is a reasonable approach that may simplify compliance for some members without degrading the quality and completeness of information available to FINRA and the public.

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

Written comments were neither solicited nor received.

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

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act [16] and Rule 19b–4(f)(6) thereunder.[17]

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or 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 email to *rule-comments@sec.gov.* Please include File No. SR–FINRA–2015–055 on the subject line.

Paper Comments

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

All submissions should refer to File No. SR–FINRA–2015–055. This file number should be included on the subject line if email 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 10:00 a.m. and 3:00 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 No. SR–FINRA–2015–055, and should be submitted on or before January 13, 2016.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[18]

Robert W. Errett,

Deputy Secretary.

[FR Doc. 2015–32191 Filed 12–22–15; 8:45 am]

BILLING CODE 8011–01–P

[16] 15 U.S.C. 78s(b)(3)(A).

[17] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. FINRA has satisfied this requirement.

[18] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–76675; File No. SR–FINRA–2015–054]

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change To Adopt the Capital Acquisition Broker Rules

December 17, 2015.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act,'' ''Exchange Act'' or ''SEA'') [1] and Rule 19b–4 thereunder,[2] notice is hereby given that on December 4, 2015, 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 substantially 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 create a separate rule set that would apply to firms that meet the definition of ''capital acquisition broker'' and elect to be governed under this rule set.

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

There are FINRA firms that are solely corporate financing firms that advise companies on mergers and acquisitions,

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

advise issuers on raising debt and equity capital in private placements with institutional investors, or provide advisory services on a consulting basis to companies that need assistance analyzing their strategic and financial alternatives. These firms often are registered as broker-dealers because of their activities and because they may receive transaction-based compensation as part of their services.

Nevertheless, these firms do not engage in many of the types of activities typically associated with traditional broker-dealers. For example, these firms typically do not carry or act as an introducing broker with respect to customer accounts, handle customer funds or securities, accept orders to purchase or sell securities either as principal or agent for the customer, exercise investment discretion on behalf of any customer, or engage in proprietary trading of securities or market-making activities.

FINRA is proposing to establish a separate rule set that would apply exclusively to firms that meet the definition of ''capital acquisition broker'' (''CAB'') and that elect to be governed under this rule set. CABs would be subject to the FINRA By-Laws, as well as core FINRA rules that FINRA believes should apply to all firms. The rule set would include other FINRA rules that are tailored to address CABs' business activities.

General Standards (CAB Rule 010 Series)

Proposed CAB Rule 014 provides that all persons that have been approved for membership in FINRA as a CAB and persons associated with CABs shall be subject to the Capital Acquisition Broker rules and the FINRA By-Laws (including the schedules thereto), unless the context requires otherwise. Proposed CAB Rule 015 provides that FINRA Rule 0150(b) shall apply to the CAB rules. FINRA Rule 0150(b) currently provides that the FINRA rules do not apply to transactions in, and business activities relating to, municipal securities as that term is defined in the Exchange Act.

CAB Rule 016 sets forth basic definitions modified as appropriate to apply to CABs. The proposed definitions of ''capital acquisition broker'' and ''institutional investor'' are particularly important to the application of the rule set.

The term ''capital acquisition broker'' would mean any broker that solely engages in any one or more of the following activities:

- Advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions, valuation services, expert testimony, litigation support, and negotiation and structuring services;
- qualifying, identifying, soliciting, or acting as a placement agent or finder with respect to institutional investors in connection with purchases or sales of unregistered securities; and
- effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company through the purchase, sale, exchange, issuance, repurchase, or redemption of, or a business combination involving, securities or assets of the company, to a buyer that will actively operate the company or the business conducted with the assets of the company, in accordance with the terms and conditions of an SEC rule, release, interpretation or ''no-action'' letter that permits a person to engage in such activities without having to register as a broker or dealer pursuant to Section 15(b) of the Exchange Act.[3]

A firm would be permitted to register as, or change its status to, a CAB *only* if the firm solely engages in one or more of these activities.

The term ''capital acquisition broker'' would not include any broker or dealer that:

- Carries or acts as an introducing broker with respect to customer accounts;
- holds or handles customers' funds or securities;
- accepts orders from customers to purchase or sell securities either as principal or as agent for the customer (except as permitted by paragraphs (c)(1)(F) and (G) of CAB Rule 016);
- has investment discretion on behalf of any customer;
- engages in proprietary trading of securities or market-making activities; or
- participates in or maintains an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933.[4]

The term ''institutional investor'' would have the same meaning as that term has under FINRA Rule 2210 (Communications with the Public), with one exception. The term would include any:

- Bank, savings and loan association, insurance company or registered investment company;
- governmental entity or subdivision thereof;
- employee benefit plan, or multiple employee benefit plans offered to employees of the same employer, that meet the requirements of Section 403(b) or Section 457 of the Internal Revenue Code and in the aggregate have at least 100 participants, but does not include any participant of such plans;
- qualified plan, as defined in Section 3(a)(12)(C) of the Exchange Act, or multiple qualified plans offered to employees of the same employer, that in the aggregate have at least 100 participants, but does not include any participant of such plans;
- other person (whether a natural person, corporation, partnership, trust, family office or otherwise) with total assets of at least $50 million; and
- person acting solely on behalf of any such institutional investor.

The definition also would include any person meeting the definition of ''qualified purchaser'' as that term is defined in Section 2(a)(51) of the Investment Company Act of 1940 (''1940 Act'').[5]

Member Application and Associated Person Registration (CAB Rule 100 Series)

The proposed CAB Rule 100 Series sets forth the requirements for firms that wish to register as a CAB. The proposed CAB Rule 100 Series generally incorporates by reference FINRA Rules 1010 (Electronic Filing Requirements for Uniform Forms), and 1122 (Filing of Misleading Information as to Membership or Registration), and NASD Rules 1011 (Definitions), 1012 (General Provisions), 1013 (New Member Application and Interview), 1014 (Department Decision), 1015 (Review by National Adjudicatory Council), 1016 (Discretionary Review by FINRA Board), 1017 (Application for Approval of Change in Ownership, Control, or Business Operations), 1019 (Application to Commission for Review), 1090 (Foreign Members), 1100 (Foreign Associates) and IM–1011–1 (Safe Harbor for Business Expansions). Accordingly, a CAB applicant would follow the same procedures for membership as any other FINRA applicant, with four modifications.

[3] *See* proposed CAB Rule 016(c)(1).

[4] *See* proposed CAB Rule 016(c)(2).

[5] *See* proposed CAB Rule 016(i). FINRA Rule 2210 does not include ''qualified purchaser'' within its definition of ''institutional investor.''

• First, an applicant for membership that seeks to qualify as a CAB would have to state in its application that it intends to operate solely as such.

• Second, in reviewing an application for membership as a CAB, the FINRA Member Regulation Department would consider, in addition to the standards for admission set forth in NASD Rule 1014, whether the applicant's proposed activities are consistent with the limitations imposed on CABs under CAB Rule 016(c).

• Third, proposed CAB Rule 116(b) sets forth the procedures for an existing FINRA firm to change its status to a CAB. If an existing firm is already approved to engage in the activities of a CAB, and the firm does not intend to change its existing ownership, control or business operations, it would not be required to file either a New Member Application (''NMA'') or a Change in Membership Application (''CMA''). Instead, such a firm would be required to file a request to amend its membership agreement or obtain a membership agreement (if none exists currently) to provide that: (i) The firm's activities will be limited to those permitted for CABs under CAB Rule 016(c), and (ii) the firm agrees to comply with the CAB rules.[6]

• Fourth, proposed CAB Rules 116(c) and (d) set forth the procedures for an existing CAB to terminate its status as such and continue as a FINRA firm. Under Rule 116(c), such a firm would be required to file a CMA with the FINRA Member Regulation Department, and to amend its membership agreement to provide that the firm agrees to comply with all FINRA rules.[7]

Under Rule 116(d), however, if during the first year following an existing FINRA member firm's amendment to its membership agreement to convert a full-service broker-dealer to a CAB pursuant to Rule 116(b) a CAB seeks to terminate its status as such and continue as a FINRA member firm, the CAB may notify the FINRA Membership Application Program group of this change without having to file an application for approval of a material change in business operations pursuant to NASD Rule 1017. The CAB would instead file a request to amend its membership agreement to provide that the member firm agrees to comply with all FINRA rules, and execute an amended membership agreement that imposes the same limitations on the member firm's activities that existed prior to the member firm's change of status to a CAB.[8]

The proposed CAB Rule 100 Series also would govern the registration and qualification examinations of principals and representatives that are associated with CABs. These Rules incorporate by reference NASD Rules 1021 (Registration Requirements—Principals), 1022 (Categories of Principal Registration), 1031 (Registration Requirements—Representatives), 1032 (Categories of Representative Registration), 1060 (Persons Exempt from Registration), 1070 (Qualification Examinations and Waiver of Requirements), 1080 (Confidentiality of Examinations), IM–1000–2 (Status of Persons Serving in the Armed Forces of the United States), IM–1000–3 (Failure to Register Personnel) and FINRA Rule 1250 (Continuing Education Requirements). Accordingly, CAB firm principals and representatives would be subject to the same registration, qualification examination, and continuing education requirements as principals and representatives of other FINRA firms. CABs also would be subject to FINRA Rule 1230(b)(6) regarding Operations Professional registration.

Duties and Conflicts (CAB Rule 200 Series)

The proposed CAB Rule 200 Series would establish a streamlined set of conduct rules. CABs would be subject to FINRA Rules 2010 (Standards of Commercial Honor and Principles of Trade), 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices), 2040 (Payments to Unregistered Persons),[9] 2070 (Transactions Involving FINRA Employees), 2080 (Obtaining an Order of Expungement of Customer Dispute Information from the CRD System), 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information), 2263 (Arbitration Disclosure to Associated Persons Signing or Acknowledging Form U4), and 2268 (Requirements When Using Predispute Arbitration Agreements for Customer Accounts).

