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SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-65700; File No. SR-FINRA-2011-064)

November 7, 2011

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change to Adopt FINRA Rule 4524 (Supplemental FOCUS Information) and Proposed Supplementary Schedule to the Statement of Income (Loss) Page of FOCUS Reports

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 November 1, 2011, Financial Industry Regulatory Authority, Inc. (“FINRA”) 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 4524 (Supplemental FOCUS Information) to require each member, as FINRA shall designate, to file such additional financial or operational schedules or reports as FINRA may deem necessary as a supplement to the FOCUS report. The content of such supplemental schedules or reports would be specified in a Regulatory Notice (or similar communication), which FINRA would file with the SEC pursuant to proposed FINRA Rule 4524. As part of the proposed rule change, FINRA is filing one such proposed schedule, a supplement to the Statement of Income (Loss) page of the FOCUS Report.

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 website 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

Pursuant to SEA Rule 17a-5, members are required to file with FINRA reports concerning their financial and operational status using SEC Form X-17A-5, Financial and Operational Combined Uniform Single (FOCUS) Report.³ SEA Rule 17a-5 generally requires members that clear transactions or carry customer accounts to file a FOCUS Report Part II, and requires certain other members to file a FOCUS Report Part IIA. Members that use Appendix E to SEA Rule 15c3-1 to calculate net capital file a FOCUS Report Part II CSE⁴ that is similar to the FOCUS Report Part II (collectively, the FOCUS Reports Part II, Part IIA, and Part II CSE are referred to hereinafter as "FOCUS Reports").

³ 17 CFR 240.17a-5.

⁴ A broker-dealer that calculates its net capital under Appendix E of SEA Rule 15c3-1 is referred to as Alternative Net Capital ("ANC") firm.

FINRA is proposing to adopt FINRA Rule 4524, a rule that would provide the mechanism by which FINRA can obtain from members more detailed financial information to augment the FOCUS reports required to be filed pursuant to SEA Rule 17a-5. Proposed FINRA Rule 4524 would require members to file such additional financial or operational schedules or reports to supplement FOCUS reports as FINRA may deem necessary or appropriate for the protection of investors or in the public interest.⁵ Thus, the rule would provide FINRA the framework to request more specific information regarding, among other things, the assets and liabilities of a member, the generation of revenues and allocation of expenses by business segment or product lines, the sources of trading gains and losses, the types and amounts of fees earned, and the nature and extent of participation in securities offerings. Depending on the nature of the proposed supplemental schedule or report, FINRA may require that all members or any specified subset of members submit the schedule or report to FINRA.

FOCUS Reports provide FINRA with valuable information regarding a member's business; however, FINRA believes that it can better discharge its regulatory obligations with the benefit of additional information that gives FINRA a more complete and detailed view of a member's business operations. Accordingly, proposed FINRA Rule 4524 would provide FINRA a means and process to obtain greater transparency into a member's business activities and to better illuminate industry trends, allowing for more focused and effective examinations.

FINRA would effectuate proposed FINRA Rule 4524 by way of a Regulatory Notice or similar communication, the content of which would be filed with the Commission. To that end, as an initial report required pursuant to proposed FINRA Rule 4524, FINRA is also proposing a

⁵ Nothing in proposed FINRA Rule 4524 should be construed as altering in any manner a member's obligations under SEA Rule 17a-5(a)(2)(iv).

Supplemental Statement of Income (“SSOI”) to magnify the data from the Statement of Income (Loss) page of the FOCUS Reports.⁶

The proposed SSOI is intended to capture more granular detail of a firm’s revenue and expense information. The lack of more specific revenue and expense categories for certain business activities on the Statement of Income (Loss) page of the FOCUS Reports has led many firms to report much of their revenue and expenses as “other” (miscellaneous), a very general categorization that provides FINRA limited visibility into revenue and expense trends. The proposed SSOI is divided into sections containing line items that seek additional detail to permit FINRA to better understand revenue sources and expense composition on an ongoing basis. This additional detail would allow FINRA to better assess risk at a firm, and as a result, better allocate examination resources. Each member would be required to file with FINRA the proposed SSOI within 17 business days of the end of each calendar quarter.

