



November 16, 2021

Submitted via email: rule-comments@sec.gov

Securities and Exchange Commission
Attn: Ms. Vanessa Countryman, Secretary
100 F Street, NE
Washington, DC 20549

Re: **Petition for Rulemaking to Amend FINRA Rule 9554
To Preclude a Respondent from Raising the “Inability to Pay”
Defense Against an Industry Claimant¹**

Dear Ms. Countryman:

The Securities Industry and Financial Markets Association (“SIFMA”)² respectfully petitions the SEC, pursuant to Rule 192 of the SEC’s Rules of Practice, to amend FINRA Rule 9554. Specifically, we request that the SEC amend FINRA Rule 9554 to preclude a respondent from raising the “inability to pay” defense against an industry claimant. As discussed below, FINRA’s current allowance of this defense against industry claimants raises significant investor protection concerns, contributes to the number and amount of unpaid arbitration awards, and avoids critical CRD/BrokerCheck disclosures that the investing public, industry, and regulators would certainly want to know about and act upon.

¹ As used herein, the terms “respondent” and “industry claimant” refer to a FINRA member firm, or an associated person of a FINRA member firm, who owes a FINRA arbitration award, and to whom a FINRA arbitration award is owed, respectively.

² SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry’s nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

Executive Summary

When a respondent loses in arbitration, then fails to pay the award, FINRA proceeds under Rule 9554 to suspend the respondent. If the award is owed to an industry claimant, FINRA allows the respondent to claim the “inability to pay” the award. When FINRA allows this defense, the respondent avoids paying the award, avoids the suspension, and avoids any CRD disclosure. It is a great deal for the respondent, but a raw deal for everyone else. The industry claimant goes unpaid. FINRA loses its leverage to compel payment. The dollar balance of unpaid awards increases.

By raising this defense, respondents admit that they cannot pay their financial obligations. Yet FINRA allows them to continue doing business as usual. CRD does not require disclosure that respondents claimed the inability to pay.³ Thus, respondents’ existing and prospective customers, prospective employers, and regulators have no idea. There is no notice, no transparency.

The inability to pay defense should be eliminated. Respondents should either pay their arbitration awards or be suspended from the industry. Alternatively, if the defense persists, respondents should be required to prominently disclose on CRD that they have relied upon this defense to avoid paying an arbitration award.

Overview of the Process for, and Defenses to, Unpaid FINRA Arbitration Awards.

Under FINRA rules, a respondent must pay a monetary arbitration award within 30 days of receipt, unless a motion to vacate has been filed in court.⁴ If the respondent fails to pay the award, then FINRA initiates an expedited proceeding under FINRA Rule 9554 and gives written notice to the respondent that failure to comply within 21 days of service will result in a suspension or cancellation of firm membership or a suspension from associating with any member firm.⁵ The respondent has the right to request a hearing, and must specify all defenses to the FINRA action.

Under FINRA Rule 9554, several defenses are available to the respondent, including:

- the member or person paid the award in full or fully complied with the settlement agreement;
- the claimant has agreed to installment payments or has settled the matter;
- the member or person has filed a timely motion to vacate or modify the arbitration award; and
- the member or person has filed a petition in bankruptcy and the bankruptcy proceeding is pending or the award payment has been discharged by the bankruptcy court.⁶

³ CRD requires respondents to disclose unpaid judgments and liens, but not unpaid arbitration awards, or having raised the inability to pay defense to avoid payment of an arbitration award.

⁴ FINRA Rule 12904(j).

⁵ FINRA Rule 9554 (Failure to Comply with an Arbitration Award), available at <https://www.finra.org/rules-guidance/rulebooks/finra-rules/9554>.

⁶ 75 Fed. Reg. 32,525 (June 8, 2010), available at <https://www.govinfo.gov/content/pkg/FR-2010-06-08/pdf/FR-2010-06-08.pdf>.

In addition, if the award is owed to an *industry* claimant, the respondent may also seek to avoid suspension by claiming that he or she has the “inability to pay” the award. If FINRA finds that the respondent has sufficiently demonstrated a financial inability to pay the award, then the respondent avoids paying the award, avoids the suspension that would have been imposed, and avoids reporting of the prospective suspension on his or her CRD/BrokerCheck record.