CAB Rules 209 and 211 would impose know-your-customer and suitability obligations similar to those imposed under FINRA Rules 2090 and 2111. CAB Rule 211(b) includes an exception to the customer-specific suitability obligations for institutional investors similar to the exception found in FINRA Rule 2111(b).

Proposed CAB Rule 221 is an abbreviated version of FINRA Rule 2210 (Communications with the Public), essentially prohibiting false and misleading statements.

Under proposed CAB Rule 240, if a CAB or associated person of a CAB had engaged in activities that would require the CAB to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on CABs under CAB Rule 016(c), FINRA could examine for and enforce all FINRA rules against such a broker or associated person, including any rule that applies to a FINRA broker-dealer that is not a CAB or to an associated person who is not a person associated with a CAB.

FINRA has determined not to subject CABs to FINRA Rules 2121 (Fair Prices and Commissions), 2122 (Charges for Services Performed), and 2124 (Net Transactions with Customers), since CABs' business model does not raise the same concerns that Rules 2121, 2122 and 2124 are intended to address.

Rule 2121 provides that, for securities in both listed and unlisted securities, a member that buys for its own account from its customer, or sells for its own account to its customer, shall buy or sell at a price which is fair, taking into consideration all relevant circumstances, including market conditions with respect to the security at the time of the transaction, the expense involved, and the fact that the member is entitled to a profit. Further, if the member acts as agent for its customer in any such transaction, the member shall not charge its customer more than a fair commission or service charge, taking into consideration all relevant circumstances, including market conditions with respect to the security at the time of the transaction, the expense of executing the order and the value of any service the member may have rendered by reason of its experience in and knowledge of such security and the market therefor.

CABs would not be permitted to act as a principal in a securities transaction. Accordingly, the provisions of Rule 2121 that govern principal transactions would not apply to a CAB's permitted activities.

CABs would be permitted act as agent in a securities transaction only in very narrow circumstances. CABs would be allowed to act as an agent with respect to institutional investors in connection with purchases or sales of unregistered securities. CABs also would be

[6] There would not be an application fee associated with this request.

[7] Absent a waiver, such a firm would have to pay an application fee associated with the CMA. *See* FINRA By-Laws, Schedule A, Section 4(i).

[8] To the extent that the rules applicable to the member firm had been amended since it had changed its status to a CAB, FINRA would have the discretion to modify any limitations to reflect any new rule requirements.

[9] The SEC has approved FINRA's rule change to adopt rules relating to payments to unregistered persons for the consolidated FINRA rulebook. *See Regulatory Notice* 15–07 (March 2015). FINRA Rule 2040 became effective on August 24, 2015.

permitted to effect securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company or the business conducted with the assets of the company in accordance with the terms and conditions of an SEC rule, release, interpretation or ''no-action'' letter.

In both instances, FINRA believes that these circumstances either involve institutional parties that negotiate the terms of permitted securities transactions without the need for the conditions set forth in Rule 2121, or involve the sale of a business as a going concern, which differs in nature from the types of transactions that typically raise issues under Rule 2121.

Rule 2122 provides that charges, if any, for services performed, including, but not limited to, miscellaneous services such as collections due for principal, dividends, or interest; exchange or transfer of securities; appraisals, safekeeping or custody of securities, and other services shall be reasonable and not unfairly discriminatory among customers. As discussed above, CABs typically provide services to institutional customers that generally do not need the protections that Rule 2122 offers, since these customers are capable of negotiating fair prices for the services that CABs provide. Moreover, CABs are not permitted to provide many of the services listed in Rule 2122, such as collecting principal, dividends or interest, or providing safekeeping or custody services.

Rule 2124 sets forth specific requirements for executing transactions with customers on a ''net'' basis. ''Net'' transactions are defined as a type of principal transaction, and CABs may not trade securities on a principal basis. For these reasons, FINRA does not believe it is necessary to include FINRA Rules 2121, 2122 and 2124 as part of the CAB rule set.

CAB Rule 201 would subject CABs to FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade), which requires a member, in the conduct of its business, to observe high standards of commercial honor and just and equitable principles of trade. Depending on the facts, other rules, such as Rule 2010, may apply in situations in which a CAB charged a commission or fee that clearly is unreasonable under the circumstances.

Supervision and Responsibilities Related to Associated Persons (CAB Rule 300 Series)

The proposed CAB Rule 300 Series would establish a limited set of supervisory rules for CABs. CABs would be subject to FINRA Rules 3220 (Influencing or Rewarding Employees of Others), 3240 (Borrowing from or Lending to Customers), and 3270 (Outside Business Activities of Registered Persons).

Proposed CAB Rule 311 would subject CABs to some, but not all, of the requirements of FINRA Rule 3110 (Supervision) and, consistent with Rule 3110, is designed to provide CABs with the flexibility to tailor their supervisory systems to their business models. CABs would be subject to many of the provisions of Rule 3110 concerning the supervision of offices, personnel, customer complaints, correspondence and internal communications. However, CABs would not be subject to the provisions of Rule 3110 that require annual compliance meetings (paragraph (a)(7)), review and investigation of transactions (paragraphs (b)(2) and (d)), specific documentation and supervisory procedures for supervisory personnel (paragraph (b)(6)), and internal inspections (paragraph (c)).

FINRA does not believe that the annual compliance meeting requirement in FINRA Rule 3110(a)(7) should apply to CABs given the nature of CABs' business model and structure. FINRA has observed that most current FINRA member firms that would qualify as CABs tend to be small and often operate out of a single office. In addition, the range of rules that CABs would be subject to is narrower than the rules that apply to other broker-dealers. Moreover, as noted above, CABs would be subject to both the Regulatory and Firm Element continuing education requirements. Accordingly, FINRA does not believe that CABs need to conduct an annual compliance meeting as required under FINRA Rule 3110(a)(7).[10] The fact that the annual compliance meeting requirement would not apply to CABs or their associated persons in no way would reduce their responsibility to have knowledge of and comply with applicable securities laws and regulations and the CAB rule set.

FINRA does not believe that FINRA Rule 3110(b)(2), which requires members to adopt and implement procedures for the review by a registered principal of all transactions relating to the member's investment banking or securities business, or FINRA Rule 3110(d), which imposes requirements related to the investigation of securities transactions and heightened reporting requirements for members engaged in investment banking services, should apply to CABs. CABs would not be permitted to carry or act as an introducing broker with respect to customer accounts, hold or handle customers' funds or securities, accept orders from customers to purchase or sell securities except under the narrow circumstances discussed above, have investment discretion on behalf of any customer, engage in proprietary trading or market-making activities, or participate in Crowdfunding or Regulation A securities offerings. Accordingly, due to these restrictions, FINRA does not believe a CAB's business model necessitates the application of these provisions, which primarily address trading and investment banking functions that are beyond the permissible scope of a CAB's activities.[11]

FINRA does not believe that the requirements of FINRA Rule 3110(b)(6) should apply to CABs. Paragraph (b)(6) generally requires a member to have procedures to prohibit its supervisory personnel from (1) supervising their own activities; and (2) reporting to, or having their compensation or continued employment determined by, a person the supervisor is supervising.[12] FINRA also does not believe that FINRA Rule 3110(c), which requires members to conduct internal inspections of their businesses, should apply to CABs.

FINRA believes that a CAB's business model, which is geared toward acting as a consultant in capital acquisition transactions, or acting as an agent solely in connection with purchases or sales of unregistered securities to institutional investors, or with the transfer of ownership and control of a privately-held company, does not give rise to the same conflicts of interest and

[10] For the same reasons, FINRA does not believe that FINRA Rule 3110.04 should apply to CABs.

[11] For the same reasons, FINRA does not believe that FINRA Rule 3110.05 should apply to CABs.

[12] FINRA Rule 3110(b)(6)(C)(i) and (ii). FINRA Rule 3110(b)(6) also requires that a member's supervisory procedures include the titles, registration status and locations of the required supervisory personnel and the responsibilities of each supervisory person as these relate to the types of business engaged in, applicable securities laws and regulations, and FINRA rules, as well as a record of the names of its designated supervisory personnel and the dates for which such designation is or was effective. FINRA Rule 3110(b)(6)(A) and (B). In addition, paragraph (b)(6) requires a member to have procedures reasonably designed to prevent the standards of supervision required pursuant to FINRA Rule 3110(a) from being compromised due to the conflicts of interest that may be present with respect to an associated person being supervised. FINRA Rule 3110(b)(6)(D).

supervisory concerns that paragraph (b)(6) is intended to address. As discussed above, many CABs operate out of a single office with a small staff, which reduces the need for internal inspections of numerous or remote offices. In addition, part of the purpose of creating a separate CAB rule set is to streamline and reduce existing FINRA rule requirements where it does not hinder investor protection. FINRA believes that the remaining provisions of FINRA Rule 3110, coupled with the CAB Rule 200 Series addressing duties and conflicts, will sufficiently protect CABs' customers from potential harm due to insufficient supervision.[13]

Proposed CAB Rule 313 would require CABs to designate and identify one or more principals to serve as a firm's chief compliance officer, similar to the requirements of FINRA Rule 3130(a). CAB Rule 313 would not require a CAB to have its chief executive officer (''CEO'') certify that the member has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable federal securities laws and regulations, and FINRA and MSRB rules, which are required under FINRA Rules 3130(b) and (c). FINRA does not believe the CEO certification is necessary given a CAB's narrow business model and smaller rule set.

Proposed Rule 328 would prohibit any person associated with a CAB from participating in any manner in a private securities transaction as defined in FINRA Rule 3280(e).[14] FINRA does not believe that an associated person of a CAB should be engaged in selling securities away from the CAB, nor should a CAB have to oversee and review such transactions, given its limited business model. This restriction would not prohibit associated persons from investing in securities on their own behalf, or engaging in securities transactions with immediate family members, provided that the associated person does not receive selling compensation.

