Welcome and Opening Remarks
Thursday, January 23, 2020
9:00 a.m. – 9:05 a.m.

Speaker: Chip Jones
Senior Vice President
FINRA Member Relations and Education

Speaker Biography:

Chip Jones is Senior Vice President of Member Relations and Education for FINRA. In leading the Member Relations and Education Department, Mr. Jones' responsibilities include maintaining and enhancing open and effective dialog with FINRA member firms. Mr. Jones also oversees FINRA's Member Education area, which includes FINRA conferences and other member firm educational offerings such as the FINRA Institute at Georgetown for the Certified Regulatory and Compliance Professional (CRCP)® designation. Prior to joining FINRA, Mr. Jones spent six years as Vice President of Regulatory and Industry Affairs at American Express Financial Advisors (AEFA). Previous to AEFA, he spent two years as Advocacy Administrator for the Association for Investment Management and Research (AIMR). Mr. Jones was employed by the Virginia Securities Division as a senior examiner/investigator prior to joining AIMR.

South Region Member Forum

January 23, 2020 | Hollywood, FL

Welcome and Opening Remarks

FINRA®

Speaker

- Speaker
  - Chip Jones, Senior Vice President, FINRA Member Relations and Education

Transformation of FINRA's Examination and Risk Monitoring Program
Thursday, January 23, 2020
9:05 a.m. – 9:45 a.m.

During this session, FINRA staff will discuss the new firm grouping structure, the status of changes and what firms can expect going forward.

Moderator:
Thomas Nelli
Senior Vice President, Examinations and Risk Monitoring Standards
FINRA Member Supervision

Speakers:
Brooks Brown
Senior Director, Examinations – Atlanta Office
FINRA Member Supervision

Dawn Calonge
Director, Member Supervision Quality Assurance Program – Boca Raton Office
FINRA Member Supervision

Erin Vocke
Vice President, Firm Group Examinations, Retail – New Orleans Office
FINRA Member Supervision

Transformation of FINRA's Examination and Risk Monitoring Program Panelist Bios:

Moderator:

Thomas Nelli is Senior Vice President and leads teams responsible for executing examinations, setting risk monitoring standards across FINRA's firm groupings and quality assurance testing. Previously, Mr. Nelli served as Regional Director overseeing FINRA's South Region, which includes offices in Atlanta, Boca Raton, Dallas and New Orleans. Prior to joining FINRA, Mr. Nelli was a Managing Director Deputy Chief Compliance officer in Morgan Stanley Wealth Management Compliance. In this role, Mr. Nelli headed the Investment Products and Services, Advisory, Research Equity, Futures and Options and Fixed Income Compliance Groups. Mr. Nelli received a Bachelor of Science in Psychology from Brooklyn College.

Speakers:

Brooks Brown is Senior Director, Examinations in FINRA's Atlanta Office. Mr. Brown has been with FINRA since 2001 and currently oversees the High Risk Representative Program. Mr. Brown is responsible for directing the identification and examination efforts related to registered representatives exhibiting elevated risk to investors. Previously, Mr. Brown served as an Associate District Director and Examination Manager as part of the Atlanta Office's firm examination program, overseeing examiners who conducted cycle examinations for compliance with FINRA and SEC rules. Prior to joining FINRA, Mr. Brown worked with Trustmark National Bank in Jackson, Mississippi as an equity analyst in Trustmark's Trust Department. Mr. Brown is a graduate of Millsaps College in Jackson, Mississippi, and has a Master of Business Administration Degree from Millsaps College's Else School of Management. Mr. Brown also earned the Certified Regulatory and Compliance Professional designation from the Wharton School in 2013.

Dawn Calonge is Director in FINRA's Quality Assurance Program within Member Supervision. Ms. Calonge is responsible for the development and implementation of the Quality Assurance Program for Risk Monitoring within FINRA's Member Supervision Department. Prior to becoming the Director in the QA Program, Ms. Calonge was a Surveillance Director and managed the Regulatory Coordinator staff that were responsible for the ongoing risk monitoring of member firms in the Florida District Office. Prior to becoming a Surveillance Director, she served as an Examination Manager responsible for managing examination staff that conducted cycle and cause examinations. Ms. Calonge joined FINRA as a Staff Examiner, investigating a wide range of member firm activities. Prior to joining FINRA, Ms. Calonge worked at the U.S. Securities and Exchange Commission and the New York Stock Exchange. Prior to her regulatory work, Ms. Calonge worked in the accounting field and received her Bachelor of Business Administration degree with a major in Accounting from the University of Miami in Coral Gables, Florida.

Erin C. Vocke is Vice President, Firm Group Examinations, Retail located in the New Orleans District Office. Ms. Vocke began her career in 1995 as an examiner in the New Orleans District Office. During this time, she conducted routine and cause examinations of member firms and focused examinations in the areas of variable products and mutual funds. Ms. Vocke became Supervisor of Examiners and relocated to the Florida District Office. She assumed responsibilities for supervising Continuing Membership Applications and financial surveillance of member firms, in addition to routine and cause examinations. Ms. Vocke was promoted to Associate District Director of the Dallas Office and assumed responsibility of overseeing the District cycle, cause, financial surveillance and Membership Application Programs. She served as the District Director of the Dallas District Office for approximately five years and the District Director for both the Dallas and New Orleans District Offices for approximately six years. In her new role, she will be responsible for examinations of Retail member firms across Member Supervision.

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Transformation of FINRA's Examination and Risk Monitoring Program

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Panelists

- Moderator
  - Thomas Nelli, Senior Vice President, Examinations and Risk Monitoring Standards, FINRA Member Supervision
- Panelists
  - Brooks Brown, Senior Director, Examinations – Atlanta Office, FINRA Member Supervision
  - Dawn Calonge, Director, Member Supervision Quality Assurance Program – Boca Raton Office, FINRA Member Supervision
  - Erin Vocke, Vice President, Firm Group Examinations, Retail – New Orleans Office, FINRA Member Supervision

