granted 12 months beginning on the effective date of the proposed rule change to pass

persons apply for Operations Professional registration (provided there are no existing deficiencies). See also supra note 7.

¹² If a person elects to register with FINRA as an Operations Professional by newly qualifying in an eligible registration (i.e., does not have an active eligible registration when he or she requests Operations Professional registration via Form U4 in CRD), such person must contact FINRA upon passing the alternative examination to request that the eligible registration be applied to the request for Operations Professional registration. This would include, for example, a person who requests both the Operations Professional and General Securities Representative registrations via Form U4 in CRD and passes the Series 7 examination. Such person would be required to contact FINRA to alert FINRA staff that the General Securities Representative registration will be used as an eligible registration to qualify as an Operations Professional.

such qualifying examination, during which time such persons may function as an Operations Professional.¹³ To be eligible to function as an Operations Professional for the 12-month transition period, Day-One Professionals subject to an examination requirement must request Operations Professional registration via Form U4 in CRD during the 60-day identification period and pass the Operations Professional examination (or an eligible qualification examination) before the expiration of 12 months from the effective date of the proposed rule change.¹⁴ If a Day-One Professional does not pass an acceptable examination by the expiration of the 12-month transition period, such person must cease functioning as an Operations Professional.

The 12-month transition period to pass a qualification examination would only apply to Day-One Professionals. Any person who is not subject to the registration requirements for Operations Professionals as of the effective date of the proposed rule change (i.e., a person who does not meet the depth of personnel criteria and/or is not engaged in one or more covered functions as of the effective date, or persons hired after

¹³ When a person requests Operations Professional registration via Form U4 in CRD during the 60-day identification period, an examination window for the Operations Professional qualification examination will open in CRD that expires 12 months from the effective date of the proposed rule change. After the 60-day identification period, the examination window for the Operations Professional qualification examination will open for the standard 120 days.

¹⁴ Members should note that the standard examination window in CRD applicable to a particular registration category will apply notwithstanding the 12-month examination window established for purposes of the transition period. The 12-month examination window is only for the Operations Professional qualification examination. Thus, a person who elects to qualify, for example, by passing the Series 7 examination would have only 120 days to take and pass the Series 7 examination once the window for such examination is opened in CRD. Members should plan accordingly so that associated persons are prepared to take the requisite examination within the prescribed window for that registration category, and that any requisite examination is passed before the expiration of the 12-month transition period for Day-One Professionals.

the effective date of the proposed rule change who will be placed in such roles) (“non-Day-One Professionals”) would be required to register as an Operations Professional and, if applicable, pass the Operations Professional qualification examination (or an eligible qualification examination), prior to engaging in any activities that would require such registration. The 60-day identification period and the 12-month transition period do not affect the obligations of non-Day-One Professionals to register as an Operations Professional prior to engaging in functions that would require such registration. However, any non-Day-One Professional associated with a non-clearing member who must pass the Operations Professional qualification examination (or an eligible qualification examination) to obtain registration would be granted a grace period of 120 days beginning on the date such person requests Operations Professional registration via Form U4 in CRD to pass such qualifying examination, during which time such person may function as an Operations Professional. FINRA believes that allowing a person associated with a non-clearing member to function as an Operations Professional for a 120-day period will enable these firms to manage their more limited staffs to comply with the proposed registration requirements without disrupting those firms’ obligations to customers. Non-Day-One Professionals associated with a self-clearing or clearing member would not have the benefit of the 120-day grace period and would be required to register as an Operations Professional prior to engaging in activities that would require such registration.

Members would be responsible for tracking and monitoring their associated persons to ensure that such persons are registered, and conducting their activities, in compliance with the time frames described above.

G. FINRA Continuing Education Rule

The proposed rule change would adopt NASD Rule 1120 (Continuing Education Requirements) as new FINRA Rule 1250 (Continuing Education Requirements). In addition to the proposed change noted in Section E., which would expand the scope of “covered registered persons” subject to the Firm Element to include persons registered as Operations Professionals, the proposed rule change would make additional minor changes to NASD Rule 1120 to update cross-references and reflect the conventions of the consolidated FINRA Rulebook.

NASD Rule 1120 and Incorporated NYSE Rule 345A were adopted in 1995 in response to the recommendation of a task force, which subsequently became the Securities Industry Regulatory Council on Continuing Education (the “Council”),¹⁵ to create uniform continuing education requirements in the securities industry. As advised by the Council, the continuing education requirements include a Regulatory Element and a Firm Element. The NASD and Incorporated NYSE rules are nearly identical in keeping with the goals of the Council to create uniform continuing education requirements.¹⁶

The Regulatory Element consists of periodic computer-based training on regulatory, compliance, ethical, supervisory subjects and sales practice standards. A registered person is required to participate and complete a designated Regulatory Element

¹⁵ The Council is comprised of up to 16 industry members from broker-dealers, representing a broad cross section of industry firms, and representatives from SROs as well as liaisons from the SEC and the North American Securities Administrators Association (“NASAA”).

¹⁶ The proposed rule change would not delete Incorporated NYSE Rule 345A (and its Interpretation). Rather, FINRA expects to address Incorporated NYSE Rule 345A (and its Interpretation) and propose additional changes to proposed FINRA Rule 1250 as part of the consolidated registration and qualification rules. See Regulatory Notice 09-70 (December 2009).

within a 120-day period that commences with the second anniversary of such person's initial securities registration, and reoccurs every three years thereafter for as long as such person remains in the securities business. Failure to complete the Regulatory Element will result in a registered person's registration becoming inactive and such person cannot conduct a securities business on behalf of the member until the requirement is met.¹⁷

The Firm Element requirements currently apply to any person registered with a member who has direct contact with customers in the conduct of the member's securities sales, trading and investment banking activities, any person registered as a research analyst pursuant to NASD Rule 1050, and to the immediate supervisors of such persons (collectively, "covered registered persons"). However, as noted above, the proposed rule change would expand the scope of "covered registered persons" subject to the Firm Element to include persons registered as Operations Professionals. The Firm Element consists of annual, member-developed and administered training programs designed to keep covered registered persons current regarding securities products, services and strategies offered by the member. The Firm Element requires members to annually evaluate and prioritize their training needs (i.e., conduct a Needs Analysis and develop a written plan). In planning, developing and implementing the Firm Element training, each member must take into consideration its size, organizational structure, scope of business, types of products and services it offers, as well as regulatory developments and the

¹⁷ A registered person will be required to retake the Regulatory Element in the event such person is: (1) subject to a statutory disqualification as defined by Section 3(a)(39) of the Exchange Act; (2) subject to a suspension or imposition of a fine of \$5,000 or more by an SRO or other securities governmental agency; or (3) ordered to do so as a sanction in a disciplinary action by an SRO or other securities governmental agency.

performance of its covered registered persons in the Regulatory Element. FINRA may require a member to provide specific training to a member's covered registered persons as FINRA deems appropriate. Each member must administer its Firm Element Continuing Education Program in accordance with its annual Needs Analysis and written plan, and must maintain records documenting the content of the program and completion of the program by covered registered persons.

FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 90 days following Commission approval. The implementation date will be no later than 240 days following Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹⁸ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes the proposed rule change to expand FINRA's registration and continuing education requirements to Operations Professionals will help ensure that investor protection mechanisms are in place in all areas of a member's business that could harm the member, a customer, the integrity of the marketplace, or the public.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

¹⁸ 15 U.S.C. 78o-3(b)(6).

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The proposed rule change was published for comment in Regulatory Notice 10-25 (May 2010) (the "Notice"). Forty-nine comment letters were received in response to the Notice.¹⁹ A copy of the Notice is attached as Exhibit 2a. A list of the comment letters received in response to the Notice is attached as Exhibit 2b. Copies of the comment letters received in response to the Notice are attached as Exhibit 2c. Below is a summary of the comments and FINRA's responses.

General Concerns Regarding the Scope of the New Registration Category

Certain commenters generally opposed the proposed rule change stating that it is overly broad and ambiguous, poorly defined, imposes requirements that are unnecessary to meet FINRA's stated objectives and may have unintended consequences.²⁰ Other commenters argued that licensing requirements do not make people honest or increase their efficiency or proficiency²¹ and that no amount of licensing will change failures of human character.²² Two commenters noted that frauds are almost always committed on the frontlines by individuals who are already licensed.²³ Additionally, certain commenters opposed registration requirements for covered persons because their work is

¹⁹ All references to the commenters under this Item are to the commenters as listed in Exhibit 2b.

²⁰ ACLI, AIC, Bank of America, Crowell, ESI, Horace Mann, IPA, IRI, Modern Woodmen, Navidar, NSCP, PSD, Quasar, UPFS, Scottrade, SIFMA, Sutherland, TIAA, Wellington and Wells Fargo.

²¹ Mutual Trust.

²² AIC and Wells Fargo.