Proposed CAB Rule 331 would require each CAB to implement a written anti-money laundering (''AML'') program. This is consistent with the SEC's requirements and Chapter X of Title 31 of the Code of Federal Regulations. Accordingly, the proposed rule is similar to FINRA Rule 3310 (Anti-Money Laundering Compliance Program); however, the proposed rule contemplates that all CABs would be eligible to conduct the required independent testing for compliance every two years.

Financial and Operational Rules (CAB Rule 400 Series)

The proposed CAB Rule 400 Series would establish a streamlined set of rules concerning firms' financial and operational obligations. CABs would be subject to FINRA Rules 4140 (Audit), 4150 (Guarantees by, or Flow through Benefits for, Members), 4160 (Verification of Assets), 4511 (Books and Records—General Requirements), 4513 (Records of Written Customer Complaints), 4517 (Member Filing and Contact Information Requirements), 4524 (Supplemental FOCUS Information), 4530 (Reporting Requirements), and 4570 (Custodian of Books and Records).

Proposed CAB Rule 411 includes some, but not all, of the capital compliance requirements of FINRA Rule 4110. CABs would be required to suspend business operations during any period a firm is not in compliance with the applicable net capital requirements set forth in SEA Rule 15c3–1, and the rule also would authorize FINRA to direct a CAB to suspend its operation under those circumstances. Proposed CAB Rule 411 also sets forth requirements concerning withdrawal of capital, subordinated loans, notes collateralized by securities, and capital borrowings.

CABs would not be subject to FINRA Rules 4370 (Business Continuity Plans and Emergency Contact Information) or 4380 (Mandatory Participation in FINRA BC/DR Testing Under Regulation SCI). FINRA does not believe it would be necessary for a CAB to maintain a business continuity plan (BCP), given a CAB's limited activities, particularly since a CAB would not engage in retail customer account transactions or clearance, settlement, trading, underwriting or similar investment banking activities. Moreover, FINRA Rule 4380 relates to Rule SCI under the Exchange Act, which is not applicable to a member that limits its activities to those permitted under the CAB rule set.

Because CABs would not carry or act as an introducing broker with respect to customer accounts, they would have more limited customer information requirements than is imposed under FINRA Rule 4512.[15] CABs would have to maintain each customer's name and residence, whether the customer is of legal age (if applicable), and the names of any persons authorized to transact business on behalf of the customer. CABs would still have to make and preserve all books and records required under SEA Rules 17a–3 and 17a–4.

CAB Rule 452(a) establishes a limited set of requirements for the supervision and review of a firm's general ledger accounts.

Securities Offerings (CAB Rule 500 Series)

The proposed CAB Rule 500 Series would subject CABs to certain rules concerning securities offerings. CABs would be subject to FINRA Rules 5122 (Private Placements of Securities Issued by Members) and 5150 (Fairness Opinions).

Investigations and Sanctions, Code of Procedure, and Arbitration and Mediation (CAB Rules 800, 900 and 1000)

CABs would be subject to the FINRA Rule 8000 Series governing investigations and sanctions of firms, other than FINRA Rules 8110 (Availability of Manual to Customers), 8211 (Automated Submission of Trading Data Requested by FINRA), and 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA).

CABs would not be subject to FINRA Rule 8110 (Availability of Manual to Customers), which requires members to make available a current copy of the FINRA manual for examination by customers upon request. If the Commission approves this proposed rule change, the CAB rule set would be available through the FINRA Web site. Accordingly, FINRA does not believe this rule is necessary for CABs.

CABs also would not be subject to FINRA Rules 8211 (Automated Submission of Trading Data Requested by FINRA) or 8213 (Automated Submission of Trading Data for Non-Exchange-Listed Securities Requested by FINRA). Given that these rules are intended to assist FINRA in requesting trade data from firms engaged in securities trading, and that CABs would not engage in securities trading, FINRA

[13] For the same reasons, FINRA does not believe that FINRA Rules 3110.10, .12, .13, or .14 should apply to CABs. FINRA also believes that it is unnecessary to apply FINRA Rule 3110.15 to CABs, since the temporary program authorized by the rule expired on December 1, 2015.

[14] FINRA Rule 3280(e) defines ''private securities transaction'' as ''any securities transaction outside the regular course or scope of an associated person's employment with a member, including, though not limited to, new offerings of securities which are not registered with the Commission, provided however that transactions subject to the notification requirements of NASD Rule 3050, transactions among immediate family members (as defined in FINRA Rule 5130), for which no associated person receives any selling compensation, and personal transactions in investment company and variable annuity securities, shall be excluded.''

[15] *See* proposed CAB Rule 451(b).

does not believe that these rules should apply to CABs.

CABs would be subject to the FINRA Rule 9000 Series governing disciplinary and other proceedings involving firms, other than the FINRA Rule 9700 Series (Procedures on Grievances Concerning the Automated Systems). Proposed CAB Rule 900(c) would provide that any CAB may be subject to a fine under FINRA Rule 9216(b) with respect to an enumerated list of FINRA By-Laws, CAB rules and SEC rules under the Exchange Act. Proposed CAB Rule 900(d) would authorize FINRA staff to require a CAB to file communications with the FINRA Advertising Regulation Department at least ten days prior to use if the staff determined that the CAB had departed from CAB Rule 221's standards.

CABs would be subject to the FINRA Rule 12000 Series (Code of Arbitration Procedure for Customer Disputes), 13000 Series (Code of Arbitration Procedure for Industry Disputes) and 14000 Series (Code of Mediation Procedure).

If the Commission approves 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 60 days following Commission approval. The effective date will be no later than 180 days following publication of the *Regulatory Notice* announcing 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,[16] 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 will improve efficiency and reduce regulatory burden by reducing the range of rules that apply to capital acquisition brokers given their limited activities and institutional business model, while maintaining necessary investor protections.

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. FINRA has undertaken an economic impact assessment, as set forth below, to analyze the regulatory need for the proposed rulemaking, its potential economic impacts, including anticipated costs and benefits, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

Economic Impact Assessment

A. Regulatory Need

As discussed above, many firms solely engage in corporate financing activities, including advising companies on mergers and acquisitions, advising issuers on raising debt and equity capital in private placements with institutional investors, or providing advisory services on a consulting basis. These firms often register as broker-dealers because of their activities and because they may receive transaction-based compensation as part of their services, but unlike traditional broker-dealers, they do not handle customer funds or securities, carry or act as an introducing broker with respect to customer accounts, or provide products and services to retail customers. As a result, many FINRA rules are not applicable to the business activities of these firms. The proposed rule change establishes a separate set of streamlined rules that would apply exclusively to these firms and is tailored to address their business activities, while maintaining necessary investor protections.

B. Economic Impacts

The proposed rule change would impact member firms that engage in CAB-related business activities, discussed above. As a baseline and based on staff experience, FINRA preliminarily estimates that the number of member firms that meet this definition would range from 650 to 750 firms.[17] Thus, it is possible that between 16 and 19 percent of all FINRA member firms may be eligible to operate under this proposed rule set.[18] These firms currently are required to comply with all applicable FINRA rules. These firms currently may incur costs to evaluate new FINRA rules and interpretations to ensure that they are not applicable for their business.

FINRA anticipates that some firms provide similar services but are not currently registered as broker-dealers with the SEC or FINRA. For example, some firms may currently limit activities, such as not accepting transaction-based compensation for their services, to avoid broker-dealer registration requirements and attendant costs. Others may accept transaction-based compensation, but may be relying on SEC no-action relief to avoid broker-dealer registration.[19] It is possible that some of these firms would reconsider their non-registered status if the new rules were in effect.

(i) Anticipated Benefits

The proposed rule change would reduce the regulatory burden for CABs by decreasing the range and scope of current FINRA rules that would be applicable to them given their limited activities and institutional business model. For example, as discussed above, the proposed rule change would establish a streamlined set of conduct rules. Similarly, the proposed CAB rules would establish a limited set of supervisory rules that are better designed to provide CABs with the flexibility to tailor their supervisory systems to their business models. As discussed above, CABs also would be subject to more limited customer information requirements than those applicable to other broker-dealers.

The reduction in these regulatory requirements is anticipated to reduce compliance costs for member firms that would register as CABs without diminishing investor protections. These cost savings would include reduction in costs associated with maintaining FINRA membership, including ongoing compliance activities such as maintaining policies and procedures. These firms also would likely benefit from more focused examinations that are tailored to their business activities. To avail themselves of these benefits, firms would, however, be required to maintain their CAB status and as a result limit their activities to those permitted under the CAB rules.

As discussed above, CAB rules also may encourage non-member firms that engage in similar kinds of services as CABs to register with FINRA. FINRA membership would benefit these non-member firms by allowing them to expand their securities business and

[16] 15 U.S.C. 78*o*–3(b)(6).

[17] FINRA notes that a commenter reported a higher estimate of 906 member firms that would meet the CAB definition based on information available on BrokerCheck® (*See* comment of 3PM). This estimate is based on the number of firms that report their business line (in Form BD) only as ''Private Placement,'' ''Other,'' or ''Private Placement'' *and* ''Other.'' FINRA notes that these business lines may overlap with some of the business activities of CABs, but do not exactly correspond to the activities that would meet the CAB definition.

[18] There are 4,031 firms that are registered with FINRA as broker-dealers. Accordingly, 650 and 750 firms account for 16% and 19%, respectively, of the total FINRA membership. *See https://www.finra.org/newsroom/statistics* (accessed June 29, 2015).

[19] *See M&A Brokers,* 2014 SEC No-Act. LEXIS 92 (January 31, 2014).

engage in activities permitted under the CAB rules. FINRA membership would subject these firms to certain FINRA rules, including conduct rules, supervisory rules, and rules concerning financial and operational obligations of the firms. As a result, FINRA membership would increase regulatory oversight of these firms, thereby enhancing investor protection of their customers.

(ii) Anticipated Costs

A member firm that seeks to register as a CAB would incur initial legal and other compliance costs associated with effectively completing the application to amend its membership agreement to elect CAB status. Such a firm also would incur administrative costs associated with updating its policies and procedures. FINRA, however, anticipates that these costs would likely be minimal relative to the cost savings from the streamlined CAB rules. As firms would have discretion to determine whether to apply for the amended status, FINRA anticipates that only those firms that anticipate net benefits to them would do so.