1 Overview of Transformation

2 Firm Groupings

3 New Structure and Roles

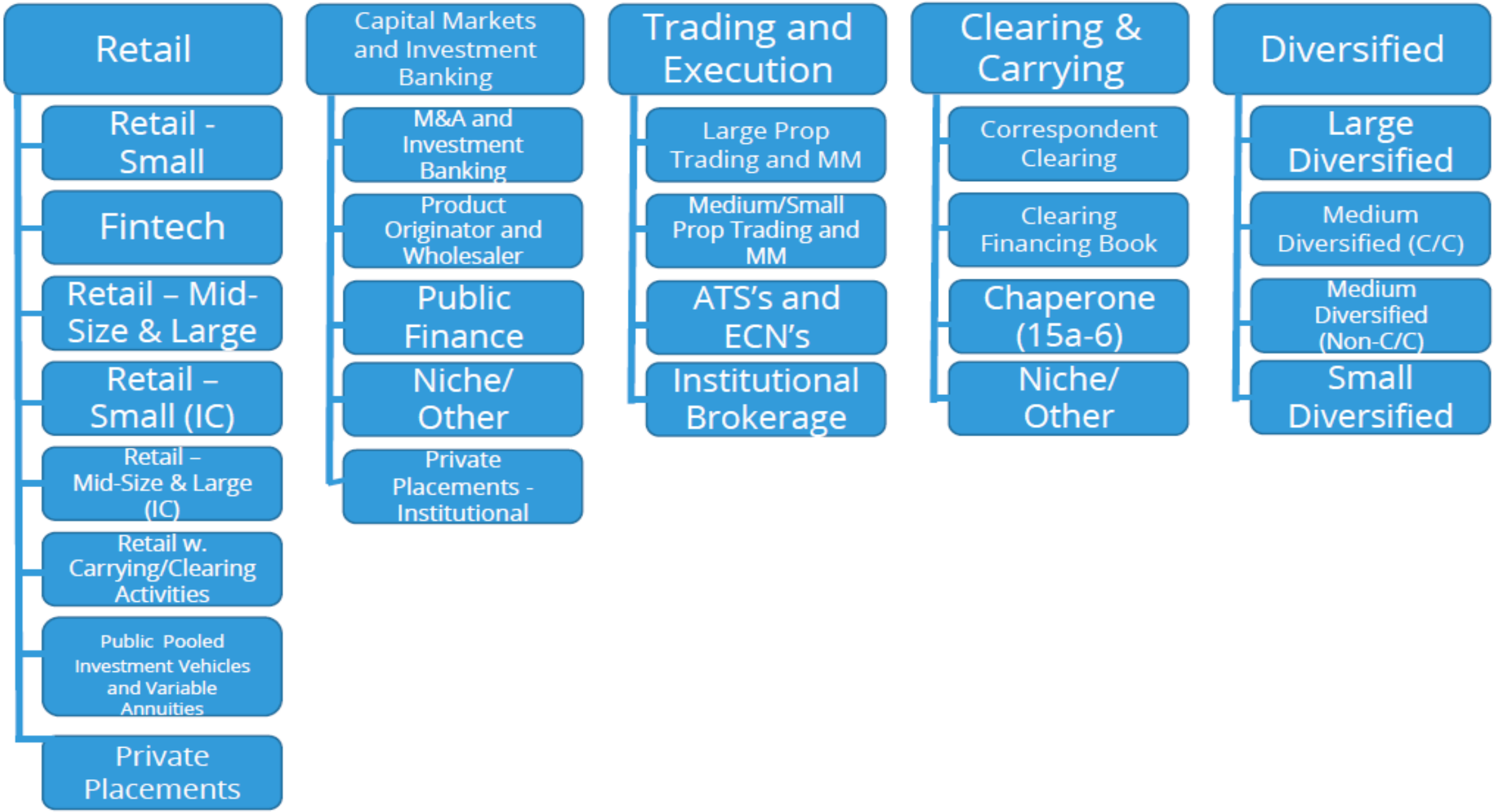
4 Risk Monitoring

5 Examination

6 Branch and Representative Programs

1 | Overview of Transformation

2 | Firm Groupings


Retail
Retail - Small
Fintech
Retail – Mid-Size & Large
Retail – Small (IC)
Retail – Mid-Size & Large (IC)
Retail w. Carrying/Clearing Activities
Public Pooled Investment Vehicles and Variable Annuities
Private Placements
Capital Markets and Investment Banking
M&A and Investment Banking
Product Originator and Wholesaler
Public Finance
Niche/ Other
Private Placements - Institutional
Trading and Execution
Large Prop Trading and MM
Medium/Small Prop Trading and MM
ATS's and ECN's
Institutional Brokerage
Clearing & Carrying
Correspondent Clearing
Clearing Financing Book
Chaperone (15a-6)
Niche/ Other
Diversified
Large Diversified
Medium Diversified (C/C)
Medium Diversified (Non-C/C)
Small Diversified

3 New Structure and Roles

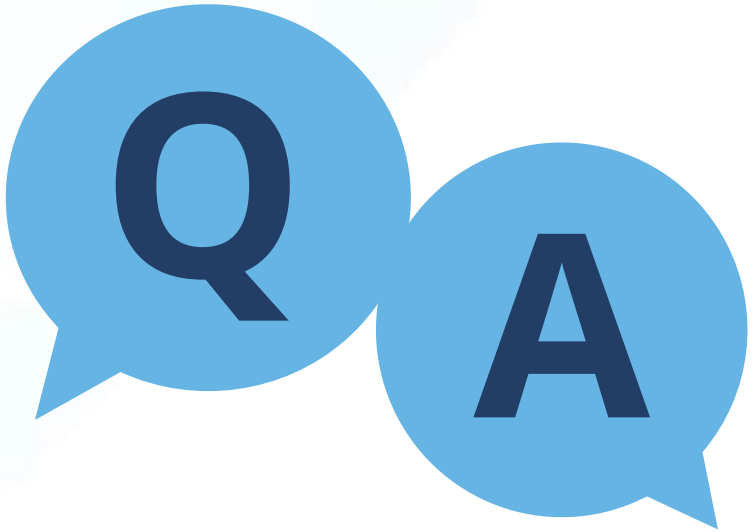
New Structure and Roles - Senior Leadership Team

- Bari Havlik, Head of Member Supervision
- Tom Nelli, Senior Vice President, will lead the teams responsible for executing the examinations, setting standards across the firm groupings, and quality assurance testing.
- Ornella Bergeron, Senior Vice President, will lead the Single Point of Accountability and Risk Monitoring teams for the Carrying and Clearing and Diversified firm groups.
- Bill St. Louis, Senior Vice President, will lead the Single Point of Accountability and Risk Monitoring teams for the Retail and Capital Markets firm groups.
- Tim Thompson, Senior Vice President, will lead the Single Point of Accountability and Risk Monitoring teams for the Trading and Execution firm group.

4 | Risk Monitoring

5 | Examinations

6 | Branch and Representative Programs



Suspicious Activity Monitoring: What to Look for and How to Find It
Thursday, January 23, 2020
10:00 a.m. – 11:00 a.m.

As the first line of defense, compliance advisors may identify money laundering and other financial crimes. It is the responsibility of all firm associates to understand these risks. Join FINRA staff and industry professionals as they discuss new and concentrated areas of focus, such as terrorist financing, bribery and corruption. Attendees will also learn about new fraud trends and risks related to digital currencies.

Moderator:
Scott Maestri
Examination Manager – Dallas Office
FINRA Member Supervision

Speakers:
Brock Miller
Vice President, US AML/FCM Brokerage Program Lead
Raymond James Financial, Inc.

Blake Snyder
Senior Director
FINRA Anti-Money Laundering Investigative Unit (AMLIU)

Melinda Wolfe
Senior Vice President and Chief Compliance Officer
Kovack Securities, Inc.

Suspicious Activity Monitoring: What to Look for and How to Find It Panelist Bios:

Moderator:

Scott H. Maestri is Examination Director located in FINRA's Dallas Office. He began his career with NASD in 1999 as an examiner in the New Orleans District Office. Mr. Maestri was promoted to management in September of 2003 and became responsible for a team of examiners who monitored member firms through cycle and cause investigations, as well as, the Membership Application Process and Financial Surveillance. Mr. Maestri was promoted to the Associate District Director position in May of 2010 where his primary responsibility was the review and approval of the District Office's major program areas. Beginning in 2020, Mr. Maestri's role changed to focus on leading a team of four managers and 20 examiners located throughout the country who are responsible for conducting examinations of firms with a retail business model. Prior to NASD, Mr. Maestri worked in a variety of sales, operational, and compliance roles with both Morgan Stanley and Legg Mason in the Jackson, Mississippi branch office locations. During the course of his career, Mr. Maestri has been selected for Advanced Management training, and successfully obtained the Certified Regulatory and Compliance Professional™ (CRCP™) designation both issued through The Wharton School at the University of Pennsylvania. Mr. Maestri received his B.B.A. in Finance from The Else School of Management at Millsaps College.