²³ AIC and PSD.

already supervised and approved by a firm principal²⁴ and holding principals accountable for failures in these areas would be more cost effective.²⁵ Numerous commenters proposed an alternative approach under which firms would delegate each of the covered functions to existing registered principals of the firm and reflect such assignments in the firm's written supervisory procedures ("WSPs").²⁶ Other commenters noted the proposed rule change is unnecessary because people who handle customer funds go through background checks and fingerprinting.²⁷

In response, FINRA notes that covered persons are performing regulated broker-dealer functions on behalf of a member, and believes such persons should be subject to registration, examination and continuing education requirements to ensure that they attain and maintain specified levels of competence and knowledge to properly carry out their responsibilities to the member and its customers. FINRA does not agree that principal approval or background checks and fingerprinting are sufficient safeguards to ensure members' operations departments are functioning in a manner that will promote investor protection to the highest level possible. The proposed rule change is intended, among other things, to increase covered persons' awareness and knowledge that they are operating in a regulated environment designed to protect investors' interests and the integrity of the operations of a broker-dealer. In addition, the proposed rule will help to ensure that any fraudulent activity that may start in the front office of a firm cannot be

²⁴ Crowell, IRI, M. Griffith, PSD and RiverStone.

²⁵ Crowell and Wellington.

²⁶ IRI, Nationwide, PSD and Sutherland.

²⁷ PSD, RiverStone and Wells Fargo.

processed without passing through a properly registered and trained Operations Professional. Requiring registration, testing and training for Operations Professionals should further strengthen members' compliance with securities laws, rules and regulations.

Certain commenters expressed concern that requiring registration of covered persons will dramatically limit the pool of candidates that may be considered for hiring when personnel changes occur in operations departments.²⁸ As an initial matter, FINRA notes that it is always correct to state that conduct once regulated becomes constrained by that regulation, but that observation by itself is not a credible reason not to engage in the regulation. The proper test is whether that regulation is appropriately tailored and needed in furtherance of the interests of investors and the securities markets. The immediate prior paragraph restates those interests, and the depth of personnel as set forth in Section A. of the Purpose section demonstrates the appropriate tailoring of the proposed regulation. Finally, Section D. of the Purpose section indicates that many candidates for positions that would require registration may possess an eligible registration and qualify for an exception from the requirement to take the Operations Professional qualification examination.

Two commenters suggested FINRA reduce the obligations for Operations Professionals and specify that not all of the rules applicable to associated persons apply to such persons since they are generally not customer-facing personnel.²⁹ Certain other commenters sought clarification that the proposed rule change does not eliminate or limit

²⁸ NPB and RiverStone.

²⁹ TIAA and Wells Fargo.

the ability of a securities issuer and its associated persons to rely on the issuer exemption under Exchange Act Rule 3a4-1³⁰ to avoid broker-dealer registration requirements.³¹

Another commenter requested that FINRA provide guidance on the impact of the proposed rule change on FINRA Rule 2310 (Direct Participation Programs) and clearly state that the salaries of Operations Professionals be categorized as “non-transaction-based-compensation” and that there is a blanket exception from “underwriting compensation” for Operations Professionals.³²

FINRA does not agree that Operations Professionals should be subject to a limited set of rules. Covered persons are not only associated persons of a member but their activities are crucial enough to the business of a member to require registration with FINRA. The proposed rule change does not alter a person’s status as an associated person under Exchange Act Rule 3a4-1 or otherwise, nor does it address the definitions of certain types of compensation under FINRA rules. However, FINRA recognizes that additional guidance may be needed following the adoption of the proposed rule change and will address interpretive questions as needed, similar to FINRA’s approach to other regulatory initiatives with wide-ranging and novel impacts.

Covered Persons for Inclusion in the New Registration Category

Certain commenters requested clarification with respect to proposed FINRA Rule 1230(b)(6)(A)(i) regarding scope of the term senior management and whether this provision applies beyond senior managers with primary or direct responsibility over the

³⁰ 17 CFR § 240.3a4-1.

³¹ PSD, Sutherland and TIAA.

³² IPA.

covered functions.³³ Two commenters advocated limiting the depth of personnel for the proposed rule change to a single category for senior management with responsibility over the covered functions, and requiring firms to maintain policies and procedures reasonably designed to ensure that operations personnel have an awareness of investor protection mechanisms in place at a firm.³⁴

FINRA believes this provision is clear as originally proposed and, while FINRA understands titles may differ between firms, members should be able to identify operations personnel that would be subject to proposed Rule 1230(b)(6)(A)(i) based on their functions and responsibilities as senior managers overseeing the covered functions. FINRA would consider any senior manager in the chain of command responsible for a covered function to be subject to the proposed rule, up to and including the Principal Operations Officer.³⁵ FINRA does not agree that “covered persons” should be limited to senior management with responsibility over the covered functions because the proposed registration category is intended to include other individuals who exercise supervisory and discretionary authority in direct furtherance of the covered functions. Accordingly, FINRA has not proposed changes to proposed FINRA Rule 1230(b)(6)(A)(i).

Proposed FINRA Rule 1230(b)(6)(A)(ii) would include as covered persons supervisors, managers or other persons responsible for approving or authorizing work, including work of other persons, in direct furtherance of the covered functions. One

³³ IRI, Nationwide, NSCP and TIAA.

³⁴ Wellington and Wells Fargo.

³⁵ See Regulatory Notice 09-70 (December 2009) for a discussion of the Principal Operations Officer registration category. See also infra note 61 and accompanying text.

commenter suggested the proposed rule explicitly state that covered persons are limited to those persons with decision-making and/or oversight authority.³⁶ Certain commenters requested that FINRA clarify what is meant by the phrase “approve or authorize work.”³⁷ Other commenters stated that this provision is written too broadly;³⁸ creates potential for misinterpretation in determining how far up or down the reporting chain this registration requirement would apply;³⁹ could sweep in affiliate employees, mid or low level employees,⁴⁰ third-party vendors⁴¹ and margin clerks;⁴² and that it should be limited to supervisors, managers or other persons responsible for primary oversight of covered functions, including managers for dual hat employees.⁴³ One commenter suggested that FINRA revise this provision to clarify that supervisors and managers be senior members of their respective departments or units.⁴⁴ Numerous commenters recommended deleting the phrase “work of other persons” because it is unclear.⁴⁵

³⁶ Morgan Stanley.

³⁷ ESI, NFP, TIAA and UPFS.

³⁸ ACLI, NSCP, Quasar and Wells Fargo.

³⁹ ACLI.

⁴⁰ Morgan Stanley.

⁴¹ Schwab.

⁴² Scottrade.

⁴³ ARM, TIAA and Wells Fargo.

⁴⁴ Bank of America.

⁴⁵ Bank of America, IPA, SIFMA and Wells Fargo.

FINRA believes proposed FINRA Rule 1230(b)(6)(A)(ii) is clear as proposed and notes that it consulted with industry representatives in developing the proposed rule change, including the definition and appropriate depth of personnel to be subject to the Operations Professional registration category. As noted above, FINRA believes members will be able to identify supervisors, managers or other persons responsible for approving or authorizing work in direct furtherance of the covered functions based on their functions and responsibilities. The phrases “approve or authorize work” and “work of other persons” are not legal terms of art but, rather, comport with commercially understood operating terms and do not require clarification. Accordingly, FINRA has not revised this provision as suggested by the commenters; however, FINRA proposes a minor modification to the original proposal by re-locating the phrase “including the work of other persons” to streamline the provision, as reflected in Section A. of the Purpose section.

As originally proposed in the Notice, FINRA Rule 1230(b)(6)(A)(iii) required registration as an Operations Professional for persons with the authority or discretion to commit the member’s capital in direct furtherance of the covered functions or to commit the member to any contract or agreement (written or oral) in direct furtherance of the covered functions. Certain commenters stated this provision is unclear and too far-reaching⁴⁶ and noted it would capture persons who perform routine, daily activities, or enter into agreements consistent with firm policies that have no material impact on firm operations (including margin clerks, who often have flexibility to obligate firm capital up

⁴⁶ Bank of America, TIAA and NSCP.

to certain limits).⁴⁷ Two commenters noted that the provision should only be triggered if the contracts are sufficiently material to the firm.⁴⁸ One commenter noted that it may be so broad as to require registration of junior associates if they sign or approve contracts, retain vendors or make clerical postings to the books of a member.⁴⁹ Another commenter noted that this provision is inconsistent with the first two categories of covered persons, which focus on senior managers, supervisors and those who approve work in the covered functions.⁵⁰ Another commenter requested clarification with respect to the term “firm capital” because it could sweep in persons who approve the payment of vendor invoices for services related to some aspect of a covered function.⁵¹ Two commenters noted it is unclear what individuals, other than those engaged in or supervising securities lending activities, the proposed third category of covered persons intends to cover and suggested certain amendments to clarify the proposal with respect to such persons.⁵²

Based on the comments, FINRA has revised the third category of covered persons from the original proposal in the Notice, as discussed in Section A. of the Purpose section. Under the revised proposal, FINRA Rule 1230(b)(6)(A)(iii) would require persons with the authority or discretion materially to commit a member’s capital in direct furtherance of the covered functions or to commit a member to any material contract or

⁴⁷ T. Rowe Price and Wells Fargo.

⁴⁸ Bank of America and TIAA.

⁴⁹ Bank of America.