The proposed SSOI contains a *de minimis* exception for providing details of revenue and expenses for certain designated sections. If a member’s total dollar amount for a designated section is \$5,000 or less for the reporting period, the member would only be required to enter the total dollar amount to complete the section. Additionally, not every line item would apply to every member, especially those with limited product offerings, thus limiting the burden of completing the form.

The proposed SSOI includes a new Operational Page that would collect additional information from certain members with respect to participation in unregistered offerings during the reporting period. Members whose revenue from unregistered offerings exceeds 10% of total revenue for the reporting period would be required to complete the Operational Page by

⁶ See Exhibit 3.

providing specific information about each unregistered offering. FINRA believes that such information would provide it with greater transparency and a stronger understanding regarding the types of unregistered offerings that generate significant revenue for members.

The proposed rule change will be effective upon Commission approval. FINRA will announce the implementation dates of both proposed FINRA Rule 4524 and the proposed schedule (i.e., the proposed SSOI) in a Regulatory Notice to be published no later than 60 days following Commission approval of the proposed rule change. The implementation date of the proposed schedule will be no sooner than 180 days, and no later than 365 days, following Commission approval of the proposed rule change.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁷ 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 that the proposed rule change is consistent with the provisions of the Act noted above in that supplemental FOCUS information will further strengthen FINRA's ability to protect investors through a more informed understanding of the drivers of members' business that can be used for more targeted examinations.

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.

⁷ 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 and the proposed SSOI were published for comment in Regulatory Notice 10-33 (July 2010) (the “Notice”). FINRA received 28 comment letters in response to the Notice.⁸ A copy of the Notice is attached as Exhibit 2a.⁹ A list of the comment letters received in response to the Notice is attached as Exhibit 2b. Copies of the comment

⁸ See Letter from Ivy League Financial Services, Inc., dated July 21, 2010 (“Ivy”); letter from M.S. Howells & Co., dated July 23, 2010 (“M.S. Howells”); letter from Hunter, Keith, Marshall & Co., Inc, dated July 27, 2010 (“HKM”); letter from Balanced Financial Securities, dated July 31, 2010 (“BFS”); letter from Foresters Equity Services, Inc., dated August 5, 2010 (“FES”); letter from Hodges Capital Management-First Dallas Securities, dated August 5, 2010 (“HCM”); letter from Farragut Capital LLC, dated August 12, 2010 (“Farragut”); letter from Integrity Investments, Inc., dated August 12, 2010 (“Integrity”); letter from Stephen Kinkade CPA, dated August 15, 2010 (“Kinkade”); letter from Wachtel & Co., Inc., dated August 16, 2010 (“Wachtel”); letter from First Asset Financial Inc., dated August 17, 2010 (“FAF”); letter from Aileen Gallagher, dated August 17, 2010 (“Gallagher”); letter from National Association of Independent Broker-Dealers, Inc., dated August 17, 2010 (“NAIBD”); letter from Securities Industry and Financial Markets Association, dated August 17, 2010 (“SIFMA”); letter from Wilson-Davis & Co., Inc., dated August 17, 2010 (“WDC”); letter from Allegheny Investments, LTD, dated August 18, 2010 (“Allegheny”); letter from Berkshire Bridge Capital, LLC, dated August 18, 2010 (“Berkshire”); letter from IBG Trading Inc., dated August 18, 2010 (“IBG”); letter from Integrated Management Solutions, dated August 18, 2010 (“IMS”); letter from Probitas Partners, dated August 18, 2010 (“Probitas”); letter from Real Estate Investment Securities Association, dated August 18, 2010 (“REISA”); letter from Regional Bond Dealers Association, dated August 18, 2010 (“RBDA”); letter from Sutherland Asbill & Brennan LLP, dated August 18, 2010 (“Sutherland”); letter from Southlake Capital Advisors, Inc., dated August 18, 2010 (“SCA”); letter from Trust Advisory Group, Ltd., dated August 18, 2010 (“TAG”); letter from Wedbush Securities Inc., dated August 18, 2010 (“Wedbush”); letter from Bank of America Merrill Lynch, dated August 19, 2010 (“B of A”); and letter from Citigroup Global Markets, Inc., dated August 20, 2010 (“Citi”).