Speakers:

Brock Miller is currently Vice President within the Raymond James Financial Anti-Money Laundering (AML) & Financial Crimes Management (FCM) department. Mr. Miller is responsible for overseeing the US Broker Dealer AML & FCM Programs as well as enhancing and overseeing the enterprise Know Your Client (including client identification, client due diligence and enhanced due diligence) program. Mr. Miller joined Raymond James Financial, Inc. in September 2015 with a mandate to develop and oversee the Higher Risk Securities Management program for Raymond James, which focused on identifying and monitoring penny stock transactions. Prior to joining Raymond James in 2015, Mr. Miller spent many years with Ernst & Young assisting major financial institutions in designing and implementing their AML and Financial Crimes programs, with a focus on regulatory response. Mr. Miller is a Certified Public Accountant, Certified Anti-Money Laundering Specialist and Certified Fraud Examiner. Mr. Miller received his BBA in Accounting, with an additional focus in Finance from the University of Cincinnati.

Blake Snyder is Senior Director of FINRA's AML Investigative Unit, which consists of a specialized team of examination staff that conduct complex Anti-Money Laundering examinations. The AMLIU's other functions include providing guidance to FINRA examination and Enforcement staff in connection with examinations and investigations; providing training to FINRA staff throughout the country; and providing education and training to the industry on AML issues. Mr. Snyder assists in developing FINRA's AML-related priorities and serves as a Regulatory Specialist within FINRA in the areas of AML, fraud and financial crime. Mr. Snyder holds the Certified Regulatory and Compliance Professional™ (CRCP)™ designation, and graduated from Florida State University with a Bachelor's degree in Finance. Mr. Snyder works from FINRA's Florida Office, and has been with FINRA for 19 years.

Melinda Wolfe is Senior Vice President and Chief Compliance Officer for Kovack Securities, Inc. Ms. Wolfe has worked in the financial services industry for approximately 30 years. She has been with Kovack Securities, Inc. for 14 years, the last eight in the capacity of Chief Compliance Officer. She supervises a team of 15 compliance officers in the department. Kovack Securities, Inc. is a mid-sized, independent Broker/Dealer in business for 20 years, with approximately 450 RR's and IAR's. Kovack Securities, Inc. has, in the past five years, filed one NMA and three CMA's. Ms. Wolfe is on the FINRA South Region Committee and serves as a hearing officer. Ms. Wolfe graduated from Florida International University with a BBA, majoring in Accounting. She holds the 6, 7, 24, 27, 79, and 99 licenses.

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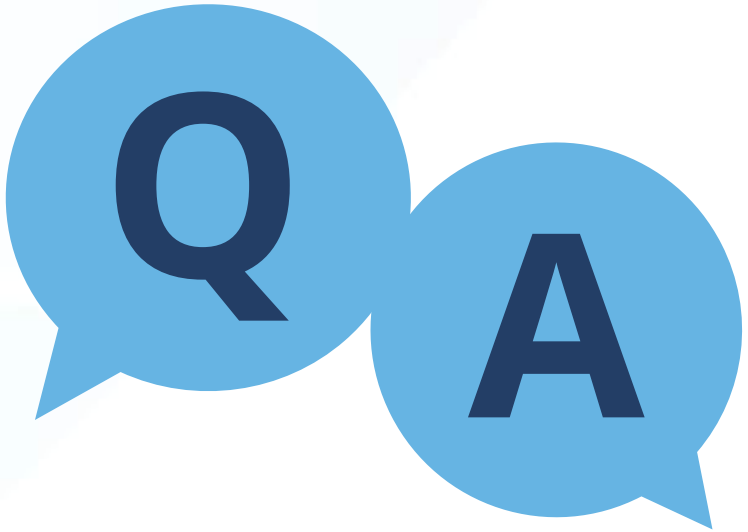
Suspicious Activity Monitoring: What to Look for and How to Find It

FINRA®

Panelists

- Moderator
  - Scott Maestri, Examination Manager – Dallas Office, FINRA Member Supervision
- Panelists
  - Brock Miller, Vice President, US AML/FCM Brokerage Program Lead, Raymond James Financial, Inc.
  - Blake Snyder, Senior Director, FINRA Anti-Money Laundering Investigative Unit (AMLIU)
  - Melinda Wolfe, Senior Vice President and Chief Compliance Officer, Kovack Securities, Inc.



FINRA Examination Findings and Priorities
Thursday, January 23, 2020
11:15 a.m. – 12:15 p.m.

Panelists discuss the examination findings and priorities letters. FINRA staff will review effective practices and considerations worth highlighting due to their potential impact on investors and markets or the frequency with which they occur.

Moderator:
Erin Vocke
Vice President, Firm Group Examinations, Retail - New Orleans Office
FINRA Member Supervision

Speakers:
Grant Gibbons
Examination Director, New Orleans Office
FINRA Member Supervision

Elizabeth Mauro
Examination Director, Boca Raton Office
FINRA Member Supervision

Michael Pedlow
Senior Vice President and Chief Compliance Officer
Kestra Investment Services, LLC

FINRA Examination Findings and Priorities Panelist Bios:

Moderator:

Erin C. Vocke is Vice President, Firm Group Examinations, Retail located in the New Orleans District Office. Ms. Vocke began her career in 1995 as an examiner in the New Orleans District Office. During this time, she conducted routine and cause examinations of member firms and focused examinations in the areas of variable products and mutual funds. Ms. Vocke became Supervisor of Examiners and relocated to the Florida District Office. She assumed responsibilities for supervising Continuing Membership Applications and financial surveillance of member firms, in addition to routine and cause examinations. Ms. Vocke was promoted to Associate District Director of the Dallas Office and assumed responsibility of overseeing the District cycle, cause, financial surveillance and Membership Application Programs. She served as the District Director of the Dallas District Office for approximately five years and the District Director for both the Dallas and New Orleans District Offices for approximately six years. In her new role, she will be responsible for examinations of Retail member firms across Member Supervision.

Speakers:

Grant Gibbons is Examination Director of the FINRA New Orleans Office. He began his career in 1997 as an Examiner in the New Orleans District Office. In March 2004, Mr. Gibbons was promoted to Supervisor of Examiners in the Dallas District Office. He oversaw a team of examiners responsible for the regulation of member firms relating to financial and operational matters, sales practice concerns, surveillance monitoring, customer complaints and termination for cause reviews. In March 2014, he assumed the role of Examination Manager in the New Orleans District Office. In this role, he managed a team of cycle examiners and helped form and successfully led the New Orleans Fixed Income team. In July 2016, he was promoted to the Associate District Director (n.k.a. Examination Director) of the New Orleans Office where he is responsible for the execution of the offices regulatory programs. Mr. Gibbons received a B.S. in Business Administration (Finance) from Auburn University in Auburn, Alabama.

Elizabeth Mauro is Examination Director at FINRA and is responsible for leading a team of managers and examiners that conduct Firm Examinations of member firms that fall within the Retail Firm Grouping. Ms. Mauro's knowledge of the securities industry has evolved from approximately 23 years of regulatory experience while working in various examination and surveillance roles at FINRA, the New York Stock Exchange and U. S. Securities and Exchange Commission. Her experience includes investigating and monitoring compliance and regulatory issues spanning a broad range of products and activities with expertise in broker-dealer risks associated with Sales Practice obligations to customers, Net Capital and Customer Segregation rules. Ms. Mauro received her Bachelor in Business Administration degree in Finance and Banking from Hofstra University, and is a Certified Anti-Money Laundering Specialist.

Mike Pedlow is Senior Vice President and Chief Compliance Officer at Kestra Financial. Mr. Pedlow directs all aspects of Compliance for Kestra Financial. He maintains company alignment with regulatory policies, while helping independent financial advisors meet the expectations of regulators as they conduct their day-to-day business. Working to balance the dual challenges of risk and business needs within the tightly regulated financial sector, Mr. Pedlow and his team actively seek to influence policy, rules and laws that may adversely impact advisors and their practice. He attributes this fresh, highly engaged approach in part to his time working as an independent financial advisor. Under his leadership, advisors experience a uniquely proactive, collaborative and supportive team of consultants within Advertising Compliance, Retirement Plan Compliance and Firm Policy. Mr. Pedlow also serves as the chief compliance officer for Kestra Private Wealth Services, a Kestra Financial affiliate. Previously, he held senior compliance positions as vice president of Investment Advisory Compliance at Kestra Financial and as RIA compliance officer at Raymond James Financial Services. Mr. Pedlow holds a Bachelor of Arts in economics from the University of South Florida and multiple industry licenses, including FINRA Series 7, 24 and 66.