⁵⁰ SIFMA.

⁵¹ Scottrade.

⁵² Morgan Stanley and SIFMA.

agreement (written or oral) in direct furtherance of the covered functions to register as an Operations Professional. FINRA purposefully did not limit the third category of covered persons to supervisors and managers because the capacity to make material discretionary decisions above a member's pre-established spending guidelines and risk management policies under this provision is not confined to senior or supervisory personnel.

Numerous commenters suggested that FINRA add language to the proposed rule to clarify, as stated in the Notice, that the proposed rule does not apply to persons who perform functions ancillary to a covered function or whose function is to serve a role that can be viewed as supportive of, or advisory to, the performance of a covered function, such as internal audit, legal or compliance personnel.⁵³ One commenter further urged FINRA to add rule language to note that individuals performing quality assurance and quality control functions in direct furtherance of a covered function are similarly excluded.⁵⁴ One commenter noted that registering clerical personnel only increases costs unnecessarily and creates hiring barriers for new applicants.⁵⁵ One commenter requested that FINRA provide specific examples of activities it deems ministerial or clerical in nature, especially when such activities require Financial and Operations Principal review and control procedures.⁵⁶

Based on the comments, and as noted in Section A. of the Purpose section of this rule filing, FINRA is proposing supplementary material .06 to the proposed rule to clarify

⁵³ Bank of America, FSI, NSCP, Scottrade, SIFMA and TIAA.

⁵⁴ TIAA.

⁵⁵ Martin Nelson.

⁵⁶ Quasar.

that any person whose activities are limited to performing a function ancillary to a covered function, or whose function is to serve a role that can be viewed as supportive of or advisory to the performance of a covered function (e.g., internal audit, legal or compliance personnel who review but do not have primary responsibility for any covered function), or who engages solely in clerical or ministerial activities in a covered function would not be required to register as an Operations Professional. FINRA declines to provide examples of clerical and ministerial activities at this time, believing the term to be well understood in the industry;⁵⁷ however, as noted above, FINRA will consider issuing additional guidance as needed regarding the categories of persons subject to the Operations Professional registration category.

One commenter encouraged FINRA to clarify whether an Operations Professional must be supervised by a qualified supervisory principal.⁵⁸ Another commenter requested clarification regarding whether a firm must assign or designate an Operations Professional and whether a person who is already a registered principal must register as an Operations Professional.⁵⁹

As noted above, as registered persons, Operations Professionals will be subject to all FINRA rules applicable to associated persons and/or registered persons. Accordingly, pursuant to NASD Rule 3010(a)(5), each Operations Professional must be assigned to an appropriately registered representative(s) and/or principal(s) who shall be responsible for supervising that person's activities. Additionally, FINRA expects that each member

⁵⁷ See, e.g., NASD Rule 1060 (Persons Exempt from Registration).

⁵⁸ Pershing.

⁵⁹ Crowell.

would have at least one registered Operations Professional, who often may be the member's Financial and Operations Principal and/or the Principal Operations Officer. In this regard, neither principal registration, nor representative registration in another category, obviates the requirement for a covered person to register as an Operations Professional. As noted in Section D. of the Purpose section, there are numerous eligible registrations that would except such registered persons from the requirement to pass the Operations Professional qualification examination.

Certain commenters inquired as to the proposed rule change's relationship to, and consistency with, the proposals set forth in Regulatory Notice 09-70⁶⁰ and two commenters requested clarification regarding how the proposed requirement under Regulatory Notice 09-70 that firms appoint a distinct Principal Operations Officer and a distinct Principal Financial Officer intersects with the proposed Operations Professional designation.⁶¹

The proposed rule change does not conflict with the proposals set forth in Regulatory Notice 09-70. The proposed rule change should be read as a separate registration requirement that will be added to the consolidated FINRA registration rules. To note, the proposed rule change would include persons engaged in or supervising stock loan/securities lending activities that meet the depth of personnel as a covered person in Section A. above. FINRA also is proposing separate registration requirements for a "Securities Lending Representative" and a "Securities Lending Supervisor" in Regulatory Notice 09-70; consequently, firms should be aware of both sets of proposed

⁶⁰ PSD, Sutherland and Wells Fargo.

⁶¹ IRI and TIAA.

requirements.⁶² With respect to the proposed requirements in Regulatory Notice 09-70 for Principal Operations Officers and Principal Financial Officers, such persons likely would be required to register as an Operations Professional, depending on whether they meet the criteria of a covered person as described in Section A. of the Purpose section. The requirement for a covered person to register as an Operations Professional applies regardless of any other, separate registration requirements; however, such other registration may be used as an eligible registration to qualify a covered person for an exception from the requirement to take the Operations Professional qualification examination.

One commenter noted the proposed rule change could have costly and burdensome implications regarding state registration and licensing so FINRA should be as clear as possible in defining who is covered under the proposed rule change.⁶³ As noted above, FINRA believes the definitions of covered persons are sufficiently clear and will provide additional guidance as needed regarding the scope of persons subject to the new requirements.

Covered Functions for Inclusion in the New Registration Category

Numerous commenters stated that the covered functions as proposed in the Notice are too broad, unclear and inconsistent, and will incur unnecessary costs for firms.⁶⁴ The

⁶² See supra note 5.

⁶³ NSCP.

⁶⁴ Commonwealth, Crowell, ESI, FSI, IPA, IRI, Modern Woodmen, Morgan Stanley, NFP, Northwestern Mutual, NSCP, PSD, TIAA, SIFMA, Sutherland, UPFS and WSFG.

commenters requested more precise descriptions of the covered functions.⁶⁵ One commenter requested that FINRA clarify that the covered functions apply only to activities performed by or on behalf of a firm's securities and investment banking business.⁶⁶ Two commenters urged FINRA to group dependent technology-related covered functions into a single entry.⁶⁷ Another commenter suggested that certain functions be deleted because they are roles that support other covered functions and are not stand-alone functions.⁶⁸

Based on the comments, FINRA has made certain changes to the covered functions as originally proposed in the Notice to clarify and streamline the proposed rule. As a general matter, FINRA has revised the list of covered functions, as reflected in Section B. of the Purpose section, to group related functions together. Substantive revisions to the covered functions are described in detail below.

To clarify the proposed rule change, FINRA has revised Rule 1230(b)(6)(B)(i) (as originally proposed in the Notice) by limiting this covered function to the “[a]pproval of pricing models used for valuations,” instead of the “[d]evelopment and approval of pricing models used for valuations.” FINRA also moved this provision to proposed Rule 1230(b)(6)(B)(x).

⁶⁵ Commonwealth, Crowell, ESI, FSI, IPA, IRI, Modern Woodmen, Morgan Stanley, NFP, Northwestern Mutual, NSCP, PSD, TIAA, SIFMA, Sutherland, UPFS and WSFG.

⁶⁶ TIAA.

⁶⁷ Morgan Stanley and NSCP.

⁶⁸ Schwab.

Two commenters requested a definition for the term “client on-boarding” in proposed FINRA Rule 1230(b)(6)(B)(v) (as originally proposed in the Notice).⁶⁹ FINRA notes from its consultation with industry representatives in the rule development process that this is a term commonly used for this covered function and believes the proposed rule text provides sufficient clarity (*i.e.*, “[c]lient on-boarding (customer account data and document maintenance)”).

Numerous commenters requested clarification with respect to the scope of proposed FINRA Rule 1230(b)(6)(B)(vi) (as originally proposed in the Notice), the covered function addressing the “[c]apturing of business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements.”⁷⁰ One commenter noted that this provision should apply only to individuals who “define and approve” business requirements, rather than individuals who “capture” such requirements.⁷¹ Similarly, to reduce the likelihood of inadvertently capturing personnel who merely prepare initial drafts of business requirements documents and who perform routine quality assurance or quality control testing, two commenters suggested incorporating the concepts of “accepting” and “approving” in lieu of “capturing” and “defining” for the covered functions that include these terms.⁷²

⁶⁹ PSD and Sutherland.

⁷⁰ ESI, FSI, Horace Mann, Modern Woodmen, NFP, Scottrade, TIAA and UPFS.

⁷¹ Northwestern Mutual.

⁷² Bank of America and SIFMA.

Based on the comments, FINRA has revised the original proposal to eliminate the concept of “capturing” in proposed FINRA Rule 1230(b)(6)(B)(vi). The proposed rule change renumbers this provision as proposed FINRA Rule 1230(b)(6)(B)(xiii) and includes as a covered function, “[d]efining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements.” FINRA has not eliminated the concept of “defining” from the covered functions because it believes covered persons who are responsible for defining and approving business system requirements are professional level staff that should be subject to registration with FINRA. The covered functions generally would not include a person who engages in administrative responsibilities, such as an initial drafter or a code developer. However, a person who supervises or approves such activities generally would be required to register as an Operations Professional.