Non-member firms that choose to register as a CAB would incur implementation and ongoing costs associated with joining and maintaining their broker-dealer registrations with FINRA. The initial implementation costs would include FINRA application fees, costs associated with adapting technology infrastructure for regulatory data reporting requirements, as well as other legal or consulting costs associated with developing policies and procedures to ensure continued compliance with SEC and CAB rules. The ongoing costs would include annual fees associated with FINRA membership, costs of maintaining data reporting, costs of legal work relating to FINRA membership, and other costs associated with additional compliance activities. FINRA notes, however, that the proposed rule change would not impose these costs on non-member firms because registering as a broker-dealer and electing CAB status is optional. Non-member firms would likely only choose to register as a CAB broker-dealer and incur these costs if the anticipated benefits of registering exceed the costs of doing so.

C. Alternatives

In considering how to best meet its regulatory objectives, FINRA considered several alternatives to particular features of this proposal. For example, the initial proposal would have allowed CABs to solicit only institutional investors as that term is defined in FINRA Rule 2210. As discussed in more detail below, several commenters suggested that the proposed rule change also allow CABs to provide products and services to accredited investors or qualified purchasers. FINRA's regulatory programs have uncovered significant concerns associated with the ways in which firms sell private placements to accredited investors. Accordingly, FINRA does not believe it is appropriate to lower the institutional investor threshold for the CAB rules to the accredited investor standard.

Nonetheless, FINRA agrees that the definition of institutional investor under the CAB rules should include qualified purchasers as that term is defined under the 1940 Act, since qualified purchasers are required to own significantly more investments than those required for accredited investors, and as a result qualified purchasers are more likely to have the resources necessary to protect themselves from potential sales practice problems. Accordingly, FINRA has revised the institutional investor definition to include qualified purchasers, which would allow CABs to offer interests in private funds that are excluded from the definition of ''investment company'' and thus exempt from registration under the 1940 Act, such as hedge funds or private equity funds.

In developing this proposal, FINRA also considered expanding the scope of permissible activities for CABs. For example, as discussed below, commenters suggested that FINRA allow CABs to engage in activities related to the transfer of ownership or control of a privately-held company consistent with the SEC's M&A Brokers no-action letter. FINRA agrees that CABs should be permitted to engage in merger and acquisition transactions to the same extent as an unregistered broker-dealer pursuant to the M&A Brokers no-action letter and has revised the definition of CAB to allow such activities.

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

Background

In February 2014, FINRA published *Regulatory Notice* 14–09 (the ''*Notice*''), requesting comment on a proposed rule set for firms that meet the definition of ''limited corporate financing broker'' (''LCFB'') (the ''*Notice* proposal''). A copy of the *Notice* is attached as Exhibit 2a. The comment period expired on April 28, 2014. FINRA received 51 comments in response to the *Notice*.[20] A list of the commenters in response to the *Notice* is attached as Exhibit 2b, and copies of the comment letters received in response to the *Notice* are attached as Exhibit 2c.[21] A summary of the comments and FINRA's response is provided below.

As discussed below, most of the comments opposed the *Notice* proposal on the ground that it did not go far enough to relieve LCFBs of their current regulatory burdens. This concern, combined with the limitations in activities that the proposal's rules would impose, would lead most firms commenting on the proposal not to change their status to an LCFB.[22]

Application of LCFB Rules to Municipal Securities

LCFB Rule 015 would have stated that the LCFB rules do not apply to transactions in, and business activities relating to, municipal securities as defined in Section 3(a)(29) of the Exchange Act. One commenter noted that some FINRA member firms provide financial advisory services only to municipalities or municipal agencies, including recommending the timing and type of offering and to assist in the selection of an underwriter. The commenter stated that if this type of firm does not engage in the sale of municipal securities and would otherwise qualify, it should be eligible to be an LCFB.[23]

LCFB Rule 015 would not prevent an LCFB from engaging in municipal securities activities. Rather, as revised, it simply would clarify that FINRA Rule 0150(b) applies to the CAB rules. FINRA Rule 0150(b) currently provides that the FINRA rules do not apply to transactions in, and business activities relating to, municipal securities as defined in the Exchange Act.

Definition of ''Customer''

LCFB Rule 016(d) would have defined the term ''customer'' as ''any natural person and any entity receiving corporate financing services from an LCFB.'' It also would have specified that

[20] Twenty-one of the comments were short emails or letters endorsing the comments of 3PM.

[21] *See* Exhibit 2b for a list of abbreviations assigned to commenters.

[22] As noted above, the proposal would have referred to firms subject to the proposed rule set as ''limited corporate financing brokers'' (''LCFBs'') rather than ''capital acquisition brokers'' (''CABs''). Similarly, this discussion refers to the rules proposed in the *Notice* as the ''LCFB rules'' rather than the ''CAB rules.'' The CAB rules which are submitted as part of this proposed rule change have been revised from the prior LCFB rules, but maintain the same rule numbers as the LCFB rules.

[23] *See* Sutter.

the term ''customer'' does not include a broker or dealer.

One commenter stated that this definition is unclear and should be replaced with other terms, such as ''issuer,'' ''investor,'' ''qualified investor,'' and ''intermediary,'' since these terms better describe the counterparties involved in an LCFB's business.[24] Two other commenters recommended that FINRA use the term ''client'' rather than ''customer.'' [25] Another commenter suggested that FINRA be clearer as to what types of corporate financing services a customer may receive from an LCFB.[26]

FINRA does not believe it would be appropriate to replace the term ''customer'' with other terms such as issuer, investor, or intermediary. The meaning of the term ''customer'' depends on the context in which it is used, such as the requirements to know your customer or to recommend a suitable investment to a customer. Terms such as ''issuer'' or ''investor'' would not be appropriate in these contexts. However, FINRA does believe that the term customer should be interpreted in a manner consistent with the way it is interpreted under the FINRA rules. Accordingly, FINRA has revised this term to have the same definition as it has under the FINRA rules.[27]

Institutional Investor Definition

LCFB Rule 016(h) would have allowed an LCFB to solicit only institutional investors. LCFB Rule 016(g) would have defined the term ''institutional investor'' to include banks, savings and loan associations, insurance companies, registered investment companies, governmental entities and their subdivisions, employee benefit plans and qualified plans with at least 100 participants (but not including the participants themselves), any other person with at least $50 million in assets, and persons acting on an institutional investor's behalf.

Seven commenters recommended that the LCFB rules allow LCFBs to offer interests in privately placed companies to accredited investors, as that term is defined in SEC Regulation D.[28] One commenter noted that requiring an LCFB to pre-qualify potential investors to meet the LCFB rules' definition of institutional investor, rather than the Regulation D accredited investor definition, would be difficult, since an LCFB may not know the financial status of a potential buyer, and could potentially harm an LCFB client seller by diminishing the pool of prospective investors.[29] Three other commenters recommended that the term ''institutional investor'' be replaced with a new term, ''qualified investor,'' which would include ''qualified investors'' as that term is defined under the 1940 Act.[30] One commenter questioned whether an LCFB would be permitted to accept an unsolicited offer from a non-institutional investor.[31] Another commenter inquired as to the documents that FINRA would require an LCFB to retain to confirm an investor's institutional status.[32]

As discussed in the *Notice,* FINRA purposely did not propose to define ''institutional investor'' based on a more inclusive standard, such as the definition of ''accredited investor'' in Regulation D under the Securities Act of 1933. FINRA's regulatory programs have uncovered serious concerns with the manner in which firms market and sell private placements to accredited investors. Application of the CAB rules to firms that market and sell private placements to accredited investors would require FINRA to expand the applicable conduct rules and other provisions. Therefore, lowering the threshold of ''institutional investor'' to the accredited investor standard would frustrate the purposes of a streamlined rule set.

Nevertheless, FINRA agrees that the definition of ''institutional investor'' should include persons that meet the definition of ''qualified purchaser'' under the 1940 Act.[33] Persons that meet the definition of ''qualified purchaser'' in most cases must own not less than $5 million in investments, far greater than the minimum assets required by the accredited investor standard. FINRA believes that it is much less likely that a CAB would commit the types of sales practice problems that FINRA has observed in connection with the sale of Regulation D private placements to accredited investors if an investor is required to meet the qualified purchaser standard, since a qualified purchaser likely would have the resources necessary to protect itself from potential sales practice problems. In addition, by defining ''institutional investor'' to include qualified purchasers, CABs would be able to offer interests in private issuers, such as hedge funds or private equity funds, that are excepted from the definition of ''investment company'' pursuant to Section 3(c)(7) of the 1940 Act.

Moreover, as discussed below, FINRA has proposed to expand the permissible activities of CABs to include effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company in accordance with the terms and conditions of an SEC rule, release, interpretation or no-action letter.[34] By expanding CABs' proposed activities to include these kinds of M&A transactions, CABs would not be limited to selling ownership or control of a privately-held company only to institutional investors as defined by the CAB rules, since the SEC's M&A Brokers no-action letter [35] does not contain this limitation. FINRA believes this expansion should address many of the commenters' concerns with the institutional investor definition.

Limited Corporate Financing Broker Definition

The proposed definition of LCFB would have allowed firms meeting this definition to engage in:

- Advising an issuer, including a private fund concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions; and
- qualifying, identifying, or soliciting potential institutional investors.

The proposed definition of LCFB would have excluded any broker or dealer that carries or maintains customer accounts, holds or handles customers' funds or securities, accepts orders from customers to purchase or sell securities either as principal or agent for the customer, possesses investment discretion on behalf of any customer, or engages in proprietary trading of securities or market making activities.

Although one commenter felt that the definition of LCFB was

[24] *See* 3PM.

[25] *See* Achates and Q Advisors.

[26] *See* CFSC.

[27] *See* FINRA Rule 0160(b)(4) (''The term 'customer' shall not include a broker or dealer'').