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January 23, 2020 | Hollywood, FL

FINRA Examination Findings and Priorities

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Panelists

- Moderator
  - Erin Vocke, Vice President, Firm Group Examinations, Retail - New Orleans Office, FINRA Member Supervision
- Panelists
  - Grant Gibbons, Examination Director, New Orleans Office , FINRA Member Supervision
  - Elizabeth Mauro, Examination Director, Boca Raton Office, FINRA Member Supervision
  - Michael Pedlow, Senior Vice President and Chief Compliance Officer, Kestra Investment Services, LLC

AGENDA

1. Introductions
2. Nuts and Bolts
3. Topics for Discussion
4. Questions

2 | Nuts and Bolts

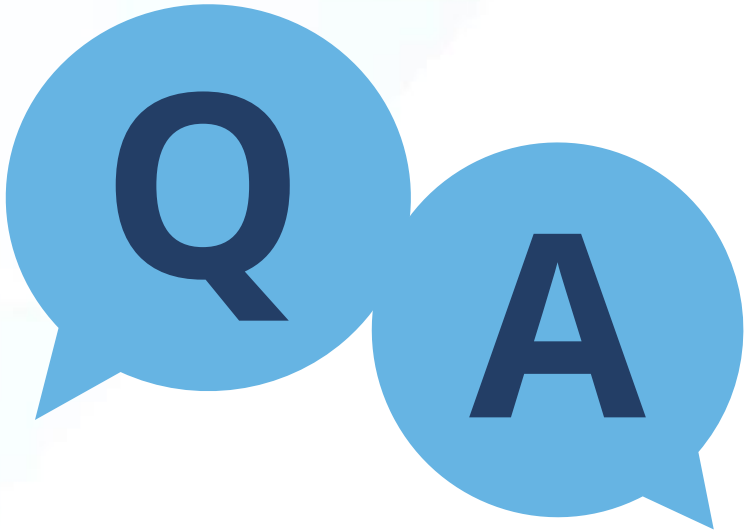
3 | Topics for Discussion

Topics for Discussion

- Variable Annuities
- Concentration
- BD/IA Issues
- Fixed Income markup/ mark-down disclosures
- Positions of Trust

Topics of Discussion (Continued)

- Cybersecurity
- Private Placements/Retail Communications
- Trading Authorization
- Contractual Commitments



2019 Report on FINRA Examination Findings and Observations

INTRODUCTION

In both 2017 and 2018, FINRA issued Reports on Examination Findings in response to firms' requests that we make publicly available a summary of key findings from FINRA's examinations of member firms. Firms use this information, as well as effective practices observed by FINRA at certain firms, to anticipate potential areas of concern and improve their procedures and controls. (We subsequently refer to the two prior years' documents as the "2017 Report" and the "2018 Report.")

The name of this year's report—the "2019 Report on Examination Findings and Observations"—reflects FINRA's recent decision to distinguish more clearly between examination findings and observations. Findings constitute a determination that a firm or registered person has violated U.S. Securities and Exchange Commission (SEC), FINRA or other relevant rules. By contrast, observations (formerly known as recommendations) are suggestions to a firm about how it could improve its control environment in order to address perceived weaknesses that elevate risk, but do not typically rise to the level of a rule violation or cannot be tied to an existing rule, and are communicated to firms separately from the formal examination report. This report reflects key findings and observations identified in recent examinations, and contains effective practices, where noted, that could help firms improve their compliance and risk management programs. Where a matter is rule-based, the applicable regulatory sources ("Regulatory Obligations") are identified under the topic heading.

As a reminder, this report does not represent a complete inventory of findings, observations or effective practices. In fact, an individual firm may not have any deficiencies identified in this report, or may have other deficiencies that were not included. Similarly, we recognize that firms may employ effective practices that are not described in this report.

Further, this report does not create new legal or regulatory requirements or new interpretations of existing requirements. There should be no inference that FINRA requires firms to implement any specific effective practices described in this report or those that extend beyond the requirements of existing securities rules and regulations.

FINRA always welcomes feedback on how we can improve the content, structure, format or other elements of future reports on examination findings and observations. If you have suggestions, please contact Steven Polansky, Senior Director, Member Supervision, at (202) 728-8331 or by email, or Elena Schlickenmaier, Principal Research Analyst, Member Supervision, at (202) 728-6920 or by email.

Supervision

Regulatory Obligations

FINRA Rule 3110 (Supervision) requires firms to establish, maintain and enforce a system to supervise their activities and the activities of their associated persons that is reasonably designed to achieve compliance with federal securities laws and regulations, as well as FINRA rules. This includes updating supervisory processes and written supervisory procedures (WSPs) to address new or amended rules, as well as products and services.

Customer account and trading supervision includes complying with other obligations, such as FINRA Rule 4512 (Customer Account Information), which specifies the categories of customer account information firms must maintain. Further, FINRA Rule 2231 (Customer Account Statements) generally requires firms to send customers account statements containing their securities positions, money balances and account activity at least once each calendar quarter. Rules 17a-3 and 17a-4 under the Securities Exchange Act of 1934 (Exchange Act), as well as the FINRA Rule Series 4510 (Books and Records Requirements) prescribe recordkeeping obligations relating to customer account records, trading records and related documentation.

Noteworthy Examination Findings

FINRA noted the following issues relating to supervision and documentation requirements.

- **Insufficient WSPs for New or Amended Rules –** Some firms did not adequately address newly adopted or amended rules by developing controls to address the new requirements applicable to their business and updating their WSPs accordingly, for example: new fixed income mark-up disclosure requirements under FINRA Rule 2232 (Customer Confirmations); new trusted contact person information requirements pursuant to Rule 4512 (Customer Account Information); temporary holds, supervision and record retention requirements under new Rule 2165 (Financial Exploitation of Specified Adults) (if they intended to use the rule); and compliance with amended Rule 3310 (Anti-Money Laundering Compliance Program), which incorporates FinCen's new Customer Due Diligence (CDD) rule obligations. Firms are expected to evaluate which new and amended laws and regulations apply to their business, and review whether their supervisory systems, WSPs and training programs need to be amended to comply with any new or amended requirement(s).
- **Limited Supervision and Internal Inspections –** Some firms did not have reasonably designed branch supervision and inspection programs. In particular, some firms did not adequately understand the activities being conducted through their branch offices, including products and services that were offered only at certain branch locations, which could prevent such firms from effectively supervising and addressing the unique risks of each branch location. Many firms also did not conduct periodic inspections of non-branch locations as required by FINRA Rule 3110(c) (Internal Inspections); did not determine relevant areas of review at branch offices or non-branch locations, taking into consideration the nature and complexity of the products and services offered or any indicators of irregularities or misconduct; failed to reduce the inspections and reviews to a written report; or did not follow through on corrective action determined to be necessary through their branch inspections.
- **Inadequate Supervision of Account Statements, Consolidated Account Reports and Other Forms –** FINRA found that some firms did not consistently maintain accurate information in account documents, which impacted their ability to reasonably supervise account activity.
    - *Consolidated Account Reports (CARs)*[1] – In certain instances, firms did not have supervisory systems to evaluate whether and when registered representatives used CARs, did not know

when CARs included manual entries by representatives or customers, and did not require review of relevant customer documents to confirm that CARs accurately represented customers' assets and values that were held outside the broker-dealer. FINRA notes that firms with stronger supervisory systems maintained comprehensive WSPs and training addressing the use and supervision of CARs; had strict limits on the use of CARs, including around manual entries; and determined whether they accurately reflected customer holdings outside of the broker-dealer.