Additionally, certain commenters requested clarification with respect to proposed Rule 1230(b)(6)(B)(vii) (as originally proposed in the Notice), which includes as a covered function, “[w]ith respect to the covered functions, defining and approving business security requirements and policies for information technology (including, but not limited to, systems and data).”⁷³ One commenter noted that this function should only require persons who “approve” business requirements for systems and information technology to register so that the final approvals for technology requirements are performed by licensed Operations Professionals.⁷⁴

⁷³ ESI, FSI, Horace Mann, Modern Woodmen, NFP, Scottrade and UPFS.

⁷⁴ Morgan Stanley.

FINRA has made minor changes to the original proposal with respect to Rule 1230(b)(6)(B)(vii). The proposed rule change renumbers this provision as proposed FINRA Rule 1230(b)(6)(B)(xiv) and includes as a covered function, “[d]efining and approving business security requirements and policies for information technology, including, but not limited to, systems and data, in connection with the covered functions.” As noted above, FINRA believes that covered persons engaged in defining and approving business security requirements and policies for information technology should be registered as Operations Professionals.

One commenter requested clarification with respect to proposed Rule 1230(b)(6)(B)(viii) (as originally proposed in the Notice), which includes as a covered function, “[d]efining information entitlement policy in connection with the covered functions.”⁷⁵

Based on the comments and in line with the changes noted above, FINRA has revised Rule 1230(b)(6)(B)(viii). The proposed rule change renumbers this provision as proposed FINRA Rule 1230(b)(6)(B)(xv) and includes as a covered function, “[d]efining and approving information entitlement policies in connection with the covered functions.”

One commenter recommended that FINRA combine paragraphs (b)(6)(B)(vii) and (viii) (as originally proposed in the Notice) since both sections cover overlapping sets of supervisors in the Information Management area.⁷⁶ Another commenter noted that proposed FINRA Rules 1230(b)(6)(B)(vi), (vii), (viii) and (xv) are not separate functions

⁷⁵ Scottrade.

⁷⁶ Bank of America.

but are ancillary to other covered functions and may require managers from both the actual covered functions and these ancillary areas to register.⁷⁷ One commenter requested clarification that FINRA Rules 1230(b)(6)(B)(vi), (vii) and (viii) (as originally proposed in the Notice) are limited to only those individuals directly employed by the FINRA member.⁷⁸ Another commenter suggested limiting these provisions to individuals responsible for ensuring that systems related to sales and trading and to covered functions meet business and regulatory requirements and “information security” (firewalls, data access, and system entitlements in connection with the covered functions).⁷⁹

FINRA believes that the proposed revisions to these provisions noted above clarify the proposed rule and is not proposing further changes at this time. FINRA notes that these covered functions should remain as separate items since they address different activities (e.g., defining, approving and validating business requirements for sales and trading systems or other systems relating to the covered functions vs. defining and approving entitlement policies in connection with the covered functions) and firms may have different internal reporting structures so that these activities are not part of the same area or subject to the same supervisory scheme.

Certain commenters suggested deleting proposed Rule 1230(b)(6)(B)(xv) (as originally proposed in the Notice), which includes as a covered function, “[p]osting entries to the books and records of a member in connection with the covered functions,”

⁷⁷ NSCP.

⁷⁸ IPA.

⁷⁹ SIFMA.

because it is ambiguous, too broad⁸⁰ and may sweep in clerical staff.⁸¹ Another commenter requested clarification regarding the term “books and records” and requested that FINRA add a reference to Exchange Act Rule 17a-3⁸² or MSRB Rule G-8.⁸³ Two commenters recommended that FINRA revise this provision to tailor it to separate regulatory issues such as customer protection or financial responsibility concerns.⁸⁴

FINRA has revised Rule 1230(b)(6)(B)(xv) to clarify this covered function. The proposed rule change renumbers this provision as FINRA Rule 1230(b)(6)(B)(xvi) and includes as a covered function, “[p]osting to a member’s books and records in connection with the covered functions to ensure integrity and compliance with the federal securities laws and regulations and FINRA rules.”

One commenter noted that some of the covered functions may cause confusion with respect to other registration categories, including proposed FINRA Rules 1230(b)(6)(B)(ix) and (xiv) (as originally proposed in the Notice), the covered functions for “[f]inancial controller (including general ledger)” and “[f]inancial regulatory reporting,” respectively, and the functions supervised by the financial and operations principal, and may overlap with the proposed designation of the Principal Operations Officer under Regulatory Notice 09-70.⁸⁵ Based on the comment, FINRA has revised

⁸⁰ Bank of America and SIFMA.

⁸¹ Crowell and SIFMA.

⁸² 17 CFR § 240.17a-3.

⁸³ Rockfleet.

⁸⁴ Morgan Stanley and SIFMA.

⁸⁵ IRI.

these items. The proposed rule change renumbers these items as proposed FINRA Rules 1230(b)(6)(B)(xi) and (xii), respectively, and includes as covered functions, “[f]inancial control, including general ledger and treasury” and “[c]ontributing to the process of preparing and filing financial regulatory reports.” FINRA does not agree that the proposed rule change causes confusion with respect to other registration requirements. Members must determine whether the proposed registration requirements for Operations Professionals would apply to an associated person based on his or her functions and responsibilities notwithstanding any other, separate registration requirements.

One commenter noted that the title of the proposed registration category is too narrow and not reflective of the covered functions. Alternatively, the commenter suggested that the registration category should be titled “Operations, Support or Securities Lending Professionals.”⁸⁶ FINRA believes that the proposed title for the new registration category, Operations Professionals, is appropriate and succinctly captures the individuals to which the proposed requirements would apply given the breadth of activities covered under the proposed rule change.

Certain commenters requested clarification that ongoing insurance company functions relating to variable annuity contracts as well as other functions performed by insurance company staff are not included in the covered functions.⁸⁷ FINRA does not intend to make any categorical exclusions from the covered functions. The proposed requirements will apply if a person meets the depth of personnel criteria and engages in

⁸⁶ SIFMA.

⁸⁷ IRI, PSD and Sutherland.

one or more covered function on behalf of a member regardless of where they are employed.

Operations Professional Qualification Examination

One commenter noted that elements of the qualification examination and continuing education requirements have no relevance to the products and operations of limited purpose broker-dealers that comprise more than 50% of FINRA’s membership.⁸⁸ Other commenters noted that the two areas of proposed examination coverage, “essential product and market knowledge for an Operations Professional” and “knowledge associated with operations activities,” should be eliminated from the examination curriculum because they undercut FINRA’s premise that it will not be a “competency” examination and render the test extremely challenging for many operations personnel since they lack the background and experience to pass the examination and have little testing experience.⁸⁹ Another commenter similarly noted that the proposed examination requirement could result in well-qualified employees losing their jobs and firms’ operations departments could have compromised functionality, and supervision (*i.e.*, a “brain drain”) of qualified operations personnel, thus undermining the goals of the proposal.⁹⁰

Numerous commenters stated that an examination is unnecessary because training and education for operations personnel should be addressed in a member’s WSPs⁹¹ and

⁸⁸ ACLI.

⁸⁹ NSCP and ACLI.

⁹⁰ NSCP.

⁹¹ FSI, M. Griffith, Navidar and PSD.

registered principals are responsible for training operations personnel.⁹² To reduce cost burdens on firms, certain commenters recommended ongoing training requirements as an alternative to registration and testing of operations personnel.⁹³ Certain other commenters noted that FINRA can address operations personnel through registration and continuing education⁹⁴ and an examination not based on competency serves no essential function.⁹⁵ One commenter stated that the Series 27 and 28 examinations already test for the covered functions, so a new exam is a poor use of member firm fees and will unnecessarily delay implementation of the proposal.⁹⁶

One commenter noted that based on the definition of a covered person, the Operations Professional qualification examination should be a principal-level examination with corresponding continuing education requirements.⁹⁷ One commenter requested that FINRA publish a study outline for notice and comment prior to making the test effective.⁹⁸ Another commenter recommended that FINRA offer the proposed

⁹² Modern Woodmen and Martin Nelson.

⁹³ Harrison, NSCP, RMOA and Wells Fargo.

⁹⁴ Commonwealth, ESI, FSI, Horace Mann, NFP, UFPS and WSFG.

⁹⁵ Horace Mann, JRCO, Modern Woodmen, NSCP, RMOA, Rockfleet, UPFS and WSFG.

⁹⁶ Rockfleet.

⁹⁷ Rockfleet.

⁹⁸ NSCP.

examination as an optional test for people who want to learn about back-office, but not as a mandatory examination for Operations Professional registration.⁹⁹

FINRA believes the qualification examination requirement is appropriate as proposed. The proposed examination is being tailored to test for basic securities industry knowledge and ethics. Although the examination will not test for proficiency with respect to the specific covered functions, FINRA believes there is value in an examination that tests for general knowledge about the securities industry. The proposed examination will be appropriately tailored to individuals subject to the proposed registration requirements. It is crucial for covered persons to understand their professional responsibilities, including key regulatory and control themes, as well as the importance of identifying and escalating red flags that may harm a firm, its customers, the integrity of the marketplace, or the public.

Additionally, FINRA believes a representative-level examination is appropriate for Operations Professionals because the proposed registration category is based on functions performed by operations personnel and is not limited to supervisory or managerial staff (e.g., persons who fall within proposed FINRA Rule 1230(b)(6)(A)(ii) and (iii)).