⁹ The Commission notes that while provided in Exhibit 2a to FINRA's filing with the Commission, the Notice is not attached hereto. The Notice can be accessed online at http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p12174_2.pdf.

letters received in response to the Notice are attached as Exhibit 2c.¹⁰ Below is a summary of the comments and FINRA's responses.

A. Schedule Not Needed or Justified

A number of commenters argued that the proposed SSOI is not needed or justified.¹¹

Some commenters stated that FINRA or the SEC can already request the information required by the proposed SSOI.¹² One commenter believed that the current reports provide sufficient detail for FINRA to understand a member's business.¹³ Two commenters believed that routine exams already give a detailed view of a member's business operations.¹⁴ Several other commenters did not see how the requested information protected investors.¹⁵ Finally, one commenter argued that FINRA has not justified why the proposed SSOI is the best means of achieving FINRA's regulatory objectives without undue burden on members.¹⁶ FINRA disagrees with the contentions that the information sought is unnecessary or superfluous. As stated in the Notice, FINRA believes that it can better discharge its regulatory obligations with the benefit of additional information that gives FINRA a more complete and detailed view of a member's business operations. Moreover, FINRA believes the proposed SSOI is the most effective and

¹⁰ The Commission notes that while provided in Exhibit 2c to the filing, the list of the commenters and comment letters received by FINRA are not attached hereto. Those comment letters can be accessed online at <http://www.finra.org/Industry/Regulation/Notices/2010/P121743>. As stated previously, all references to "commenters" are to the commenters to the Notice, which are listed in Exhibit 2b.

¹¹ Allegheny, FAF, Farragut, Integrity, Ivy, Kinkade, Probitas, REISA, Sutherland and WDC.

¹² Allegheny, Sutherland, Farragut, Integrity and Kinkade.

¹³ Ivy.

¹⁴ REISA and WDC.

¹⁵ Farragut, Kinkade, Probitas and WDC.

¹⁶ RBDA.

timely way to obtain the additional detail of the generation of revenues and allocation of expenses by business segment or product lines, the sources of trading gains and losses, the types and amounts of fees earned, and the nature and extent of participation in securities offerings.

B. Small Firm Concerns

Several commenters stated that the proposed SSOI will be costly and time consuming for small firms.¹⁷ Some of these commenters argued that FINRA should provide an exemption from the rule for smaller firms.¹⁸ Several commenters asserted that the Operational Page creates an unfair bias against smaller firms.¹⁹ FINRA believes that the required information is important to identify regulatory risk and trends, irrespective of firm size. Therefore, FINRA does not believe a small firm exemption is appropriate. However, as mentioned above, the proposed SSOI contains a *de minimis* exception that will make the form less time consuming for many smaller firms. Additionally, FINRA points out that many of the line items will not apply to smaller firms with limited product offerings.

C. Clarifications and Recommended Changes

Certain commenters requested clarification of the information required on the proposed SSOI.²⁰ Several commenters suggested that FINRA should include instructions and definitions for the proposed SSOI.²¹ One commenter had concerns that the “numbers reported on the FOCUS Report and the Proposed Schedule will not automatically ‘match.’”²² Further, several

¹⁷ Allegheny, BFS, FAF, Farragut, FES, Gallagher, HCM, HKM, IMS, Integrity, Kinkade, M.S. Howells, Probitas, RBDA, REISA, TAG, Wachtel and WDC.

¹⁸ BFS, HKM, Wachtel and WDC.

¹⁹ HKM, Kinkade, NAIBD and REISA.

²⁰ Allegheny, B of A, Citi, FAF, IMS, Kinkade, NAIBD, RBDA, Sutherland and WDC.

²¹ Citi, IMS, Kinkade, NAIBD, RBDA and Sutherland.

²² Sutherland.

commenters recommended changes to specific line items on the proposed SSOI.²³ In response to these comments, FINRA has developed instructions for the proposed SSOI, which are included in the attached Exhibit 3. The instructions include guidance, clarifications and definitions with respect to certain line items that FINRA believes should ameliorate the commenters' concerns. Additionally, in response to recommended changes to specific line items, FINRA has amended the proposed SSOI by making the requested tax information less burdensome, allowing flexibility regarding the reporting of dividends and interest for principal trades and allowing revenue from unit investment trusts that are open-end companies to be included with revenue from investment company shares.