- *Falsifying Documents* – Some firms did not have reasonable processes to detect or prevent various forms of forgeries, including "accommodation forgery," where registered representatives and associated persons asked customers to sign blank, partial or incomplete documents. Some firms expanded risk-based reviews of associated persons' communications to cover requests for customer signatures or enhanced firm reviews of customer complaints for issues relating to forgery or falsification of documents. In addition, some firms did not follow their protocols relating to notarization and medallion stamp guarantees, or did not have any supervisory procedures for supervising the use of such stamps.

- **Insufficient Supervision for Specific Types of Accounts –** FINRA noted the following supervisory issues.
  - *Restricted and Insider Accounts* – Some firms failed to update timely their watch and restricted lists, or reasonably identify and restrict account activity susceptible to insider trading. Other firms did not have surveillance systems or procedures to review and approve restricted trading because they relied on clearing firms to conduct the review. Both introducing and correspondent firms are required to have supervisory systems reasonably designed to detect and prevent insider trading.
  - *Margin Accounts* – Some firms allowed customers to open margin accounts even though the customers did not meet the firms' standards for such accounts. FINRA also identified that some firms' systems of supervision were not reasonably designed to detect recommended margin account activity that appeared to be unsuitable and inconsistent with the cost and expense of margin use. Many firms' supervisory systems could not identify situations where the firm failed to accurately disclose their own—as well as their clearing firms'—fees, costs and charges relating to customers' use of margin.
  - *Options Accounts* – FINRA noted instances where some firms did not identify or prevent registered representatives from creating and canceling fictitious orders to circumvent sales limits; mismarking opening options transactions as "closing"; listing inaccurate receipt time, execution time and origin codes on tickets; failing to record purchases and time of order transmission for routed options orders in the firms' order management systems; and failing to show the terms or conditions of the order on tickets.

Additional Resources

- *Regulatory Notice* 10-19 (FINRA Reminds Firms of Responsibilities When Providing Customers with Consolidated Financial Account Reports)
- New Account Application Template
- Supervision Topic Page
- Books and Records Topic Page
- Broker-Dealer – Written Supervisory Procedures Checklist
- Supervision category of the Peer-2-Peer Compliance Library
- Customer Information category of the Peer-2-Peer Compliance Library

Suitability[2]

Regulatory Obligations

Currently, FINRA's suitability rule establishes obligations that are central to promoting ethical sales practices and high standards of professional conduct. FINRA Rule 2111 (Suitability) establishes three primary obligations for firms and their associated persons: (1) reasonable-basis suitability, (2) customer-specific suitability and (3) quantitative suitability.[3]

Noteworthy Examination Findings

Some firms did not have adequate systems of supervision to review that recommendations were suitable in light of a customer's individual financial situation and needs, investment experience, risk tolerance, time horizon, investment objectives, liquidity needs and other investment profile factors. This report shares some new suitability-related findings, as well as additional nuances on prior years' findings.

- **Inadequate Supervision of Product Exchanges –** Some firms did not maintain a supervisory system reasonably designed to assess the suitability of recommendations that customers exchange certain products, such as mutual funds, variable annuities or unit investment trusts (UITs). In particular, some firms did not maintain blotters or other processes to identify patterns of unsuitable recommendations of exchanges involving long-term products.[4] Additionally, some firms did not reasonably supervise exchanges because they could not verify the information provided by registered representatives in their rationales to justify a recommended exchange, such as inaccurate descriptions of product fees, costs and existing product values. In other instances, firm supervision did not detect that the source of funds for a purchase was misrepresented (*i.e.*, as "new" money), when other account information revealed another likely source of funds (*e.g.*, funds from a liquidation of another financial product at the firm).
- **Limited Supervision to Identify "Red Flags" for Suitability –** Some firms' supervisory systems were not reasonably designed or used to detect red flags of possible unsuitable transactions. For example, some firms did not identify or question patterns of similar recommendations by representatives or branch offices across many customers with different risk profiles, time horizons and investment objectives. In some instances, several customers of a representative or branch office appeared to have made "unsolicited" transactions in identical securities, which could raise questions around whether the transactions were actually "unsolicited."
- **Inadequate Supervision of Changes to Customer Account Information –** As discussed further in the Supervision section of this report, FINRA noted instances where registered representatives unilaterally changed account information, such as customers' income, net worth or account objectives. In many instances, the changes preceded or were contemporaneous with one or more transactions that, but for the account change, would have been subject to heightened supervisory scrutiny, raised suitability concerns or would not have been approved.
- **Limited Supervision of Trading Activity for Excessive Trading or Churning –** FINRA identified a variety of situations where supervisors failed to recognize when a pattern of transactions rendered the series of recommendations unsuitable. FINRA also noted that some firms did not adequately train supervisors how to use exception reports to identify red flags indicative of excessive trading. In other cases, some firms did not appropriately respond to and address red flags indicating excessive trading identified through their exception reports.[5]

- **Unsuitable Options Strategy Recommendations –** FINRA identified registered representatives recommending complex options strategies to customers who did not have the sophistication to understand the features of an option or the associated strategy, or without adequately considering the customers' individual financial situations and needs, as well as other investment profile factors. Further, some firms did not implement trade limits and controls to identify and prevent options trading that exceeded customer pre-approved investment levels.

Additional Resources

- 2017 Report – Product Suitability
- 2018 Report – Suitability for Retail Customers
- *Regulatory Notice 18-13* (FINRA Requests Comment on Proposed Amendments to the Quantitative Suitability Obligation Under FINRA Rule 2111)
- Supervision Topic Page
- Suitability Topic Page
- Customer Information category of the Peer-2-Peer Compliance Library

Digital Communication

Regulatory Obligations

Exchange Act Rules 17a-3 and 17a-4, as well as FINRA Rule 3110(b)(4) (Review of Correspondence and Internal Communications) and FINRA Rule Series 4510 (Books and Records Requirements) require a firm to, among other things, create and preserve, in an easily accessible place, originals of all communications received and sent relating to its "business as such." If a firm permits its associated persons to use a particular application—for example, an app-based messaging service or a collaboration platform—the firm must preserve records of business-related communications and supervise the activities and communications of those persons on the application. Firms remain responsible for conducting due diligence to comply with the securities laws and FINRA rules and follow up on red flags of potentially violative activity and may, in some cases, use services provided by the relevant digital channel or third-party vendors.

Noteworthy Examination Findings

FINRA has noted that some firms encountered challenges complying with supervision and recordkeeping requirements for various digital communications tools, technologies and services (collectively, "digital channels").

- **Use of Prohibited Digital Channels –** In some instances, firms prohibited the use of texting, messaging, social media or collaboration applications (*e.g.*, WhatsApp, WeChat, Facebook, Slack or HipChat) for business-related communication with customers, but did not maintain a process to reasonably identify and respond to red flags that registered representatives were using impermissible personal digital channel communications in connection with firm business. Red flags could be detected through, for example, customer complaints, representatives' email, outside business activity reviews or advertising reviews.
- **Prohibited Electronic Sales Seminars –** Some registered representatives conducted "electronic sales seminars" in a chatroom or on digital channels that were not permitted by their firms and were outside of supervision or recordkeeping programs.

Effective Practices

Firms implemented a number of effective practices to manage registered representatives' use of digital channels.