[28] *See* Achates, LIATI, SFA, Dole, RWI, HighBank, and EYCA. *See also* 17 CFR 230.501(a).

[29] *See* SFA.

[30] *See* 3PM, Q Advisors, and M&A Brokers Letter Attorneys.

[31] *See* SFA.

[32] *See* EYCF.

[33] *See* 15 U.S.C. 80a–2(a)(51).

[34] *See* proposed CAB Rule 016(c)(1)(G).

[35] *See M&A Brokers,* 2014 SEC No-Act. LEXIS 92 (January 31, 2014).

others recommended that the definition of LCFB be amended specifically to permit an LCFB to provide valuation services,[37] expert testimony and litigation support.[38] Other commenters recommended that the definition be clarified to permit LCFBs to engage in negotiation of transactions,[39] and to act as a placement agent for a buyer or seller.[40] Another commenter urged FINRA to revise the definition so that it spells out in more detail the types of advice that an LCFB may provide to a client (*e.g.,* preparing a business for sale, financial modeling, financial alternatives, evaluating competing offers, structuring transactions, due diligence and transition issues) and that it should allow an LCFB to act as a finder (introducing parties to a transaction).[41] Others recommended that LCFBs be permitted to provide research and engage in public company transactions in connection with their advisory work.[42]

Commenters also suggested that FINRA allow LCFBs to advise controlling or minority shareholders in a private business in connection with the sale of stock,[43] and that FINRA look to the SEC's M&A Brokers letter for a description of appropriate LCFB activities.[44] The latter commenter also recommended that LCFBs be allowed to solicit non-institutional investors if both the seller and buyer are or will be actively involved in running the business (which also is consistent with the M&A Brokers letter).

FINRA intended to allow CABs to provide valuation, expert testimony, litigation support, negotiation and structuring services, and to act as a placement agent for, or finder of, institutional investors. Accordingly, FINRA has revised the definition of CAB to make this clearer. FINRA does not agree, however, that CABs should be allowed to produce research for the investing public. If a CAB produced research reports, FINRA would need to consider whether to add FINRA Rule 2241 and potentially other rules to the list of CAB rules, which currently do not include these rules.

FINRA agrees that CABs should be permitted to engage in M&A transactions to the same extent as an unregistered broker pursuant to the M&A Brokers no-action letter. Accordingly, FINRA has revised the definition of CAB to allow such firms to effect securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company in accordance with the terms and conditions of an SEC rule, release, interpretation or no-action letter that permits a person to engage in such activities without registering as a broker under Section 15(b) of the Exchange Act.[45]

One commenter argued that the term ''limited corporate financing broker'' itself is problematic because it may confuse clients into thinking that a firm has reduced its servicing offerings when in fact they remain unchanged.[46] In response to this concern, FINRA has changed the name of this defined term, and the name of the rule set, from ''limited corporate financing broker'' to ''capital acquisition broker.''

New Member and Change of Business Applications

LCFB Rule 112 would have subjected LCFBs to NASD Rule 1013, which governs new FINRA membership applications. LCFB Rule 112 also would have required applicants for FINRA membership that seek to qualify as LCFBs to state in their applications that they intend to operate as an LCFB.

LCFB Rule 116 would have subjected LCFBs to NASD Rule 1017, which governs applications for approval of change in ownership, control, or business operations. Rule 116 also would have allowed an existing FINRA member firm that seeks to change its status to an LCFB, and that is already approved to engage in the activities of an LCFB, but which does not intend to change its existing ownership, control, or business operations, to file a request to amend its membership agreement or obtain a membership agreement (if none exists), to provide that: (i) The member firm's activities will be limited to those permitted for LCFBs under LCFB Rule 016(h); and (ii) the member firm agrees to comply with the LCFB rules. Rule 116 further specified that an LCFB that seeks to terminate its status as such and continue as a FINRA member firm would have to file an application for approval of a material change in business operations pursuant to NASD Rule 1017 (a ''CMA''), and would have to amend its membership agreement to provide that it agrees to comply with all FINRA rules.

One commenter also recommended that FINRA streamline the new member and change in membership process for LCFBs, reduce the time period for decisions, and lower the application fees.[47] Other commenters stated that any request to change a firm's membership agreement to elect LCFB status should be without a fee, and that firms should be allowed to revert back to their original non-LCFB status without having to file a change in membership application during the firm's first year of operation as an LCFB.[48] Commenters also noted that the proposed requirement to pay a $5000 fee as part of the CMA in order to buy back a firm's full broker status is a substantial disincentive to become an LCFB.[49]

FINRA does not agree that it should create a different new member process for applicants that are not already registered broker-dealers and that seek to become CABs. Although CABs would be subject to fewer FINRA requirements than other broker-dealers, FINRA still believes that it is important for investor protection and industry confidence reasons that FINRA have an opportunity to vet new CAB firms in the same manner that FINRA vets other new firm applicants. Similarly, if a firm wishes to change its ownership, control or business operations, FINRA believes that it is important that these changes receive the same review as any other registered firm. FINRA has modified CAB Rule 112, however, to clarify that a CAB applicant must state in its application that it intends to operate solely as a CAB.[50]

CAB Rule 116 already permits an existing FINRA member firm to elect CAB status by requesting a change in its membership agreement, and without filing a CMA or paying a filing fee. However, FINRA agrees that Rule 116 should provide some more flexibility to a CAB that seeks to revert to its full broker status within the first year after electing CAB status. Accordingly, FINRA has amended Rule 116 to provide that, if during the first year following an existing FINRA member firm's amendment to its membership agreement to elect CAB status, the firm seeks to terminate its CAB status and

[37] *See* CFSC.

[38] *See* Sutter and RWI.

[39] *See* Q Advisors.

[40] *See* Q Advisors and M&A Brokers Letter Attorneys.

[41] *See* RWI.

[42] *See* Fells and EYCF.

[43] *See* Harris.

[44] *See* ABA.

[45] FINRA also revised the list of activities that a CAB may not engage in to clarify that a CAB may not carry or act as an introducing broker with respect to customer accounts or participate in or maintain an online platform in connection with offerings of unregistered securities pursuant to Regulation Crowdfunding or Regulation A under the Securities Act of 1933. *See* proposed CAB Rule 016(c)(2).

[46] *See* McCracken.

[47] *See* M&A Brokers Letter Attorneys.

[48] *See* 3PM and RWI.

[49] *See* Achates and RWI.

[50] FINRA also has modified CAB Rules 111, 112, 113, 114, and 115 to clarify that they apply to persons applying for membership in FINRA as a CAB as well as to the CABs themselves.

continue as a FINRA member firm, the firm may notify the Membership Application Program group of this change without having to file a CMA. The member firm seeking this change would have to file a request to amend its membership agreement to provide that the firm agrees to comply with all FINRA rules, and execute an amended membership agreement that imposes the same limitations on the firm's activities that existed prior to the firm's change to CAB status.

Registration Categories

Proposed LCFB Rule 123 would have allowed persons registered with LCFBs to hold only a limited set of registrations that relate to an LCFB's business.[51] The proposal also would have subjected LCFBs to the Operations Professional (Series 99) registration requirement.

Commenters objected to limiting the types of registrations that an associated person of an LCFB may retain.[52] Commenters noted that registered persons may be required to hold other registrations under state law.[53] In addition, commenters argued that this restriction would penalize individuals who may want to change jobs later and return to a full service broker-dealer, where other registrations would be required. They favored allowing registered persons to retain their registrations while employed with an LCFB. Commenters also opposed requiring LCFBs to employ an Operations Professional.[54] Two commenters encouraged FINRA, as part of this process, to re-examine the permissible scope of activities of various registration categories, such as Series 22, 62, 79 and 82 registrations.[55]

However, one commenter supported the restrictions. It recommended that LCFB representatives be required to obtain the Series 79 registration, and that LCFB representatives not be permitted to obtain other registration categories or retain other existing registrations during the time they are associated with an LCFB.[56] Another commenter suggested that LCFB principals and representatives not be permitted to hold other registrations unless a firm can adequately supervise the activities covered by those registrations.[57]

FINRA is persuaded that not allowing registered principals and representatives to obtain and hold the full range of registration categories could potentially penalize individuals who have already obtained those registration categories, and that the limitations of proposed LCFB Rule 123 also could potentially conflict with state law requirements. Accordingly, FINRA is amending CAB Rule 123 to eliminate the prior restrictions on the types of registrations persons associated with CABs may hold. Associated persons still would only be permitted to retain registrations that are appropriate to their functions under the registration rules.

FINRA continues to believe that CABs should be subject to FINRA Rule 1230(b)(6) regarding Operations Professional (Series 99) registration. FINRA believes the Operations Professional registration category enhances the regulatory structure surrounding the specified (or ''covered'' functions), including contributing to the process of preparing and filing financial regulatory reports, and has noted that for some firms the Operations Professional often may be the firm's Financial and Operations Principal.[58] FINRA also is not re-examining the range of permissible activities for principals and representatives in various registration categories, as those issues are beyond the scope of this proposed rule change.

Continuing Education Requirements

Proposed LCFB Rule 125 would have required any person registered with an LCFB who has direct contact with customers in the conduct of the broker's corporate financing activities, and the immediate supervisors of such persons, to be subject to many of the same requirements contained in the Firm Element provisions of FINRA Rule 1250. Proposed LCFB Rule 125 would not have subjected persons registered with an LCFB to the Regulatory Element provisions of FINRA Rule 1250, however.

One commenter stated that it was not opposed to requiring registered persons to undergo additional training and continuing education testing to keep an associated person's registration active, but proposed that these requirements be imposed only once every two years.[59] Another commenter questioned exempting LCFB personnel from the Regulatory Element requirements of FINRA Rule 1250, and noted that investment bankers need to keep up with current rules and regulations as much as other types of brokers.[60]

Given that FINRA has revised the proposed registration rules to allow persons registered with a CAB to hold and retain any principal and representative registrations that are appropriate to their functions under the registration rules, FINRA believes it is appropriate to subject associated persons to all of the continuing education requirements of FINRA Rule 1250, including the Regulatory Element provisions. FINRA has amended CAB Rule 125 accordingly.