FINRA Eliminated the “Inability to Pay” Defense Against a Customer Claimant.

In June 2010, FINRA amended Rule 9554 to preclude a respondent from raising the inability to pay defense against a *customer* claimant.⁷ As amended, the rule now reads: “When a member or associated person fails to comply with an arbitration award ... involving a *customer*, a claim of inability to pay is no defense.”⁸ FINRA’s rule change addressed only *customer* claimant awards, and not *industry* claimant awards. FINRA offered no explanation why the defense should be eliminated only with respect to customer claimants, but not industry claimants.

In support of eliminating the inability to pay defense against customer claimants, FINRA made the following supporting arguments:

- The defense limits FINRA’s leverage to suspend a respondent, and thereby induce his or her payment of the arbitration award;
- The defense provides respondents with a ready means to purposefully avoid paying an arbitration award, in violation of FINRA’s just and equitable principles rule; and
- Even if the respondent has a bona fide inability to pay, it would not be just or equitable to allow such person – who has a demonstrated issue with managing his or her own financial affairs – to avoid suspension and continue to advise retail clients.

In approving FINRA’s amendment to Rule 9554, the SEC stated, “allowing members or their associated persons that fail to pay arbitration awards to remain in the securities industry presents regulatory risks and is unfair to harmed customers.”⁹

The SEC Should Likewise Eliminate the “Inability to Pay” Defense Against an Industry Claimant.

Each of the three bulleted arguments (immediately above) that FINRA raised in favor of eliminating the defense against customer claimants applies equally to the case for eliminating the defense against industry claimants. There is no valid reason – and none has been given – to distinguish between customer and industry claimants with respect to respondents raising the inability to pay defense.

⁷ *Id.*

⁸ FINRA Rule 9554(a) (emphasis added).

⁹ 75 Fed. Reg. at 32,525.

Over the past decade, SIFMA has written to FINRA and the SEC on five separate occasions, urging the elimination of the inability to pay defense against industry claimants: November 2011,¹⁰ April 2013,¹¹ August 2013,¹² June 2017,¹³ and December 2017¹⁴ (collectively, the “SIFMA Letters”). Neither FINRA nor the SEC has ever responded directly to the previous SIFMA Letters. This letter represents our sixth writing – at a time when it is as important as ever to acknowledge the fairness and investor protection concerns that underpin and support the SEC granting the rulemaking relief that we now request, again.

***FINRA Rule 9554 Unfairly Discriminates
Against Industry versus Customer Claimants.***

The Exchange Act requires that FINRA rules must not be “designed to permit unfair discrimination between customers, issuers, brokers, or dealers.”¹⁵ In its current form, however, Rule 9554 unfairly discriminates against industry claimants by not affording them the same protections as customer claimants, who are not susceptible to an inability to pay defense, as industry claimants are. When a respondent raises the inability to pay defense against an industry claimant, FINRA Rule 9554 operates to deny the industry claimant of both payment of their arbitration claim and suspension of the respondent, at least one of which forms of relief they certainly would have obtained if they were afforded the same protections as customer claimants.

***FINRA Rule 9554 Unnecessarily Contributes to the
Number and Amount of Unpaid Arbitration Awards.***

FINRA has a substantial number and amount of unpaid arbitration awards. FINRA continues to explore ways to reduce unpaid awards. FINRA Rule 9554, however, contributes to unpaid awards by continuing to allow the inability to pay defense against industry claimants. When respondents successfully raise this defense, they avoid paying the arbitration award, avoid suspension, and eliminate FINRA’s leverage to induce payment of the award. It makes no sense. Eliminating the defense would directly and materially help reduce the number and amount of unpaid awards.

¹⁰ SIFMA letter to FINRA (Nov. 4, 2011), available at <https://www.sifma.org/wp-content/uploads/2011/11/letter-to-FINRA-re-inability-to-pay-defense-intra-industry-cases-FINAL-11-4-11.pdf>.

¹¹ SIFMA letter to SEC (Apr. 15, 2013), available at <https://www.sifma.org/wp-content/uploads/2017/05/sifma-submits-comments-to-the-sec-on-the-finra-proposed-change-to-rule-8313-and-the-%E2%80%9Cinability-to-pay%E2%80%9D-defense.pdf>.