- **Establishing Comprehensive Governance –** Some firms maintained governance processes to manage firm decisions and develop compliance processes for each new digital channel, as well as new features of existing channels. Such firms worked closely with their marketing, compliance and information technology departments, as well as their third-party vendors, to monitor the rapidly evolving array of communication methods available to their associated persons and customers.
- **Defining and Controlling Permissible Digital Channels –** Firms with holistic supervision and record retention programs and policies clearly defined permissible (as well as prohibited) digital channels; blocked prohibited digital channels (or prohibited features of permitted channels); restricted the use of messaging and collaboration apps that limit the firm's ability to comply with its recordkeeping requirements (such as apps with end-to-end encryption or self-destructing messages); established how permitted communications will be stored in a compliant manner; and implemented supervisory review procedures for communication and recordkeeping that are appropriate for the firm's business model and tailored to each digital channel.

- **Managing Video Content –** Some firms implemented WSPs to manage the lifecycle of video content, which could include, for example, live-streamed public appearances, scripted commercials or video blogs.
- **Training –** Some firms implemented mandatory training programs prior to providing registered representatives access to firm-approved digital channels. The training clarified the firms' expectations for business and personal digital communications, and assisted personnel with using all permitted features of each channel in a compliant manner.
- **Disciplining Misuse of Digital Communications –** Some firms temporarily suspended or permanently blocked from certain digital channels those registered representatives who did not comply with the firm's digital channel policies and required additional digital communications training.

Additional Resources

- *Regulatory Notice* 19-31 (Disclosure Innovations in Advertising and Other Communications with the Public)
- *Regulatory Notice* 17-18 (Guidance on Social Networking Websites and Business Communications)
- Broker-Dealer Books and Records: New and Amended Recordkeeping Requirements Checklist
- Social Media Topic Page
- Books and Records Topic Page

Anti-Money Laundering (AML)

Regulatory Obligations

The Bank Secrecy Act (BSA) requires firms to monitor for, detect and report suspicious activity to the U.S. Treasury's Financial Crimes Enforcement Network (FinCEN). Further, FINRA Rule 3310 (Anti-Money Laundering Compliance Program) requires that members develop and implement a written AML program reasonably designed to comply with the requirements of the BSA and regulations promulgated thereunder. FINRA also notes that FinCEN's CDD rule requires that firms identify beneficial owners of legal entity customers, understand the nature and purpose of customer accounts, conduct ongoing monitoring of customer accounts to identify and report suspicious transactions, and—on a risk basis—update customer information.[6]

Noteworthy Examination Findings

FINRA identified the following issues relating to firms' AML programs, including challenges with transaction monitoring systems.

- **Inadequate AML Transaction Monitoring –** FINRA noted deficiencies in the design and implementation of systems and processes to detect and report suspicious activity:
  - Some firms did not tailor their transaction monitoring to address the risk(s) relating to the firms' business (for example, some firms did not adjust their AML programs for new sources of revenue or higher-risk customers with increased levels of activity, and other firms relied on FINRA's AML resources without tailoring them to the firms' business);[7]
  - Deficient transaction monitoring for suspicious trading and possible related money-laundering activity, which may have been due to an ongoing misconception that securities trading does not need to be monitored for suspicious activity reporting purposes, or inadequate delegation of duties to a group outside of the AML department (*e.g.*, the securities trading desk). As a result, some firms failed to detect red flags such as market dominance, prearranged trading or instances where groups of seemingly unrelated accounts were working in concert to manipulate stock prices; and
  - Transaction monitoring processes that were not reasonably designed to identify and investigate red flags associated with third-party wire transfers, where such red flags might include transfer requests that are out of the ordinary for the customer or appear designed to deter verification of the transfer instructions.
- **Overreliance on Clearing Firms –** FINRA found that some introducing firms continued to rely primarily or entirely on their clearing firm for transaction monitoring and suspicious activity reporting. While clearing firm inquiries about certain customers or activities can be triggers for further review by introducing firms, introducing firms are required to monitor for suspicious activity attempted or conducted through the firm.[8]

Additional Resources

- *Regulatory Notice* 19-18 (Guidance Regarding Suspicious Activity Monitoring and Reporting Obligations)
- 2017 Report – Anti-Money Laundering (AML) Compliance Program
- 2018 Report – Anti-Money Laundering
- Anti-Money Laundering (AML) Template for Small Firms
- Frequently Asked Questions (FAQ) Regarding Anti-Money Laundering (AML)
- Anti-Money Laundering (AML) Topic Page

Uniform Transfers to Minors Act (UTMA) and Uniform Grants to Minors Act (UGMA) Accounts

Regulatory Obligations

FINRA Rule 2090 (Know Your Customer) requires member firms and their associated persons to use reasonable diligence to determine the "essential facts" about every customer and "the authority of each person acting on behalf of such customer." *Regulatory Notice 11-02* (SEC Approves Consolidated FINRA Rules Governing Know-Your-Customer and Suitability Obligations) advised that firms verify the essential facts about a customer "at intervals reasonably calculated to prevent and detect any mishandling of a customer's account that might result from the customer's change in circumstances."

Noteworthy Examination Findings

Generally, when UTMA or UGMA accounts (UTMA/UGMA Accounts) are established, the beneficiary (a minor) becomes the owner of the property at the time of the gift; however, the custodian manages and invests the property on the beneficiary's behalf until the beneficiary reaches the age of majority, at which point the custodian is required to transfer the custodial property to the beneficiary.

FINRA noted that some firms did not establish, maintain or enforce a supervisory system reasonably designed to achieve compliance with their continuing obligation to know the essential facts of their UTMA/UGMA Account customers. Specifically, the circumstances concerning the authority of a person acting on behalf of a customer will change in UTMA/UGMA Accounts when the account beneficiary reaches the age of majority.

FINRA found that many firms were aware of the need to transfer responsibility for the account at a future date because they had policies and procedures addressing this topic, such as noting the date of majority when setting up the account. However, even though they were aware of the need to transfer the account at a future date, some firms did not take any steps to track or monitor when beneficiaries would reach the age of majority, while other firms had procedures for their registered representatives to follow, but did not require any supervisory oversight. Further, in some instances, firms permitted custodians to effect transactions in, and withdraw, journal and transfer money from UTMA/UGMA Accounts months, or even years, after the beneficiaries reached the age of majority, and ignored red flags of such activity (*e.g.*, customer complaints relating to such transactions).

Effective Practices

Some firms implemented a number of effective practices for verifying the authority of custodians of UTMA/UGMA Accounts.

- **Age of Majority –** Some firms maintained supervisory systems and used automated tools to track when each UTMA/UGMA Account beneficiary reached the age of majority.
- **Notification to Custodians –** Some firms issued letters or provided notifications to custodians to advise them that beneficiaries were approaching the age of majority and informed them about upcoming transfers of custodial property in their UTMA/UGMA Accounts, as well as any restrictions to the custodians' trading authority after the beneficiaries reached the age of majority.
- **Notification to Registered Representatives –** Some firms maintained systems to provide registered representatives with automated alerts when beneficiaries reached the age of majority and required them to communicate with the custodian about the transfer of custodial property.

Observations on Cybersecurity

While many firms have made significant improvements in their cybersecurity programs, cybersecurity attacks continue to increase in both number and level of sophistication. FINRA notes that such attacks often take advantage of and highlight weaknesses in a firm's cybersecurity program. The observations and effective practices we share below can help firms strengthen their cybersecurity programs and may support compliance with the SEC's Regulation S-P, which requires firms to have policies and procedures addressing the protection of customer records and information.[9]

We encourage firms to strengthen their cybersecurity programs by taking advantage of FINRA publications and other resources identified below. FINRA recognizes that there is no one-size-fits-all approach to cybersecurity, and reminds firms to evaluate each of the controls described in this report and other FINRA resources in the context of their business model and risk profile.