Expungement of Customer Dispute Information

Proposed LCFB Rule 208 (Obtaining an Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD) System) would have subjected LCFBs to FINRA Rule 2080, which sets forth requirements for members or associated persons seeking to expunge information from the CRD system arising from disputes with customers. FINRA did not receive any comments on this proposed rule.

Since the *Notice* was published, FINRA Rule 2081 (Prohibited Conditions Relating to Expungement of Customer Dispute Information) became effective.[61] FINRA Rule 2081 prohibits members and associated persons from conditioning or seeking to condition settlement of a customer dispute on, or otherwise compensating the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer information from the CRD system. The rule directly addresses any concerns about parties to a settlement ''bargaining for'' expungement relief as a condition to settlement and should apply equally to any CAB or its associated persons seeking to expunge information from the CRD system. Accordingly, FINRA has amended LCFB Rule 208 also to subject CABs and their associated persons to FINRA Rule 2081.

[51] Registered principals of LCFBs would have been permitted to hold the General Securities Principal (Series 24), Limited Principal—Financial and Operations (Series 27), Limited Principal—Introducing Broker/Dealer Financial and Operations (Series 28), and Limited Principal—General Securities Sales Supervisor (Series 9 and 10) registrations. Registered representatives of LCFBs would have been permitted to hold the General Securities Representative (Series 7), Limited Representative—Direct Participation Programs (Series 22), Limited Representative—Private Securities Offerings (Series 82), and Limited Representative—Investment Banking (Series 79) registrations.

[52] *See* 3PM, Achates, Signal Hill, Sutter, LIATA, RWI, HighBank, M&A Brokers Letter Attorneys, and EYCA.

[53] *See* 3PM, Achates, Sutter, and Q Advisors.

[54] *See* 3PM and M&A Brokers Letter Attorneys.

[55] *See* ABA and LeGaye.

[56] *See* CFSC.

[57] *See* Harris.

[58] *See Regulatory Notice* 11–33 (July 2011).

[59] *See* 3PM.

[60] *See* Washington U.

[61] *See Regulatory Notice* 14–31 (July 2014).

Know Your Customer and Suitability

Proposed LCFB Rules 209 (Know Your Customer) and 211 (Suitability) would have included slightly modified versions of the know your customer (''KYC'') and suitability requirements of FINRA Rules 2090 and 2111. Proposed LCFB Rule 211(b) specified that an LCFB or its associated person fulfills the customer-specific suitability obligations for an institutional account, as defined by FINRA Rule 4512(c), if (1) the broker or associated person has a reasonable basis to believe that the institutional customer is capable of evaluating investment risks independently, both in general and with regard to particular transactions and investment strategies involving a security or securities and (2) the institutional customer affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's recommendations. Where an institutional customer has delegated decision-making authority to an agent, such as an investment adviser or bank trust department, the rule would have applied these factors to the agent.

One commenter recommended that proposed LCFB Rule 209 be redrafted to remove any reference to ''customer,'' instead suggesting that LCFBs should be required to perform due diligence of issuers, as well as reviews of investors and intermediaries considering whether to invest in an issuer to ensure qualified status.[62] Another commenter argued that the rule as written is too vague, and that an examiner would be unable to know if a firm had met its obligations to effectively service a customer.[63]

Commenters also were largely critical of proposed LCFB Rule 211. One commenter stated that it was inappropriate to require a suitability analysis before any recommendation, and that the rule was written as if an LCFB services retail customers. This commenter suggested that any suitability analysis should only be required before a subscription or purchase agreement is signed, and only where an investor is not represented by a qualified intermediary.[64] Another commenter encouraged FINRA to more clearly define a ''recommendation'' in this context and reconsider the definition of ''customer'' under the proposed rules.[65]

On the other hand, one commenter stated that LCFBs advise issuers, and that the KYC and suitability requirements should apply to these types of firms.[66] Two other commenters agreed that LCFBs advise both sell-side and buy-side M&A clients, but do not make recommendations to customers in the traditional sense.[67]

FINRA believes that the KYC and suitability rules should apply to CABs. The KYC rule requires CABs to use reasonable diligence to know and retain the essential facts concerning every customer and concerning the authority of each person acting on behalf of such customer. Facts essential to knowing a firm's customer are those required to (a) effectively service the customer, (b) understand the authority of each person acting on behalf of the customer, and (c) comply with applicable laws, regulations and rules.

The rule is flexible in that it recognizes that the determination of what is required to service a particular client will always be based on the facts and circumstances of a firm's relationship with its client. Likewise, the fact that a firm's client is a party to an M&A or other private equity transaction does not alter the need to understand the authority of each person acting on behalf of the customer, or facts necessary to comply with applicable laws, regulations and rules. Again, these facts will depend on each transaction's facts and circumstances, and the rule recognizes this flexibility.

Likewise, FINRA also believes that CABs should be subject to suitability requirements. If a CAB does not recommend a securities transaction, as some commenters assert, then the suitability requirements would not apply. Likewise, the proposed rule specifies that a CAB or associated person fulfills the customer specific suitability requirements for institutional investors if (1) the broker or associated persons has a reasonable basis to believe that the institutional investor is capable of evaluating investment risks independently and (2) the institutional investor affirmatively indicates that it is exercising independent judgment in evaluating the broker's or associated person's recommendations. If the institutional investor has delegated decision-making authority to an agent, these factors apply to the agent. FINRA believes that this provision largely addresses concerns expressed by commenters that the proposed rule applies retail investor requirements to transactions involving institutional investors. It also recognizes that a CAB or its associated person may look to an institutional investor's agent if the investor is represented by an agent.

FINRA has added supplementary material to proposed Rule 211 to clarify that a CAB still must have a reasonable basis to believe, based on reasonable diligence, that a recommendation is suitable for at least some investors. FINRA also has added supplemental material providing guidance with regard to the institutional investor exemption from the customer specific suitability requirements. The text of both of these supplementary materials is taken from similar supplementary materials that follow FINRA Rule 2111. FINRA believes that these additions will help clarify the scope of a CAB's suitability responsibilities under proposed Rule 211.

FINRA also has revised the definition of ''customer'' to reflect the definition of this term under FINRA Rule 0160(b)(4). As revised, customer is defined as not including a broker or dealer. FINRA is making this change to make clear that the definition of customer under the CAB rules has the same meaning as under the FINRA rules.

Communications With the Public

Proposed LCFB Rule 221 would have required LCFB communications to meet the general principles-based content standards of FINRA Rule 2210, although it also would have prohibited LCFB communications from projecting or predicting performance. Proposed LCFB Rule 221 would not have required LCFBs to approve communications prior to use, nor would it have imposed any filing requirements for LCFB communications.

One commenter recommended that the proposed rule's content standards include a ''realistic approach'' to setting fair and balanced content standards to meet the realities of representing issuers of securities.[68] Another commenter argued that the proposed rule does not sufficiently protect investors, and that it should require new firms to file communications with FINRA and require registered principals to approve firm communications prior to use.[69] Another commenter argued that the cost of archiving emails for three years and reviewing emails periodically is burdensome.[70]

FINRA believes that proposed CAB Rule 221 is already sufficiently general to take into account the institutional nature of CABs' business models. However, FINRA recognizes that firms may need to include projections of an issuer's performance in communications that are sent to prospective investors,

[62] *See* 3PM.

[63] *See* Sutter.

[64] *See* 3PM.

[65] *See* ABA.

[66] *See* RWI.

[67] *See* HighBank and CSP.

[68] *See* 3PM.

[69] *See* CFSC.

[70] *See* Colonnade.

such as pro forma financial statements related to a business acquisition or combination. For this reason, FINRA has removed the prohibition on predictions or projections of performance. The proposed rule would continue to prohibit communications from implying that past performance will recur or making any exaggerated or unwarranted claim, opinion or forecast.

FINRA does not believe it is necessary to include either principal pre-use approval or filing requirements for CABs given the institutional nature of their business. CABs will be required to supervise communications, but FINRA intends to allow CABs the flexibility to determine the best means of such supervision given each firm's business model. LCFBs will be subject to the SEC's record-keeping requirements for emails under Exchange Act Rules 17a–3 and 17a–4, which FINRA has no authority to alter.

Engaging in Impermissible Activities

Proposed LCFB Rule 240 provided that, upon finding that an LCFB or associated person of an LCFB has engaged in activities that require the firm to register as a broker or dealer under the Exchange Act, and that are inconsistent with the limitations imposed on LCFBs under LCFB Rule 016(h), FINRA may examine for and enforce all FINRA rules against such a broker or associated person, including any rule that applies to a FINRA member broker-dealer that is not an LCFB or to an associated person who is not a person associated with an LCFB. One commenter argued that an LCFB that engages in impermissible activities should be given a defined remedial period and process for any unintentional activities of an LCFB until the rules have been in place for a while, given the potential for rule ambiguity.

FINRA does not believe it is necessary to include within the rule a specific remedial period for engaging in impermissible activities. FINRA believes that unintentional violations during a transition period are best handled through the examination and enforcement process on a case-by-case basis. Accordingly, FINRA is not proposing to amend the rule.

Outside Business Activities of Registered Persons

Proposed LCFB Rule 327 would have required LCFBs to be subject to FINRA Rule 3270 (Outside Business Activities). One commenter urged FINRA to clarify an LCFB's supervisory responsibilities when an associated person engages in private securities transactions away from the firm under NASD Rule 3040, and an LCFB's supervisory obligations when an associated person either is also registered with an affiliated or unaffiliated full-service broker-dealer or refers a customer to a full-service firm in return for a referral fee.[71]

An associated person of a CAB would not be permitted to engage in private securities transactions away from the firm, since such activities would be beyond the scope of permissible activities for a CAB under proposed CAB Rule 016(c).[72] However, in order to make this restriction more clear, FINRA has added CAB Rule 328, which would expressly prohibit associated persons of CABs from engaging in private securities transactions as defined in FINRA Rule 3280(e).