¹² SIFMA letter to SEC (Aug. 1, 2013), available at <https://www.sifma.org/wp-content/uploads/2017/05/sifma-submits-supplemental-comments-to-the-sec-on-the-finra-proposed-change-to-rule-8313-and-the-%E2%80%9Cinability-to-pay%E2%80%9D-defense.pdf>.

¹³ SIFMA letter to FINRA (Jun. 2, 2017), available at <https://www.sifma.org/wp-content/uploads/2017/06/SIFMA-Submits-Comments-on-the-Transparency-of-FINRA%E2%80%99s-Dispute-Resolution-Program.pdf>.

¹⁴ SIFMA letter to FINRA (Dec. 15, 2017), available at <https://www.sifma.org/wp-content/uploads/2017/12/SIFMA-Comments-on-FINRA-RN-17-33.pdf>.

¹⁵ 15 U.S.C.A. § 78o-3(6) (registered securities associations), available at <https://www.law.cornell.edu/uscode/text/15/78o-3>.

***FINRA Rule 9554 Directly Harms Retail Investors and
Poses Unnecessary Risks for Firms and Regulators.***

By continuing to allow the inability to pay defense against industry claimants, FINRA Rule 9554 directly harms retail investors. A respondent who successfully raises the defense is able to not only avoid suspension, but also avoid public disclosure of a suspension under FINRA Rule 8313.¹⁶ This situation represents a significant and unacceptable transparency and investor protection problem.

The fact that a respondent has an arbitration award that he or she has not paid, and claims an inability to pay the award, would certainly be highly relevant and beneficial information to: (i) a retail investor who is currently doing, or contemplates doing, business with such respondent, (ii) a member firm that currently employs, or seeks to hire, such respondent, and (iii) a regulator who oversees such respondent. Yet, there is no public disclosure of this information. It is entirely hidden from view from the retail investors, member firms, and regulators who have the greatest interest in learning this information.

***The APA Requires Reexamination of FINRA Rule 9554
and the Untenability of the Inability to Pay Defense.***

Neither FINRA nor the SEC addressed any of the concerns, arguments, or policy arguments raised in the previous SIFMA Letters, or in this letter, when proposing or approving the FINRA rule change to eliminate the inability to pay defense with respect to customer – but not industry – claimants. Consequently, the public comment file, the rule approval process, and the substantive record, on this matter are incomplete, and fail to address major investor protection, disclosure, transparency, and fairness issues. We urge the SEC to directly address and respond to these important, substantive issues with a view toward entirely eliminating the inability to pay defense under FINRA Rule 9554.

The fix, if you will, would be exceedingly simple. The following strikethrough edit is all that would be required to grant the rulemaking relief that we request: “When a member or associated person fails to comply with an arbitration award ... ~~involving a customer~~, a claim of inability to pay is no defense.”¹⁷

**Alternatively, the SEC Should Require Public Disclosure When Respondents
Successfully Raise the Inability to Pay Defense Against an Industry Claimant.**

Alternatively, if the SEC does not elect to eliminate the defense, then at a minimum, it should require prominent CRD and BrokerCheck disclosure when a respondent successfully raises the defense – thereby avoiding payment of the award and suspension – for the benefit and protection of current and prospective retail customers, current and prospective member firm employers, and regulators alike.

* * *

¹⁶ FINRA Rule 8313(a)(3), available at <https://www.finra.org/rules-guidance/rulebooks/finra-rules/8313>.

¹⁷ FINRA Rule 9554(a) (as amended to eliminate the inability to pay defense against industry claimants).

Thank you for your thoughtful consideration of our petition. If you would like to further discuss this matter, please contact the undersigned.

Sincerely,

A handwritten signature in cursive script that reads "Kevin M. Carroll". The signature is written in black ink and has a long horizontal flourish at the end.

Kevin M. Carroll
Managing Director and
Associate General Counsel

cc: *via e-mail to:*

Robert W. Cook, President and CEO, FINRA
Robert L.D. Colby, Executive Vice President and Chief Legal Officer, FINRA
Patrice Gliniecki, Senior Vice President and Deputy General Counsel, FINRA
Richard Berry, Executive Vice President and Director, FINRA-DRS
SEC, Division of Trading and Markets, Office of Chief Counsel