Highlighted below are effective practices some firms have implemented to strengthen their cybersecurity risk-management programs.

- **Branch Controls –** Firms maintained branch-level written cybersecurity policies to protect confidential data. In addition, they implemented procedures to verify that branch office controls were implemented and functioning adequately, either via automated monitoring tools or during in-person branch inspections.
- **Documented Policies on Vendor and Third-Party Management –** Firms using third-party vendors that provide critical firm services or handle sensitive client information adopted, implemented, and documented formal policies and procedures to manage the lifecycle of the firm's engagement with the vendor (*i.e.*, from onboarding, to ongoing monitoring, through off-boarding, including defining how vendors will dispose of sensitive client information).
- **Incident Response Planning –** Firms established and regularly tested written formal incident response plans that outlined procedures they would follow when responding to cybersecurity and information security incidents. Firms also developed procedures relating to incident response plans, which included a mechanism to appropriately identify, classify, prioritize, track and close cybersecurity-related incidents.
- **Data Protection Controls –** Firms encrypted all confidential data, including sensitive customer information and firm information, whether stored internally or at vendors' locations.
- **System Patching –** Firms adopted procedures to implement timely application of system security patches to critical firm resources (*e.g.*, servers, network routers, desktops, laptops and software systems) to protect sensitive client or firm information.
- **Access Controls –** Firms implemented or maintained policies and procedures to grant system and data access only when required (often referred to as "Policy of Least Privilege") and removed such access when it was no longer needed (such as when individuals departed or changed roles at the firm). In addition, firms tracked (and monitored the activities of) individuals granted administrator access to data or systems. Further, firms implemented multi-factor or two-factor authentication controls for registered representatives, employees, vendors and contractors accessing firm systems and data from outside the organization.
- **Management of Asset Inventory –** Some firms created and kept current an inventory of critical information technology assets—including hardware, software and data—in home and branch offices. These inventories also included legacy assets that vendors no longer supported, as well as corresponding cybersecurity controls to protect those assets.

- **Data Loss Prevention Controls –** Certain firms implemented data loss prevention controls to protect a broad range of sensitive customer information in addition to Social Security numbers, such as other account profile information (*e.g.*, account numbers, dates of birth, bank information and driver's license numbers).
- **Training and Awareness –** Firms provided robust cybersecurity training for registered representatives, personnel, third-party providers and consultants. This training addressed key topics relevant to individuals' roles and responsibilities (*e.g.*, training on the various types of phishing emails that might be directed towards registered representatives' associates or home office staff in the human resources or finance departments, or training on secure software development practices for developers). Some firms determined the appropriate frequency of such training based on the cybersecurity risk exposure associated with the firm, as well as individuals' roles and responsibilities.
- **Change Management Processes –** Some firms implemented change management procedures to document, review, prioritize, test, approve, and manage hardware and software changes in order to protect sensitive information and firm services.

Additional Resources

- Report on Cybersecurity Practices – 2015
- Report on Selected Cybersecurity Practices – 2018
- 2017 Report – Cybersecurity
- Small Firm Cybersecurity Checklist
- Core Cybersecurity Controls for Small Firms
- Customer Information Protection Topic Page
- Cybersecurity Topic Page
- Cybersecurity category of the Peer-2-Peer Compliance Library
- Non-FINRA Cybersecurity Resources

Business Continuity Plans (BCPs)

Regulatory Obligations

FINRA Rule 4370 (Business Continuity Plans and Emergency Contact Information) requires firms to create and maintain a written BCP with procedures that are reasonably designed to enable firms to meet their obligations to customers, counterparties and other broker-dealers during an emergency or significant business disruption.[10] The rule also requires firms to review and update their BCPs, if necessary, in light of changes to firms' operations, structure, business or location. Further, although most introducing firms rely, to some extent, on their clearing firms to allow customers to access their accounts and enter transactions, they are responsible for compliance with the BCP rule.

Noteworthy Examination Findings

FINRA found some firms encountering challenges where their BCPs did not reflect certain market conditions, business models or other circumstances.

- **Incomplete Mission-Critical Systems –** Some firms' BCPs did not identify all of their mission-critical systems. Omitted systems included those used for order management for trading desks, or vendor systems that processed and managed financing transactions, such as securities lending and repurchase agreements.
- **Insufficient Capacity –** Some larger firms did not have sufficient capacity to handle substantially increased call volumes and online activity during a business disruption, which affected customers' ability to access their accounts.
- **No Updates for Operational Changes –** Some firms did not update their BCPs after significant operational changes, such as outsourcing critical operational functions, relocating data centers or replacing other key systems, including trading desk order management systems or other systems that are critical to firms' business lines.
- **Outdated Contact Information –** Some firms' BCPs contained outdated emergency contact information and did not identify how customers could access their funds and securities during a business disruption.
- **Local Document Storage –** Some firms allowed employees to maintain critical working documents on their computers' local drives rather than requiring that they be stored on the firms' network. Firms should review their controls to test whether these files would be secure and readily accessible.
- **No Registered Principal Registrations –** Some senior management personnel, who were responsible for performing the annual BCP review, did not maintain the required registered principal registration.[11]

Effective Practices

Firms implement a number of effective practices to fulfill their obligations under the rule, especially those relating to testing of their BCP plans.

- **Engaging in Annual Testing –** Firms tested their BCPs as part of their annual review to confirm that the BCP was updated, and to evaluate its effectiveness, especially with respect to the functioning of mission-critical systems and processes, availability of key personnel and access to physical contingency site location(s). As part of these tests, some firms assessed their remote access capabilities to such systems, as well as evaluated and documented their ability to failover from one server to another. Firms also included key vendors in their BCP tests and documented results from those tests.

- **Incorporating Test Results into Firm Training –** Firms found these tests can be a valuable tool, not only to identify weaknesses in their BCPs, but also to train staff on how to implement the program, should that become necessary.

Additional Resources

- *Regulatory Notice* 19-06 (FINRA Requests Comment on the Effectiveness and Efficiency of Its Rule on Business Continuity Plans and Emergency Contact Information)
- *Regulatory Notice* 19-15 (FINRA Publishes Consolidated Criteria to Designate Firms for Mandatory Participation in FINRA's Business Continuity/Disaster Recovery Testing)
- Business Continuity Plan FAQs
- Small Firm Business Continuity Plan Template
- Business Continuity Planning Topic Page

Fixed Income Mark-up Disclosure

Regulatory Obligations

FINRA's and the Municipal Securities Rulemaking Board's (MSRB) amendments to FINRA Rule 2232 (Customer Confirmations) and MSRB Rule G-15 require firms to provide additional transaction-related pricing information to retail customers for certain trades in corporate, agency and municipal debt securities (other than municipal fund securities).[12]

Noteworthy Examination Findings

FINRA identified many of the issues previously discussed in the Fixed Income Mark-up Disclosure section of the 2018 Report, as well as the following additional issues.

- **Excluding Charges from Mark-Up/Mark-Down Disclosure –** Some firms disclosed additional charges separately from disclosed mark-ups or mark-downs, even when such charges reflected firm compensation. Firm compensation should not be mischaracterized, for example, as miscellaneous or fixed transaction fees; it should instead be included in the reported price of the transaction and accounted for when calculating mark-ups and mark-downs, consistent with applicable rules and guidance.[13]
- **Unclear or Inaccurate Labels for Sales Credits or Concessions –** Some firms disclosed registered representatives' sales credits or concessions as separate line items on confirmations, in addition to the mark-up or mark-down, without clear and accurate labeling, creating confusion about the actual disclosed mark-up and therefore diminishing its utility.[14] Similarly, some firms inaccurately labeled only the sales credits or concessions portion as the total mark-up or mark-down.
- **Incorrect Prevailing Market Price (PMP) Determinations –** Some firms did not determine the PMP as set forth in FINRA Rule 2121.02(b) (Additional Mark-Up Policy for Transactions in Debt Securities, Except Municipal Securities) for their fixed income transactions. Some firms' PMP determinations did not presumptively rely on the dealer's contemporaneous cost or proceeds, as required by Rule 2121. Other firms decided that their cost or proceeds were no longer "contemporaneous" without sufficient evidence as required by Rule 2121.02(b)(4) and used other pricing information to determine the PMP.
- **Inaccurate Time of Execution –** Some firms disclosed times of execution on customer confirmations that did not match the times of execution disseminated by the Electronic Municipal Market Access system (EMMA) or Trade Reporting and Compliance Engine (TRACE).[15] The time of execution on confirmations must match the trade times disseminated by EMMA and TRACE to allow customers to identify their specific transactions, consistent with the intent of the disclosure requirement.