For the same reasons, an associated person of a CAB also would not be allowed to register with an affiliated or unaffiliated full-service broker-dealer. An associated person could receive a fee for referring business to another broker-dealer, provided that the proposed transaction would be permissible for the CAB to conduct itself.

Anti-Money Laundering Compliance Program

Proposed LCFB Rule 331 would require an LCFB to develop and implement a written AML program reasonably designed to achieve and monitor its compliance with the requirements of the Bank Secrecy Act and the Department of Treasury regulations thereunder. The AML program would have to meet many of the same standards that full-service broker-dealers must meet under FINRA Rule 3310, except that the program would provide for independent testing for compliance no less frequently than every two years, rather than every year.

Five commenters stated that AML audits should not be required for LCFBs, since such firms receive no customer deposits and have no customer accounts.[73] Another commenter argued that LCFBs should only have to implement a customer identification program (''CIP'') for issuers and intermediaries with which the LCFB does business, and for investors where there is no intermediary.[74] However, another commenter stated that there is no reason to exempt an LCFB from the one-year AML testing requirement.[75]

Because the Bank Secrecy Act imposes AML obligations on all broker-dealers, FINRA does not believe it has the authority to exempt CABs from the requirement to adopt and implement an AML program. However, due to the limited nature of CABs' securities transactions, FINRA believes it is appropriate to allow CABs to conduct independent compliance testing of their AML programs every two years rather than every year.

Capital Compliance

Proposed LCFB Rule 411 would impose on LCFBs certain requirements imposed on full-service broker-dealers under FINRA Rule 4110 (Capital Compliance). Unless otherwise permitted by FINRA, an LCFB would have to suspend all business operations during any period in which it is not in compliance with the applicable net capital requirements set forth in Exchange Act Rule 15c3–1. The proposed rule also would authorize FINRA to issue a notice pursuant to FINRA Rule 9557 directing a non-compliant LCFB to suspend all or a portion of its business. The proposed rule would impose requirements related to withdrawal of equity capital, subordinated loans, and notes collateralized by securities and capital borrowings similar to provisions in FINRA Rule 4110.

Numerous commenters recommended that FINRA either eliminate or substantially reduce net capital requirements for LCFBs,[76] and that FINRA overhaul the net capital and FOCUS reporting requirements to better apply these requirements to LCFBs' business model.[77]

The SEC, however, sets these standards under its net capital rules and FINRA believes that the SEC would have to adjust its net capital requirements before FINRA could alter the net capital requirements that it imposes under its rules. In this regard, FINRA has clarified the CAB rules to note that CABs would be required to file supplemental FOCUS reports pursuant to FINRA Rule 4524 as FINRA may deem necessary or appropriate for the protection of investors or in the public interest.

Audit

Numerous commenters urged FINRA to work with the SEC and the Public Company Accounting Oversight Board (''PCAOB'') to carve out LCFBs from the

[71] *See* CFSC.

[72] *See* CAB Rule 014 (''Persons associated with a capital acquisition broker shall have the same duties and obligations as a capital acquisition broker under the Capital Acquisition Broker rules'').

[73] *See* Growth Venture, Signal Hill, Q Advisors, CSP, and LeGaye.

[74] *See* 3PM.

[75] *See* CFSC.

[76] *See* Growth Venture and LIATI.

[77] *See* 3PM, Colonnade, Bridge 1, CMC, McCracken, RWI, M&A Brokers Letter Attorneys, IMS, and Stonehaven.

requirement to produce audited financial statements.[78] Two commenters recommended that, as an alternative to an audit, LCFBs' financials could be subject to an AICPA ''review.'' [79] Another commenter recommended that audits not be required unless a firm has 20 or more employees or $10 million in net revenues.[80]

FINRA believes that it does not have the authority to reduce or eliminate the requirement to obtain audited financial statements.

Fidelity Bonds

The proposal would subject LCFBs to FINRA Rule 4360, which requires each member firm required to join the Securities Investor Protection Corporation (''SIPC'') to maintain blanket fidelity bond coverage that provides against loss and have insuring agreements covering at least six enumerated areas. The minimum required fidelity bond amount varies depending on a firm's net capital requirements, but in any case it must be at least $100,000.

Some commenters argued this requirement should not apply to LCFBs, since fidelity bonds protect against theft of a customer's funds. Because LCFBs may not accept or hold customer funds, these commenters argue that the bond requirement makes no sense.[81] One commenter noted that an LCFB that issues a fairness opinion should be required to carry a larger fidelity bond than $100,000.[82]

In response to these comments, FINRA has determined not to subject CABs to FINRA Rule 4360 because of CABs' unique business model. CABs' clients would be limited to issuers of unregistered securities, institutional investors, and parties to a transaction involving the change of control of a privately held company. CABs would act as agent only in transactions in which funds flow directly from a purchaser of securities to the issuer or shareholder of such securities, and would not carry or act as an introducing broker in connection with customer accounts. In addition, CABs would belong to a separate FINRA membership category that would make them unique among all other FINRA member firms. For these reasons, FINRA believes it would be appropriate not to require CABs to maintain a fidelity bond under Rule 4360.

SIPC Dues

Thirteen commenters argued that an LCFB should not have to pay dues to SIPC on the ground that an LCFB would not carry or act as an introducing broker with respect to customer accounts or hold or handle customer funds.[83]

Almost all persons registered as brokers or dealers under Section 15(b) of the Exchange Act must be members of SIPC.[84] Because these requirements are imposed by statute, FINRA has no authority to exempt any CAB from SIPC membership.

Other Comments

Commenters had a number of other observations and recommendations regarding the proposed rule set, which FINRA addresses below.

One commenter recommended that FINRA relieve LCFBs from the requirement to review and file hard copies of employees' stock trading records.[85] Another commenter recommended that FINRA impose the requirements of NASD Rule 3050 on LCFBs.[86] NASD Rule 3050 imposes certain obligations on a member firm that knowingly executes a transaction for the purchase or sale of a security for the account of a person associated with another member firm, or any account over which such associated person has discretionary authority, and on an associated person who opens an account with another member firm. Among other things, upon written request by the employer member firm, the associated person must request that the executing member firm transmit duplicate account confirmations, statements or other information.

The CAB rules would not apply NASD Rule 3050 to CABs. FINRA believes that, due to the limited institutional activities of CABs and their associated persons, it is not necessary to impose this rule's obligations on CABs.

Three commenters urged FINRA to eliminate or reduce its assessments on LCFBs due to the limited level of FINRA oversight of these firms.[87] FINRA derives its revenues from a number of sources, many of which are user fees, such as fees imposed on firms that file communications with FINRA's Advertising Regulation Department, or public offerings with FINRA's Corporate Financing Department. CABs would not be subject to many of these user fees since they would not be subject to these filing requirements. However, CABs would be subject to fees and assessments that apply to all FINRA member firms, such as the gross income assessment or the new member filing fees. FINRA believes that it is appropriate to impose these more generalized assessments on CABs to cover the costs of regulating and examining CAB activities.

One commenter expressed concern that the proposed rule set will lead to differing interpretations of rules, and will create an uneven playing field with full-service broker-dealers. This commenter believes that the proposed rule set is contrary to FINRA's mission of market integrity and investor protection, and that FINRA and the industry would be better served by expanding existing rules rather than creating a new rule set.[88]

FINRA staff strives to interpret all of its rules in a consistent manner, and it will make similar efforts to interpret rules consistently if the proposal is approved. To the extent a CAB rule requires compliance with an existing FINRA rule that applies to full-service broker-dealers, the staff anticipates that it will interpret the CAB rule in the same manner as the corresponding FINRA rule. If the CAB rule differs from its FINRA rule counterpart, the staff intends to interpret the rule consistently with respect to all CABs. FINRA does not agree that the proposed rule set would be contrary to FINRA's mission of market integrity and investor protection. FINRA has carefully crafted the rule set to include rules that should apply to all broker-dealers, or to broker-dealers that engage in M&A and other private equity activities with institutional investors, while excluding from the proposal rules that have no applicability to CABs' business model, or that would impose unnecessary burdens given the kinds of activities in which CABs engage.

One commenter suggested that the Federal Trade Commission Red Flag Rules should apply to LCFBs. This

[78] *See* 3PM, Achates, Colonnade, Growth Venture, Signal Hill, Sutter, LIATA, Bridge 1, Q Advisors, Dole, McCracken, HighBank, CSP, M&A Brokers Letter Attorneys, LeGaye, and IMS.

[79] *See* Achates and RWI.

[80] *See* Anderson.

[81] *See* 3PM, Colonnade, Growth Venture, LIATI, Bridge 1, Q Advisors, Dole, McCracken, RWI, HighBank, CSP, LeGaye, IMS, and Stonehaven.

[82] *See* Sutter.

[83] *See* 3PM, Anderson, LIATI, Bridge 1, Q Advisors, Dole, McCracken, RWI, HighBank, CSP, LeGaye, IMS, and Stonehaven.

[84] *See* Section 3(a)(2)(A) of the Securities Investor Protection Act, 15 U.S.C. 78ccc(a)(2)(A). The only exceptions to this requirement are for: (i) Firms whose principal business is conducted outside the United States, as determined by SIPC; (ii) firms whose business as a broker or dealer consists exclusively of (I) the distribution of open-end investment companies or unit investment trusts; (II) the sale of variable annuities; (III) the business of insurance; or (IV) advising investment companies or insurance company separate accounts; and (iii) firms that are registered as brokers or dealers solely for the purpose of trading security futures on an exchange.

[85] *See* Colonnade.

[86] *See* CFSC.

[87] *See* Anderson, RWI, and LeGaye.