One commenter suggested that FINRA modify the period for retaking the Operations Professional qualification examination if an applicant fails to 30 days like the Series 55.¹⁰⁰ FINRA does not intend to change its policy regarding the re-taking of qualification examinations for the proposed Operations Professional examination at this

⁹⁹ M. Griffith.

¹⁰⁰ Schwab.

time. FINRA will reconsider the policy if it finds it to be a necessary step when the qualification examination for Operations Professionals is administered.

Exception to Operations Professional Examination Requirement

One commenter noted that the proposed exceptions are so numerous that they dilute the regulatory intent of the proposed rule change; instead, FINRA should grant a limited number of exceptions to current operations employees.¹⁰¹ One commenter recommended FINRA incorporate an exception for certain small firms.¹⁰² One commenter suggested that registered principals should be completely exempt from the proposed Operations Professional requirements;¹⁰³ other commenters suggested that the proposed rule change should only apply to currently unregistered persons because the potential costs and burdens involved with tracking and monitoring multiple registrations outweigh the benefits.¹⁰⁴ One commenter suggested FINRA permit firms to identify any relied upon registration for the proposed exception in their WSPs instead of a U4 amendment, as is required currently for any person in a supervisory role.¹⁰⁵

Certain other commenters recommended a grandfather provision for experienced persons who have worked in operations areas for a certain time period (e.g., three¹⁰⁶ or

¹⁰¹ NASAA.

¹⁰² Freestone.

¹⁰³ NSCP.

¹⁰⁴ Northwestern Mutual and T. Rowe Price.

¹⁰⁵ T. Rowe Price.

¹⁰⁶ Commonwealth.

five¹⁰⁷ years) prior to the implementation of the proposed rule.¹⁰⁸ Two commenters requested that FINRA extend the proposed exception to registrations held beyond the two-year look back.¹⁰⁹ One commenter noted that there are costs and burdens of a two-year look back without a concomitant benefit.¹¹⁰ Additionally, one commenter suggested that FINRA consider incorporating standards within its Qualification Examination Waiver Guidelines that will accommodate individuals that possessed an eligible registration within a reasonably recent time period and have been performing an Operations Professional role for a reasonable period of time.¹¹¹ This commenter also suggested that FINRA finalize the permissive registration regime contemplated in Regulatory Notice 09-70 prior to implementing a new Operations Professional designation, which would provide firms and their personnel with the option to maintain licenses while the registered person occupies a non-registered position.¹¹²

¹⁰⁷ FSI, PSD and Sutherland.

¹⁰⁸ FSI, Modern Woodmen, NFP, UPFS and WSFG.

¹⁰⁹ Nationwide and TIAA.

¹¹⁰ IRI.

¹¹¹ TIAA.

¹¹² TIAA.

FINRA believes the proposed rule change clearly articulates the exception to the Operations Professional qualification examination requirement.¹¹³ A primary purpose of the proposed qualification examination is to assess a covered person's basic understanding of the securities industry and the requirement to take a registration examination serves to alert such person of the role he or she plays in this highly regulated environment. Thus, FINRA believes the eligible registrations (and corresponding examinations) serve as a valid proxy for the Operations Professional examination requirement.

FINRA believes the two-year look back for the eligible registrations is appropriate and has not revised the proposal to extend this time period. The proposed look back is based on the window during which an associated person remains eligible to re-activate his or her registration based on previously qualifying for and holding such registration. A person who qualifies for the proposed exception based on their having held an eligible registration within the two years immediately prior to registering as an Operations Professional would be required to first re-activate such eligible registration prior to requesting Operations Professional registration.¹¹⁴ Under NASD Rules 1021 and 1031, members are permitted to maintain or make application for registration as a registered principal or registered representative for a person who performs back-office operations, among other things. As such, firms are not currently prohibited from carrying

¹¹³ The Notice included as an eligible registration the General Securities Principal – Sales Supervisor Module (Series 23). FINRA has removed this examination from the list of eligible registrations. A person who passes the Series 9/10 and the Series 23 may obtain the General Securities Principal (Series 24) registration, but a person who passes solely the Series 23 is not considered registered in any capacity.

¹¹⁴ See supra note 7.

registrations for back-office personnel. FINRA has determined not to incorporate a grandfather provision for previously unregistered operations personnel. FINRA believes that all covered persons benefit from an examination requirement even if they have been working in the same position for an extended period. As noted above, the proposed Operations Professional examination will not test on specific job functions but will focus on general securities industry knowledge and key regulatory themes.

Continuing Education

Certain commenters encouraged FINRA to clarify whether the proposal requires currently registered principals to take both the S101 continuing education module and the S201¹¹⁵ and requested that FINRA refine the continuing education requirements to reflect FINRA's diverse membership.¹¹⁶

As stated in the Notice and Section E. of the Purpose section, individuals who avail themselves of the proposed exception to the Operations Professional qualification examination requirement with an eligible registration would be subject to the Regulatory Element program appropriate for such other registration category. FINRA believes the proposed continuing education requirements for Operations Professionals are clear and notes that such requirements will be appropriately suited for those subject to registration, similar to the continuing education training for other FINRA registration categories.

Outsourced and Shared Functions

One commenter requested confirmation that FINRA does not intend to alter indirectly the definition of "associated person" or the existing regulatory guidance on

¹¹⁵ Great Nation.

¹¹⁶ ACLI.

outsourcing arrangements with the proposed rule change.¹¹⁷ Numerous commenters requested clarification that covered persons are limited to persons who have been empowered by a broker-dealer to oversee the covered functions and would not include individuals who perform operations functions for affiliated entities, outsourced operations functions for a third-party service provider or supervisors within a large, diversified financial services organization who are far-removed from a member's securities business.¹¹⁸ Certain commenters requested clarification with respect to who must register where clearing and introducing firms share responsibility for operations functions ("shared functions")¹¹⁹ and whether such persons would be considered associated persons of both the introducing and clearing firms.¹²⁰ Several commenters suggested that an exemption be provided when covered functions are performed by another registered broker-dealer, bank, investment advisor, foreign entity¹²¹ or affiliated insurance company.¹²² Given a member's obligation to supervise any outsourced activity, numerous commenters stated that it should be sufficient for FINRA to confine application of the proposed registration and examination requirements to "employees" of the

¹¹⁷ SIFMA.

¹¹⁸ ACLI, A&P, ARM, Bank of America, Horace Mann, IRI, Nationwide, PSD, Sutherland and TIAA.

¹¹⁹ ESI, FSI, NFP, UPFS, Wells Fargo and WSFG.

¹²⁰ Northwestern Mutual, Pershing and Wells Fargo.

¹²¹ AIC and Pershing.

¹²² ACLI and AIC.

member.¹²³ One commenter questioned the legal ramifications that would result from requiring the registration of vendor employees with more than one member.¹²⁴ Certain commenters requested clarification with respect to how the proposed rule change affects Office of Supervisory Jurisdiction (“OSJ”) requirements relating to currently outsourced activities¹²⁵ and back-office and support locations.¹²⁶ One commenter stated the proposed rule change would place an unfair burden on small firms that outsource many of the covered functions.¹²⁷

As noted above, FINRA believes anyone who meets the criteria of a covered person and engages in one or more of the covered functions on behalf of a member must register as an Operations Professional, regardless of whether such person works internally at a member, an affiliate or third-party service provider. Also as previously noted, the proposed rule change does not alter the definition of an “associated person” but rather imposes registration, qualification examination and continuing education requirements on persons who meet the depth of personnel criteria and engage in one or more of the covered functions on behalf of a member. The proposed registration category is function-based so persons are not shielded from the requirements based on their job title or employment by an entity other than a member.

¹²³ NSCP, Pershing, Schwab, Scottrade and TIAA.

¹²⁴ Pershing.

¹²⁵ IRI.

¹²⁶ Scottrade and TIAA.

¹²⁷ Zelman.

Additionally, FINRA notes that the proposed rule change would apply to all members regardless of firm size. FINRA reminds members that the depth of personnel included as covered persons generally is focused on positions with higher-level responsibilities, so entry level staff will likely not be required to register.

With respect to clearing arrangements and consistent with Notice to Members 05-48, a covered person would not be considered an associated person of both the introducing and clearing firms based solely on functions performed pursuant to a carrying agreement approved under FINRA Rule 4311 (Carrying Agreements),¹²⁸ so FINRA would not expect dual registration as an Operations Professional in such cases. However, as noted above, FINRA expects each member will designate at least one Operations Professional, who often may be the Financial and Operations Principal and/or the Principal Operations Officer.¹²⁹

One commenter suggested that treating persons that fall within the covered categories as associated persons of a member will impact state law prohibitions on dual registration and vendor agreements.¹³⁰ FINRA has stated throughout this filing the need for this proposed rule change and its belief that the proposal is appropriately tailored to meet its stated objectives. FINRA believes it is therefore required additional regulation. That being the case, ill-defined collateral effects that can be avoided by a member do not

¹²⁸ FINRA replaced NASD Rule 3230 (Clearing Agreements) and NYSE Rule 382 (Carrying Agreements) with new consolidated FINRA Rule 4311 (Carrying Agreements). See Securities Exchange Act Release No. 63999 (March 1, 2011) (Order Approving File No. SR-FINRA-2010-061).