D. Data Capture

Several commenters suggested that the profit and loss information required by the proposed SSOI should be based on established units within a firm rather than by product.²⁴ In response, FINRA believes that requiring information by product is the best way to understand revenue sources and expense composition. However, FINRA is allowing firms, in certain instances, a choice as to which section and/or line item on the proposed SSOI to reflect revenue or expense. Firms must document the methodology chosen and apply it consistently across reporting periods. Additionally, the methodology must be made available to FINRA staff upon request.

E. Confidentiality

One commenter expressed competitive concerns with providing FINRA detailed departmental data.²⁵ Another commenter was concerned that the proposed SSOI could

²³ B of A, IMS and Kinkade.

²⁴ B of A, Citi, IMS, Kinkade, M.S. Howells and SIFMA.

²⁵ M.S. Howells.

compromise otherwise confidential deal making.²⁶ The commenter stated that members “specializing in restructuring/distressed situations are frequently bound to confidentiality by U.S. bankruptcy laws that would preclude the release of certain information.”²⁷ FINRA does not believe these concerns are valid as the proposed SSOI would be treated with the same confidentiality as the FOCUS Report to which it relates.²⁸ In regard to the commenter’s concern about being bound to confidentiality by U.S. bankruptcy laws, FINRA notes that the commenter did not provide any specific examples of such U.S. bankruptcy laws or discussion of the manner in which such laws would preclude a member from complying with the proposed rulemaking.

F. Use of the Proposed SSOI

Several commenters were concerned that the proposed SSOI would be used as the basis for the calculation of various assessments, fees and dues on members.²⁹ As previously mentioned, the proposed SSOI is intended to provide information about a member’s revenue and expenses in greater detail. The proposed SSOI supplements the FOCUS report and would not be used as the basis for any assessments, fees or dues; however, total revenue on the proposed SSOI should equal total revenue on the FOCUS report.

G. Reporting Period

Several commenters recommended that reporting of the proposed SSOI be on a quarterly basis.³⁰ These commenters stated that “[m]any firms as a matter of course have more detailed reporting requirements – both internal and external – on a quarterly basis, which would facilitate

²⁶ NAIBD.

²⁷ NAIBD.

²⁸ See SEA Rule 17a-5(a)(3).

²⁹ B of A, BBC, SIFMA and Wedbush.

³⁰ B of A and SIFMA.

this additional FINRA reporting while limiting the need for additional resources.”³¹ FINRA agrees with the commenters and has proposed quarterly basis reporting for the proposed SSOI.

H. Filing Time Frame

Two commenters suggested that the proposed SSOI should be filed within the time frames for current supplemental reporting and not on the FOCUS filing date.³² They believed that filing within such time frames would address resource constraints and would be consistent with other reporting time frames. FINRA disagrees with the commenters and instead has proposed to require the proposed SSOI to be filed within 17 business days after the end of the calendar quarter, consistent with the time frame allowed for the filing of the FOCUS Reports. FINRA believes that this time frame strikes the proper balance of ensuring FINRA receives timely information while giving firms’ sufficient time to file the proposed SSOI.

I. Operational Page of the Proposed SSOI

Several commenters believed that FINRA is unfairly targeting Regulation D offerings.³³ One commenter suggested that the Operational Page only apply to all offerings that exceed a fixed dollar amount, rather than offerings in excess of 10% of total revenue.³⁴ Another commenter stated that the information requested by the Operational Page for firm underwriting and selling group arrangements is identical to the information requested following a blue sheet transaction.³⁵ The commenter urged that if the proposed SSOI is incorporated as represented, FINRA cease routinely requiring firms to provide identical information for firm underwriting

³¹ B of A and SIFMA.

³² B of A and SIFMA.

³³ Farragut and REISA.

³⁴ Kinkade.