[88] *See* CFSC.

commenter noted that LCFBs may be in possession of confidential and sensitive information concerning their customers, and that these customers could be exposed to risks resulting from identity theft.[89] The proposal would not impact whether a CAB is subject to the Red Flag Rules adopted pursuant to the Fair Credit Reporting Act of 1970, as amended.[90] The application of the Red Flag Rules depends on whether a broker or dealer falls within the requirements of the SEC's Regulation S–ID.[91]

One commenter noted that the proposed rule set omits FINRA Rule 5150 (Fairness Opinions) and a reference to information barriers, such as the guidance provided in NASD *Notice to Members* 91–45 (July 1991). The commenter also recommended that FINRA clarify that the proposed rule set would apply only to broker-dealers whose enterprise-wide activities fit within the definition of LCFB, and not to affiliates of large financial conglomerates, even if the LCFB itself only engages in activities permissible for an LCFB.[92]

FINRA agrees that FINRA Rule 5150 should apply to a CAB that provides a fairness opinion that is subject to that rule. Although this rule generally applies to fairness opinions that are provided or described to public shareholders, it is possible that a CAB could serve as an advisor in connection with a public offering of securities and provide a fairness opinion in connection with the offering. In such a case, it would make sense to require the same disclosures regarding potential conflicts of interest in connection with the fairness opinion. Accordingly, FINRA is adding new CAB Rule 515 (Fairness Opinions), which would subject CABs to FINRA Rule 5150.

NASD *Notice to Members* 91–45 was a joint memorandum prepared by the National Association of Securities Dealers, Inc., the New York Stock Exchange, and a committee of the Securities Industry Association that explained the minimum elements of adequate information barrier policies and procedures pursuant to the requirements of the Insider Trading and Securities Fraud Enforcement Act of 1988. To the extent a CAB deals with information that would trigger application of this statute or any other insider trading law, the CAB would be required to have in place adequate information barriers necessary to meet these requirements.

FINRA disagrees that a CAB may not be affiliated with a broker-dealer that engages in activities that are not permitted for CABs. As discussed previously, the CAB rules would prohibit both a CAB firm and its associated persons from engaging in activities that are not permitted under the definition of CAB. However, FINRA does not believe that it would be inconsistent for an affiliate of a CAB to engage in a wider array of activities; in those cases, the affiliate would be subject to all FINRA rules, and not the CAB rules.

One commenter urged FINRA to collaborate with the North American Securities Administrators Association (''NASAA'') to further reduce regulatory burdens on LCFBs.[93] FINRA cooperates with NASAA representatives on securities regulatory issues, and expects that its staff will continue to discuss matters of mutual interest regarding CABs with NASAA representatives in the future.

Another commenter requested that FINRA confirm that LCFBs may serve as ''chaperones'' for non-U.S. broker-dealers under Exchange Act Rule 15a–6 by performing activities that are described in Rule 15a–6(a)(3) and related no-action letters. The same commenter recommended that FINRA confirm with the states that an LCFB would be eligible for an exemption from state business broker licensing laws, to the extent that they exempt other registered broker-dealers.[94]

FINRA is not prepared at this time to confirm that all activities listed in Rule 15a–6(a)(3) and related no-action letters would be permissible for a CAB. For example, these activities include effecting securities transactions and issuing all required confirmations and statements, which appear to be activities beyond what would be permitted under the CAB definition. Likewise, the question of whether a CAB would be subject to a particular state's business broker licensing laws would be better directed to that state.

Another commenter recommended that FINRA work with the SEC, NASAA, the Commodity Futures Trading Commission, the National Futures Association, and the industry to develop a unified simple regulatory approach to regulating broker-dealer activities on the basis of risk rather than on transaction-based compensation.[95] The commenter's suggestion is beyond the scope of this proposed rulemaking and would likely require changes to the federal securities laws.

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.

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 email to *rule-comments@sec.gov*. Please include File Number SR–FINRA–2015–054 on the subject line.

Paper Comments

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

All submissions should refer to File Number SR–FINRA–2015–054. This file number should be included on the subject line if email 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.,

[89] *See* RWI.

[90] Pub. L 91–508, 84 Stat. 1114 (1970), codified at 15 U.S.C. 1681–1681x.

[91] 17 CFR 248 Subpart C. *See also* Securities Exchange Act Release No. 69359 (April 10, 2013), 78 FR 23637 (April 19, 2013).

[92] *See* Washington U.

[93] *See* M&A Brokers Letter Attorneys.

[94] *See* EYCF.

[95] *See* IMS.

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–2015–054 and should be submitted on or before January 13, 2016.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[96]

Robert W. Errett,

Deputy Secretary.

[FR Doc. 2015–32189 Filed 12–22–15; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–76678; File No. 600–35]

Order Granting Chicago Mercantile Exchange Inc.'s Request To Withdraw From Registration as a Clearing Agency

December 17, 2015.

I. Introduction

On August 3, 2015, Chicago Mercantile Exchange Inc. (''CME'') filed with the Securities and Exchange Commission (''Commission'') a written request (the ''Written Request'') [1] to withdraw from registration as a clearing agency under Section 17A of the Exchange Act (''Exchange Act'').[2] The Commission published notice of CME's request in the **Federal Register** on September 1, 2015, to solicit comments from interested persons.[3] The Commission received no comments regarding the request. For the reasons discussed below, the Commission is granting CME's request to withdraw its registration as a clearing agency and requiring CME to retain and produce upon request certain records.

II. Discussion and Commission Findings

CME is registered as a derivatives clearing organization (''DCO'') with the Commodity Futures Trading Commission (''CFTC'') and offers clearing services for futures and swap products. Pursuant to Section 17A(l) of the Exchange Act,[4] CME became ''deemed registered'' as a clearing agency solely for the purpose of clearing security-based swaps (''SBS''). To date, CME has represented that it never cleared SBS and that it will not clear SBS (subject to the limited exception as described below).[5] CME also has filed an immediately-effective rule change with the Commission (File Number SR–CME–2014–49) reflecting its decision not to clear SBS.[6]

As a registered clearing agency, CME is required to comply with the requirements of the Exchange Act and the rules and regulations thereunder applicable to registered clearing agencies. These requirements include the obligation to file proposed rule changes pursuant to Section 19(b) of the Exchange Act.[7] CME, as a DCO, generally implements rule changes by self-certifying that the new rule complies with the Commodity Exchange Act and the CFTC's regulations. Following the effectiveness of the proposed rule change (SR–CME–2014–49) regarding CME's decision not to clear SBS, CME claimed that the overlapping but divergent rule review processes required pursuant to the Commodity Exchange Act and the Exchange Act have resulted in significant difficulties for CME.[8] Furthermore, CME concluded that given the absence of any actual or potential securities clearing activity by CME (with the limited exception of potentially clearing Restructuring European Single Name CDS Contracts), it believed that clearing agency registration is unnecessary and that future rule filings (whether eligible for immediate effectiveness or not) would be wasteful of both the Commission's and CME's resources and serve no statutory purpose. CME therefore submitted its request for withdrawal of its clearing agency registration pursuant to Section 19(a)(3) of the Exchange Act,[9] which states that a self-regulatory organization may ''withdraw from registration by filing a written notice of withdrawal with the Commission,'' upon such terms and conditions as the Commission, by rule, deems necessary or appropriate in the public interest or for the protection of investors.

Based upon the representations made by CME to the Commission, the Commission has determined that granting CME's request to withdraw from registration is appropriate. CME represents it is not performing actions that require registration as a clearing agency under Section 17A of the Exchange Act and has provided specific assurances regarding record-keeping, record-production and the lack of potential for future claims against it resulting from its registration as a clearing agency.[10] In its Written Request, CME represents that it will not seek to engage in securities clearing activity in reliance on any ''deemed registered'' status pursuant to Section 17A(l) of the Exchange Act.[11] CME further represents that if an affiliate of CME seeks to clear SBS or another securities product, such affiliate would do so after registering with the Commission pursuant to the process set forth in Commission Rule 17Ab2–1.[12]

Additionally, CME states that because CME never conducted any clearing activity for SBS, it has no known or anticipated claims associated with its clearing agency registration.[13] Furthermore, CME represents in the Written Request that it will maintain all documents, books, and records, including correspondence, memoranda, papers, notices, accounts and other

[96] 17 CFR 200.30–3(a)(12).

[1] *See* Letter from Larry E. Bergmann and Joseph C. Lombard, on behalf of CME, to Brent J. Fields, Secretary, Securities and Exchange Commission (August 3, 2015).

[2] 15 U.S.C. 78q–1.

[3] Securities Exchange Act Release No. 34–75762 (Aug. 26, 2015), 80 FR 52815 (Sept. 1, 2015) (600–35).

[4] 15 U.S.C. 78q–1(l).

[5] *See* Written Request at 2.

[6] *See* Securities Exchange Act Release No. 73615 (Nov. 17, 2014), 79 FR 69545 (Nov. 21, 2014) (SR–CME–2014–49). The only exception is with respect to a set of very limited circumstances beyond CME's control where single-name CDS contracts are created following the occurrence of a restructuring credit event in respect of a reference entity that is a component of an iTraxx Europe index CDS contract (''iTraxx Contract''). According to the standard terms of the iTraxx Contract, upon the occurrence of a restructuring credit event with respect to a reference entity that is a component of an iTraxx Contract, such reference entity will be ''spun out'' and maintained as a separate single-name CDS contract (a ''Restructuring European Single Name CDS Contract'') until settlement. If neither of the counterparties elects to trigger settlement, the positions in the Restructuring European Single Name CDS Contract will be maintained at CME until maturity of the index or the occurrence of a subsequent credit event for the same reference entity. CME stated that the potential clearing of Restructuring European Single Name CDS Contracts would be a necessary byproduct of clearing iTraxx Contracts. The Commission notes that CME has obtained no-action relief from the Division of Trading and Markets with regard to this circumstance.

[7] 15 U.S.C. 78s(b).

[8] *See* Written Request at 4–5.

[9] *See* Written Request. *See also* 15 U.S.C. 78s(a)(3).

[10] *See* Written Request at 2, 5–6.

[11] *See* Written Request at 2, note 3. *See also* 15 U.S.C. 78q–1(l).

[12] *See* Written Request at 2, note 3. *See also* 17 CFR 17Ab2–1.

[13] *See* Written Request at 6.