¹²⁹ See supra note 61 and accompanying text.

¹³⁰ TIAA.

serve as a reason to modify or negate such proposed rulemaking. Finally, FINRA already views the persons treated as covered persons in the covered functions, and indeed all non-clerical persons reporting to such covered persons, as associated persons irrespective of this proposed rule.

Small Firms Concerns

Numerous commenters noted the proposed rule change places an undue burden on, unnecessarily increases costs for, and is anticompetitive for small firms with no apparent benefit to the public.¹³¹ One commenter noted the proposal is appropriate only in its application to personnel and broker-dealers that handle customer accounts, customer funds and/or securities.¹³²

FINRA does not agree that small firms would be overly burdened by the proposed rule change since almost all other FINRA registration requirements apply to small firms and do not provide an exemption for personnel performing activities that would require registration based on a firm's limited business. FINRA also anticipates that many persons who would be subject to the new Operations Professional registration category would qualify for the proposed exception from the qualification examination based on existing registrations, and, as noted above, FINRA would not assess a separate registration fee for persons relying on the proposed exception to register as Operations Professionals. Moreover, the impact of the proposed rule change is expected to be minimal as the majority of the covered functions are generally performed by the carrying

¹³¹ Crowell, Freestone, Martin Nelson, Mutual Trust, Navidar, RiverStone, Wellington and Zelman.

¹³² FirstBank PR.

and clearing firm and, as noted above, a covered person would not be considered an associated person of both the introducing and clearing firms based solely on functions performed pursuant to a carrying agreement approved under FINRA Rule 4311 (Carrying Agreements),¹³³ so FINRA would not expect dual registration as an Operations Professional in such cases. However, as further detailed in Section F. above, in light of the limitations on personnel at certain smaller firms, FINRA is proposing a 120-day grace period for covered persons associated with a non-clearing member to transition into the proposed registration category.

Implementation of the Proposed Rule Change

Numerous commenters suggested that the proposed transition period of six to nine months for persons acting as Operations Professionals as of the effective date of the proposed rule change is insufficient for firms to fully comply because a significant number of personnel will need to become registered. The commenters noted that firms will likely need to phase-in such persons' preparation for, and taking of, the qualification examination to mitigate the impact on customer service and operational functions.¹³⁴ Also, certain commenters suggested that personnel may not pass the qualification examination on the first attempt since good test preparation services may not be available and certain operations personnel may not have test-taking skills.¹³⁵ The commenters

¹³³ See supra note 128 and accompanying text.

¹³⁴ ARM, Bank of America, Commonwealth, ESI, FSI, Horace Mann, Modern Woodmen, M. Griffith, Morgan Stanley, NFP, NSCP, Scottrade, SIFMA and WSFG.

¹³⁵ Nationwide, UPFS and Wells Fargo.

suggested extending the transition period to between 12 to 18 months¹³⁶ or up to 24 months.¹³⁷ Other commenters noted that all persons should have the benefit of the transition period regardless of when they begin work in a covered function.¹³⁸

Certain commenters suggested that persons who begin work as Operations Professionals following the effective date of the proposed rule change (i.e., new hires or associated persons who meet the depth of personnel and transfer into a covered function) should be granted a grace period to transition into the proposed registration category.¹³⁹ According to one commenter, subjecting these persons to the proposed licensing regime immediately undercuts the purpose of the transition period and may chill hiring of operations personnel while the transition period is in effect.¹⁴⁰ Numerous commenters recommended a 90-day grace period for new hires or those who transition into a covered function, consistent with current NASD Rule 1021(d), which generally allows a registered representative to act in a principal capacity for 90 days while preparing for an applicable exam.¹⁴¹ Two commenters suggested a 120-day grace period for personnel who transition into a covered function after the transition period has expired, conditioned

¹³⁶ ARM, Bank of America, Commonwealth, ESI, FSI, Horace Mann, Modern Woodmen, M. Griffith, Morgan Stanley, NFP, NSCP, Scottrade, SIFMA and WSFG.

¹³⁷ Schwab.

¹³⁸ Schwab, SIFMA and TIAA.

¹³⁹ IRI, Nationwide, NSCP, Scottrade and Wells Fargo.

¹⁴⁰ Morgan Stanley.

¹⁴¹ ARM, Bank of America, PSD, Schwab, Scottrade, Sutherland and Wells Fargo.

on supervision by a licensed Operations Professional.¹⁴² One commenter suggested a 180-day grace period.¹⁴³

Based on the comments, FINRA has amended the transition period that was proposed in the Notice. As further detailed in Section F. above, FINRA is proposing a 60-day identification period beginning on the effective date of the proposed rule change during which Day-One Professionals must request registration as an Operations Professional via Form U4 in CRD. Day-One Professionals who are identified during the 60-day period and must pass the Operations Professional examination (or an eligible qualification examination) would be granted 12 months beginning on the effective date of the proposed rule change to pass such qualifying examination, during which time such persons may function as an Operations Professional.

With respect to non-Day-One Professionals, any person associated with a clearing or self-clearing member must register as an Operations Professional and, if applicable, pass the Operations Professional qualification examination (or an eligible qualification examination) prior to engaging in any activities that would require such registration. Any non-Day-One Professional associated with a non-clearing member who must pass the Operations Professional qualification examination (or an eligible qualification examination) to obtain registration would be granted a grace period of 120 days beginning on the date such person requests Operations Professional registration via Form U4 in CRD to pass such qualifying examination, during which time such person may function as an Operations Professional.

¹⁴² Morgan Stanley and SIFMA.

¹⁴³ Wells Fargo.

Two commenters expressed sentiments regarding their general disagreement with FINRA spending¹⁴⁴ and the current regulatory structure for broker-dealers.¹⁴⁵ These comments are outside the scope of the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2011-013 on the subject line.

¹⁴⁴ Mutual Trust.

¹⁴⁵ Wellington.

Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2011-013. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2011-013 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁴⁶

Elizabeth M. Murphy

Secretary

¹⁴⁶ 17 CFR 200.30-3(a)(12).

EXHIBIT 2b

Alphabetical List of Written Comments

1. Letter from Jed Bandes, Mutual Trust Co. of America Securities (“Mutual Trust”) (July 8, 2010)
2. Letter from David T. Bellaire, Esq., Financial Services Institute (“FSI”) (July 30, 2010)
3. Letter from Joseph P. Bree, Quasar Distributors, LLC (“Quasar”) (July 28, 2010)
4. Letter from James E. Clements, Equity Services Inc. (“ESI”) (July 13, 2010)
5. Letter from Nicholas C. Cochran, American Investors Company (“AIC”) (July 9, 2010)
6. Letter from Catherine M. Corrigan, Rockfleet Financial Services, Inc. (“Rockfleet”) (July 29, 201)
7. Letter from J. Lee Covington II, Insured Retirement Institute (“IRI”) (July 30, 2010)
8. Letter from Cathy Cucharale, M. Griffith Investment Services, Inc. (“M. Griffith”) (May 28, 2010)
9. Letter from Simon Culhane, Chartered Institute for Securities and Investment (“CISI”) (July 29, 2010)
10. Letter from Stephen Day, Navidar Group (“Navidar”) (May 27, 2010)
11. Letter from Marian H. Desilets, Association of Registration Management, Inc. (“ARM”) (July 30, 2010)
12. Letter from S. Kendrick Dunn, Pacific Select Distributors, Inc. (“PSD”) (July 30, 2010)
13. Letter from Jon Feigelson, Teachers Insurance and Annuity Association of America-College Retirement Equities Fund (“TIAA”) (July 30, 2010)
14. Letter from Pamela S. Fritz, Modern Woodmen (“Modern Woodmen”) (July 7, 2010)
15. Letter from Janice Greene, Freestone Capital Management, LLC (“Freestone”) (July 16, 2010)
16. Letter from Bari Havlik, Charles Schwab & Co., Inc. (“Schwab”) (July 30, 2010)