³⁵ NAIBD.

and selling group arrangements following a blue-sheet transaction.³⁶ Finally, one commenter stated that Operational Page reporting should be disassociated with financial reporting for any member filing FOCUS Report Part IIA (not filing FOCUS Report Part II) by having its own format, frequency and deadline schedule.³⁷

FINRA believes the Operational Page of the proposed SSOI would provide greater transparency and valuable information regarding unregistered offerings. A fixed dollar amount threshold would be inappropriate as FINRA needs to capture revenue that is significant to the member. Members that exceed the 10% of total revenue threshold are considered to be obtaining significant revenue from unregistered offerings. Additionally, the information requested from the Operational Page is not identical to the information requested in a blue sheet transaction.³⁸ Finally, the Operational Page is part of the proposed SSOI, and therefore would be subject to the same frequency and deadline schedule of the proposed SSOI.

J. Implementation

Several commenters requested that FINRA provide sufficient lead time for members to prepare for the new rule.³⁹ A number of commenters stated system changes would be needed to capture the requested information.⁴⁰ One commenter suggested that the implementation of the proposed SSOI be staged as a series of pilots, beginning with clearing firms, then gradually covering the membership by firm size.⁴¹ FINRA is sensitive to the operational and systems changes that may be necessary for members to complete the proposed SSOI, and as a result, is

³⁶ NAIBD.

³⁷ Kinkade.

³⁸ See SEA Rule 17a-25.

³⁹ Citi, RBDA and SIFMA.

⁴⁰ Citi, FAF, HCM, M.S. Howells, NAIBD, RBDA and SIFMA.

⁴¹ NAIBD.

proposing to implement the SSOI no sooner than 180 days, and no later than 365 days, following Commission approval of the proposed rule change.

K. Alternatives to Schedule

A number of commenters offered alternatives to the proposed SSOI.⁴² Several commenters suggested that more detailed information should not be required unless the particular line item represents a specified percentage of a firm's business or at least a dollar amount threshold.⁴³ One commenter suggested that FINRA consider requiring that the information requested by the proposed SSOI be submitted annually with the audit report.⁴⁴ Another commenter believed that instead of adopting the proposed SSOI, FINRA should meet with members to discuss whether a new regulatory report is needed; what format works best with the FOCUS Report; and consider the costs of implementing a system.⁴⁵ FINRA has considered these alternatives and believes that obtaining information regarding the detail of revenues earned or expenses incurred by product or other more specific categories is best achieved through the proposed SSOI. FINRA notes that it consulted with its advisory committees in connection with the development of the proposed SSOI.

L. New Financial and Operational Reports or Schedules

Several commenters suggested that any new financial or operational report or schedule required by FINRA be submitted to the SEC as a proposed rule change to allow members an opportunity to provide FINRA with feedback.⁴⁶ One commenter suggested that such submission

⁴² Allegheny, NAIBD, Sutherland and Wachtel.

⁴³ NAIBD, Sutherland and Wachtel.

⁴⁴ Allegheny.

⁴⁵ Sutherland.

⁴⁶ IMS, NAIBD, RBDA and Sutherland.

is necessary due to possible conflicts that FINRA schedules and reports may have with other laws and rules.⁴⁷ Another commenter argued that the opportunity for member comment is needed because specific line items may be missing or irrelevant over time.⁴⁸

As stated above, pursuant to proposed FINRA Rule 4524, FINRA will file with the SEC the content of any Regulatory Notice (or similar communication) issued pursuant to the proposed rule. Further, if such content contains material substantive changes, FINRA will file the content for comment with the SEC. Commenters will have an opportunity to express their concerns and provide feedback at that time.

M. Comment Period

One commenter expressed disappointment that the comment period ended the same day FINRA sent the Notice.⁴⁹ The commenter believed that FINRA did not give the public ample opportunity to study the matter. FINRA believes the commenter is mistaken as the Notice was issued on July 19, 2010, requesting comment until August 18, 2010.

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 or disapprove such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

⁴⁷ Sutherland.

⁴⁸ NAIBD.

⁴⁹ SCA.

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-2011-064 on the subject line.

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-2011-064. 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 website (<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 website 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-2011-064 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.⁵⁰

Kevin M. O'Neill
Deputy Secretary

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⁵⁰ 17 CFR 200.30-3(a)(12).