17. Letter from Joan Hinchman, National Society for Compliance Professionals (“NSCP”) (July 30, 2010)
18. Letter from Kevin M. Hogan, Investment Program Association (“IPA”) (July 30, 2010)
19. Letter from David Horn, NFP Securities, Inc. (“NFP”) (July 12, 2010)
20. Letter from Nancy Kay, Wall Street Financial Group, Inc. (“WSFG”) (July 22, 2010)
21. Letter from Clifford Kirsch, Sutherland Asbill & Brennan LLP (“Sutherland”) (July 30, 2010)
22. Letter from James R. Kruger, Crowell, Weedon & Co. (“Crowell”) (July 30, 2010)
23. Letter from James Kupfer, Transcend Capital (“Transcend”) (June 18, 2010)
24. Letter from Ronald C. Long, Wells Fargo Advisors (“Wells Fargo”) (July 28, 2010)
25. Letter from Melanie Senter Lubin, North American Securities Administrators Association, Inc. (“NASAA”) (July 30, 2010)
26. Letter from C. Michael Luck, RBC Wealth Management (“RBC”) (May 26, 2010)
27. Letter from Brian Marcotte, Johnson Rice & Company, L.L.C. (“JRCO”) (May 26, 2010)
28. Letter from Sarah McCafferty, T. Rowe Price Investment Services, Inc. (“T. Rowe Price”) (July 28, 2010)
29. Letter from James T. McHale, Securities Industry and Financial Markets Association (“SIFMA”) (July 30, 2010)
30. Letter from Neal E. Nakagiri, NPB Financial Group, LLC (“NPB”) (July 9, 2010)
31. Letter from Martin Nelson, Martin Nelson & Co., Inc. (“Martin Nelson”) (June 24, 2010)
32. Letter from Jill W. Ostergaard, Morgan Stanley (“Morgan Stanley”) (July 29, 2010)
33. Letter from Douglas G. Preston, Bank of America (“Bank of America”) (July 30, 2010)
34. Letter from Clarie Santaniello, Pershing LLC (“Pershing”) (July 30, 2010)
35. Letter from Thomas Sargant, Regional Municipal Operations Association (“RMOA”) (July 9, 2010)

36. Letter from Doug Schriener, Harrison Douglas (“Harrison”) (June 2, 2010)
37. Letter from David V. Shields, Wellington Shields & Co. LLC (“Wellington”) (July 23, 2010)
38. Letter from David Shindel, United Planners Financial Services (“UPFS”) (June 30, 2010)
39. Letter from Andrew C. Small, Scottrade, Inc. (“Scottrade”) (August 2, 2010)
40. Letter from Brian E. Smith, RiverStone Wealth Management, Inc. (“RiverStone”) (June 24, 2010)
41. Letter from Joseph D. Terry, Horace Mann Investors, Inc. (“Horace Mann”) (July 7, 2010)
42. Letter from Paul J. Tolley, Commonwealth financial network (“Commonwealth”) (July 30, 2010)
43. Letter from Byron Pat Treat, Great Nation Investment Corp. (“Great Nation”) (July 29, 2010)
44. Letter from Robert L. Tuch, Nationwide Financial Services, Inc. (“Nationwide”) (July 28, 2010)
45. Letter from D. Grant Vingoe, Arnold & Porter LLP (“A&P”) (July 1, 2010)
46. Letter from Stephen H. Wank, Zelman Partners LLC (“Zelman”) (June 24, 2010)
47. Letter from Carl B. Wilkerson, American Council of Life Insurers (“ACLI”) (July 30, 2010)
48. Letter from Jeffrey B. Williams, Northwestern Mutual Investment Services, LLC (“Northwestern Mutual”) (July 26, 2010)
49. Letter from Carrie Wisniewski, FirstBank Puerto Rico Securities Corp. (“FirstBank PR”) (July 28, 2010)

EXHIBIT 5

Exhibit 5 shows the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

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Text of Proposed New FINRA Rule

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1000. MEMBER APPLICATION AND ASSOCIATED PERSON REGISTRATION

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1200. REGISTRATION AND QUALIFICATION

1230. Registration Categories

(a) Definition of Principal and Principal Registration Categories

(1) through (11) Reserved.

(b) Definition of Representative and Representative Registration Categories

(1) through (5) Reserved.

(6) Operations Professional

(A) Requirement

Each of the following persons shall be required to register with

FINRA as an Operations Professional:

(i) Senior management with responsibility over the

covered functions in paragraph (b)(6)(B) of this Rule;

(ii) Supervisors, managers or other persons responsible for

approving or authorizing work, including work of other persons, in

direct furtherance of the covered functions in paragraph (b)(6)(B) of this Rule; and

(iii) Persons with the authority or discretion materially to commit a member's capital in direct furtherance of the covered functions in paragraph (b)(6)(B) of this Rule or to commit a member to any material contract or agreement (written or oral) in direct furtherance of the covered functions in paragraph (b)(6)(B) of this Rule.

(B) Covered Functions

(i) Client on-boarding (customer account data and document maintenance);

(ii) Collection, maintenance, re-investment (i.e., sweeps) and disbursement of funds;

(iii) Receipt and delivery of securities and funds, account transfers;

(iv) Bank, custody, depository and firm account management and reconciliation;

(v) Settlement, fail control, buy ins, segregation, possession and control;

(vi) Trade confirmation and account statements;

(vii) Margin;

(viii) Stock loan/securities lending;

(ix) Prime brokerage (services to other broker-dealers and financial institutions);

(x) Approval of pricing models used for valuations;

(xi) Financial control, including general ledger and treasury;

(xii) Contributing to the process of preparing and filing financial regulatory reports;

(xiii) Defining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements;

(xiv) Defining and approving business security requirements and policies for information technology, including, but not limited to, systems and data, in connection with the covered functions;

(xv) Defining and approving information entitlement policies in connection with the covered functions; and

(xvi) Posting entries to a member's books and records in connection with the covered functions to ensure integrity and compliance with the federal securities laws and regulations and FINRA rules.

(C) Qualification Examination

Subject to the exception in paragraph (b)(6)(D) of this Rule, any person who is required to register as an Operations Professional shall pass the Operations Professional qualification examination before such registration may become effective.

(D) Exception

Any person who is registered with FINRA as an Investment Company Products/Variable Contracts Representative, General Securities Representative, United Kingdom Securities Representative or Canada Securities Representative, Registered Options Principal, General Securities Sales Supervisor, Compliance Officer, Supervisory Analyst, General Securities Principal, Investment Company Products/Variable Products Principal, Financial and Operations Principal, Introducing Broker-Dealer Financial and Operations Principal, Municipal Fund Securities Limited Principal or Municipal Securities Principal, and any person who has been registered in one of these categories within the two years immediately prior to registering as an Operations Professional, shall be qualified to register as an Operations Professional without passing the Operations Professional qualification examination, provided that such registration is not revoked pursuant to Rules 8310 or 8320, suspended or otherwise deemed inactive.

(E) Implementation

(i) Any person who is required to register as an Operations Professional as of [insert the effective date of the rule] shall request registration as an Operations Professional via Form U4 in CRD within 60 days after [insert the effective date of the rule]. Any person who is required to register as an Operations Professional as of [insert the effective date of the rule] and must pass the Operations Professional qualification examination (or an eligible qualification examination listed in paragraph (b)(6)(D) of this Rule) to qualify for Operations Professional registration shall be allowed a period of 12 months beginning on [insert the effective date of the proposed rule] to pass such qualifying examination, during which time such person may function as an Operations Professional.

(ii) Any person who is required to register as an Operations Professional after [insert the effective date of the rule] shall register as an Operations Professional and, if applicable, pass the Operations Professional qualification examination (or an eligible qualification examination listed in paragraph (b)(6)(D) of this Rule) prior to engaging in any activities that would require such registration; provided, however, a person associated with a non-clearing member who must pass the Operations Professional qualification examination (or an eligible qualification examination listed in paragraph (b)(6)(D) of this Rule) to qualify for Operations

Professional registration shall be allowed a period of 120 days beginning on the date such person requests Operations Professional registration to pass such qualifying examination, during which time such person may function as an Operations Professional.

(7) through (14) Reserved.

• • • Supplementary Material: -----

.01 through .05 Reserved.

.06 Scope of Operations Professional Requirement. Any person whose activities are limited to performing a function ancillary to a covered function in paragraph (b)(6)(B) of this Rule, or whose function is to serve a role that can be viewed as supportive of or advisory to the performance of a covered function in paragraph (b)(6)(B) of this Rule (e.g., internal audit, legal or compliance personnel who review but do not have primary responsibility for any covered function), or who engages solely in clerical or ministerial activities in a covered function in paragraph (b)(6)(B) of this Rule shall not be required to register as an Operations Professional pursuant to paragraph (b)(6)(A) of this Rule. For the purpose of Rule 1230(b)(6)(A)(iii), the determination as to what constitutes “materially” or “material” is based on a member’s pre-established spending guidelines and risk management policies.

.07 Reserved.

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**Text of Proposed New FINRA Rule
(Marked to Show Changes from NASD Rule 1120; NASD Rule 1120 to be Deleted in
its Entirety from the Transitional Rulebook)**

* * * * *

[1120] 1250. Continuing Education Requirements

This Rule prescribes requirements regarding the continuing education of certain registered persons subsequent to their initial qualification and registration with [NASD] FINRA. The requirements shall consist of a Regulatory Element and a Firm Element as set forth below.

(a) Regulatory Element

(1) Requirements

No member shall permit any registered person to continue to, and no registered person shall continue to, perform duties as a registered person unless such person has complied with the requirements of paragraph (a) hereof.

Each registered person shall complete the Regulatory Element on the occurrence of their second registration anniversary date and every three years thereafter, or as otherwise prescribed by [NASD] FINRA. On each occasion, the Regulatory Element must be completed within 120 days after the person's registration anniversary date. A person's initial registration date, also known as the "base date," shall establish the cycle of anniversary dates for purposes of this Rule. The content of the Regulatory Element shall be determined by [NASD] FINRA and shall be appropriate to either the registered representative or principal status of persons subject to the Rule.

(2) Failure to Complete

Unless otherwise determined by [the Association] FINRA, any registered persons who have not completed the Regulatory Element within the prescribed time frames will have their registrations deemed inactive until such time as the

requirements of the program have been satisfied. Any person whose registration has been deemed inactive under this Rule shall cease all activities as a registered person and is prohibited from performing any duties and functioning in any capacity requiring registration. A registration that is inactive for a period of two years will be administratively terminated. A person whose registration is so terminated may reactivate the registration only by reapplying for registration and meeting the qualification requirements of the applicable provisions of Rule 1230(b)(6) and the NASD Rule 1020 [Series] and [the Rule] 1030 Series. [The Association] FINRA may, upon application and a showing of good cause, allow for additional time for a registered person to satisfy the program requirements.

(3) Disciplinary Actions

Unless otherwise determined by [NASD] FINRA, a registered person will be required to retake the Regulatory Element and satisfy all of its requirements in the event such person:

(A) is subject to any statutory disqualification as defined in Section 3(a)(39) of the Exchange Act;

(B) is subject to suspension or to the imposition of a fine of \$5,000 or more for violation of any provision of any securities law or regulation, or any agreement with or rule or standard of conduct of any securities governmental agency, securities self-regulatory organization, or as imposed by any such regulatory or self-regulatory organization in connection with a disciplinary proceeding; or

(C) is ordered as a sanction in a disciplinary action to retake the Regulatory Element by any securities governmental agency or self-regulatory organization.

The retaking of the Regulatory Element shall commence with participation within 120 days of the registered person becoming subject to the statutory disqualification, in the case of (A) above, or the disciplinary action becoming final, in the case of (B) and (C) above. The date of the disciplinary action shall be treated as such person's new base date with [NASD] FINRA.

(4) Reassociation in a Registered Capacity

Any registered person who has terminated association with a member and who has, within two years of the date of termination, become reassociated in a registered capacity with a member shall participate in the Regulatory Element at such intervals that may apply (second anniversary and every three years thereafter) based on the initial registration anniversary date rather than based on the date of reassociation in a registered capacity.

(5) Definition of Registered Person

For purposes of this Rule, the term “registered person” means any person registered with [NASD] FINRA as a representative, principal, assistant representative or research analyst pursuant to Rule 1230(b)(6) and the NASD Rule 1020, 1030, 1040, 1050 and 1110 Series.

(6) In-Firm Delivery of the Regulatory Element

Members will be permitted to administer the continuing education Regulatory Element program to their registered persons by instituting an in-firm program acceptable to [the Association] FINRA.

The following procedures are required:

(A) Principal/Officer In-Charge. The firm has designated a principal to be responsible for the in-firm delivery of the Regulatory Element.

(B) Site Requirements.

(i) The location of all delivery sites will be under the control of the firm.

(ii) Delivery of Regulatory Element continuing education will take place in an environment conducive to training.

(Examples: a training facility, conference room or other area dedicated to this purpose would be appropriate. Inappropriate locations would include a personal office or any location that is not or cannot be secured from traffic and interruptions.)

(iii) Where multiple delivery terminals are placed in a room, adequate separation between terminals will be maintained.

(C) Technology Requirements. The communication links and firm delivery computer hardware must comply with standards defined by [the Association] FINRA or its designated vendor.

(D) Supervision.

(i) The firm's Written Supervisory Procedures must contain the procedures implemented to comply with the requirements of in-firm delivery of the Regulatory Element continuing education.

(ii) The firm's Written Supervisory Procedures must identify the principal designated pursuant to Rule [1120] 1250(a)(6)(A) and contain a list of individuals authorized by the firm to serve as proctors.

(iii) Firm locations for delivery of the Regulatory Element continuing education will be specifically listed in the firm's Written Supervisory Procedures.

(E) Proctors.

(i) All sessions will be proctored by an authorized person during the entire Regulatory Element session. Proctors must be present in the session room or must be able to view the person(s) sitting for Regulatory Element continuing education through a window or by video monitor.

(ii) The individual responsible for proctoring at each administration will sign a certification that required procedures have been followed, that no material from Regulatory Element continuing education has been reproduced, and that no candidate received any assistance to complete the session. Such certification

may be part of the sign-in log required under Rule [1120] 1250(a)(6)(F).

(iii) Individuals serving as proctors must be persons registered with an SRO and supervised by the designated principal for purposes of in-firm delivery of the Regulatory Element continuing education.

(iv) Proctors will check and verify the identification of all individuals taking Regulatory Element continuing education.

(F) Administration.

(i) All appointments will be scheduled in advance using the procedures and software specified by [the Association] FINRA to communicate with [the Association's] FINRA's system and designated vendor.

(ii) The firm/proctor will conduct each session in accordance with the administrative appointment scheduling procedures established by [the Association] FINRA or its designated vendor.

(iii) A sign-in log will be maintained at the delivery facility. Logs will contain the date of each session, the name and social security number of the individual taking the session, that required identification was checked, the sign-in time, the sign-out time, and the name of the individual proctoring the session. Such

logs are required to be retained pursuant to [SEC] SEA Rules 17a-3 and 17a-4.

(iv) No material will be permitted to be [utilized] used for the session nor may any session-related material be removed.

(v) Delivery sites will be made available for inspection by [the SROs] FINRA.

(vi) Before commencing in-firm delivery of the Regulatory Element continuing education, members are required to file with their Designated Examining Authority (“DEA”), a letter of attestation (as specified below) signed by a principal executive officer or executive representative, attesting to the establishment of required procedures addressing principal in-charge, supervision, site, technology, proctors, and administrative requirements. Letters filed with [NASD Regulation, Inc.] FINRA should be sent to [Member Regulation] Registration and Disclosure, Continuing Education Department, 9509 Key West Avenue, Rockville, MD 20850.

Letter of Attestation for In-Firm Delivery of Regulatory Element Continuing Education

[Name of member] has established procedures for delivering Regulatory Element continuing education on its premises. I have determined that these procedures are reasonably designed to comply with SRO requirements pertaining to in-firm delivery of Regulatory Element continuing education, including that such procedures have been

implemented to comply with principal/officer in-charge, supervision, site, technology, proctors, and administrative requirements.

Signature

Printed name

Title [Must be signed by a Principal Executive Officer (or Executive Representative) of the firm]

Date

(7) Regulatory Element Contact Person

Each member shall designate and identify to [NASD] FINRA (by name and e-mail address) an individual or individuals responsible for receiving e-mail notifications provided via the Central Registration Depository regarding when a registered person is approaching the end of his or her Regulatory Element time frame and when a registered person is deemed inactive due to failure to complete the requirements of the Regulatory Element program. Each member shall identify, review, and, if necessary, update the information regarding its Regulatory Element contact person(s) in the manner prescribed by NASD Rule 1160.

(b) Firm Element

(1) Persons Subject to the Firm Element

The requirements of this subparagraph shall apply to any person registered with a member who has direct contact with customers in the conduct of the member's securities sales, trading and investment banking activities, any person registered as an operations professional pursuant to Rule 1230(b)(6) or a research analyst pursuant to NASD Rule 1050, and to the immediate supervisors of such persons (collectively, “covered registered persons”). “Customer” shall mean any natural person and any organization, other than another broker or dealer, executing securities transactions with or through or receiving investment banking services from a member.

(2) Standards for the Firm Element

(A) Each member must maintain a continuing and current education program for its covered registered persons to enhance their securities knowledge, skill, and professionalism. At a minimum, each member shall at least annually evaluate and prioritize its training needs and develop a written training plan. The plan must take into consideration the member's size, organizational structure, and scope of business activities, as well as regulatory developments and the performance of covered registered persons in the Regulatory Element. If a member's analysis establishes the need for supervisory training for persons with supervisory responsibilities, such training must be included in the member's training plan.

(B) Minimum Standards for Training Programs — Programs used to implement a member's training plan must be appropriate for the business of the member and, at a minimum must cover the following matters concerning securities products, services, and strategies offered by the member:

- (i) General investment features and associated risk factors;
- (ii) Suitability and sales practice considerations;
- (iii) Applicable regulatory requirements; and
- (iv) With respect to registered research analysts and their immediate supervisors, training in ethics, professional responsibility and the requirements of NASD Rule 2711.

[*NASD members must implement the provisions of Rule 1120(b)(2)(B)(iv) on January 26, 2004, or such later date as determined by NASD*]

(C) Administration of Continuing Education Program — A member must administer its continuing education programs in accordance with its annual evaluation and written plan and must maintain records documenting the content of the programs and completion of the programs by covered registered persons.

(3) Participation in the Firm Element

Covered registered persons included in a member's plan must take all appropriate and reasonable steps to participate in continuing education programs as required by the member.

(4) Specific Training Requirements

[The Association] FINRA may require a member, individually or as part of a larger group, to provide specific training to its covered registered persons in such areas as [The Association] FINRA deems appropriate. Such a requirement may stipulate the class of covered registered persons for which it is applicable, the time period in which the requirement must be satisfied and, where appropriate, the actual training content.

* * * * *