Additional Resources

- *Regulatory Notice 17-24* (FINRA Issues Guidance on the Enhanced Confirmation Disclosure Requirements in Rule 2232 for Corporate and Agency Securities)
- Report Center – FINRA's MSRB Markup/Markdown Analysis Report
- Report Center – FINRA's TRACE Markup/Markdown Analysis Report
- Fixed Income Confirmation Disclosure: Frequently Asked Questions (FAQ)
- Municipal Securities Topic Page
- Fixed Income Topic Page

Best Execution

Regulatory Obligations

FINRA Rule 5310 (Best Execution and Interpositioning) requires firms to conduct a "regular and rigorous" review of the execution quality of customer orders if the firm does not conduct an order-by-order review.[16] Where "regular and rigorous" reviews are used instead of order-by-order reviews, the reviews must be performed at a minimum on a quarterly basis and on a security-by-security, type-of-order basis (*e.g.*, limit order, market order and market on open order). If a firm identifies any material differences in execution quality among the markets that trade the securities under review, it must modify its routing arrangements or justify why it is not doing so.

Noteworthy Examination Findings

FINRA continued to identify issues with some firms' execution quality reviews, as well as conflicts of interest and related disclosures.

- **No Execution Quality Assessment of Competing Markets –** Some firms did not compare the quality of the execution of their existing order routing and execution arrangements against the quality of executions that the firm could have obtained from competing venues.
- **No Review of Certain Order Types –** In some instances, firms did not conduct adequate reviews on a type-of-order basis, including, for example, on market, marketable limit or non-marketable limit orders.
- **No Evaluation of Required Factors –** Some firms did not consider factors set forth in FINRA Rule 5310 (Best Execution and Interpositioning) when conducting their execution quality reviews, including, among other things, the speed of execution, price improvement opportunities and the likelihood of execution of limit orders.
- **Conflicts of Interest –** Some firms did not adequately consider and address potential conflicts of interest relating to their routing of orders to affiliated alternative trading systems (ATSs) or market centers that provide payment for order flow or other routing inducements. In addition, some firms continue to route significant portions of their order flow to such venues without conducting an adequate "regular and rigorous" review to support such routing decisions.
- **Inadequate SEC Rule 606 Disclosures –** Some firms did not provide adequate information in the material disclosures section of their order routing reports required by Rule 606 of Regulation NMS. For example, certain firms did not disclose, when required, the specific, material aspects of the non-directed order flow routed to their own trading desk, including that the firm stands to share in 100 percent of the profits generated by the firm's trading as principal with its customers' orders.[17] Other firms did not disclose material aspects of their relationships with each of the significant venues identified on their reports, including descriptions and terms of all arrangements for payment for order flow (including the amounts of payment for order flow on a per share or per order basis)[18] and profit-sharing relationships that may have influenced the firms' order routing decisions.

Additional Resources

- 2017 Report – Best Execution
- 2018 Report – Best Execution
- *Regulatory Notice 15-46* (Guidance on Best Execution Obligations in Equity, Options and Fixed Income Markets)
- Report Center, Equity Report Cards section – FINRA's Best Execution Outside-of-the-Inside Report Card

Direct Market Access Controls

Regulatory Obligations

Compliance with Exchange Act Rule 15c3-5 (Market Access Rule) requires firms that provide access to trading in securities on an exchange or ATS to incorporate appropriate controls to mitigate key risks. The Market Access Rule is particularly important with the continued increase in automated and high-speed trading.

Noteworthy Examination Findings

FINRA continued to find many of the same issues identified in the Market Access Controls sections of the 2017 and 2018 Reports, as well as additional challenges with certain other market access controls, especially those related to fixed income transactions.

- **Insufficient Controls and WSPs –** Some firms' risk management controls and WSPs did not include pre-trade order limits, pre-set capital thresholds and duplicative and erroneous order controls for accessing ATSs, especially for fixed income transactions.
- **Inadequate Financial Risk Management Controls –** In some instances, firms with market access, or those that provide it, did not establish appropriate capital thresholds for trading desks, aggregate daily limits, or credit limits on institutional customers and counterparties. In some instances, firms with market access, or those that provide it, did not have reasonably designed risk-management controls or WSPs to manage the financial, regulatory or other risks associated with this business activity. Firms should regularly assess the appropriateness of their capital thresholds and pre-set credit limits for each customer.
- **Inadequate Basis for CEO Certification –** Some firms did not maintain reasonably designed risk-management controls that could support the CEO's certification pursuant to the requirements of Exchange Act Rule 15c3-5(e)(2).
- **Inaccurate Intra-day (Ad Hoc) Adjustments –** FINRA identified weaknesses in some firms' processes for requesting, approving, reviewing and documenting ad hoc credit threshold increases. For example, institutional clients requested ad hoc (daily) adjustments to financial limits in anticipation of increased order activity related to events such as an index rebalancing or a public offering, but once the event concluded (typically the next trading day), firms did not return the limits to their original values. Some firms maintained a manual process for reverting limits to their original values or did not revert the elevated credit limits in a timely fashion, which exposed clients and firms to elevated levels of financial risk.
- **Ineffective Erroneous Trading Controls –** Some firms failed to implement adequate controls relating to duplicative and erroneous orders. For example, some firms set controls to prevent the routing of a market order based on impact (Average Daily Volume Control) at unreasonable levels, preventing such firms from blocking erroneous trades. These controls can be effective tools (particularly in thinly traded securities) when set at reasonably high levels, and firms should calibrate them to reflect, among other things, the characteristics of the relevant securities, the business of the firm, and market conditions.
- **Insufficient Post-Trade Controls and Surveillance –** Some firms that provide direct market access via multiple systems, including sponsored access arrangements, did not employ reasonable controls to confirm that those systems' records were aggregated and integrated in a timely manner. As a result, those firms were not able to successfully conduct holistic post-trade and supervisory reviews for, among other things, potential manipulative trading patterns.

Additional Resources

- *Regulatory Notice* 15-09 (Guidance on Effective Supervision and Control Practices for Firms Engaging in Algorithmic Trading Strategies)
- *Regulatory Notice* 16-21 (SEC Approves Rule to Require Registration of Associated Persons Involved in the Design, Development or Significant Modification of Algorithmic Trading Strategies)
- Algorithmic Trading Topic Page
- Market Access Topic Page

Short Sales

Regulatory Obligations

Regulation SHO Rules 200 to 204 require firms to address risks relating to market manipulation, market liquidity and investor confidence by regulating excessive and "naked" short sales so that purchasers of securities from short sellers receive their securities positions in a timely manner. Regulation SHO requires firms to appropriately mark their securities orders; confirm that they have deliverable securities to complete short sale transactions; and have a process to close-out fails to deliver within the required timeframes.

Noteworthy Examination Findings

In addition to the findings FINRA shared in the Regulation SHO section of the 2017 Report, we found some firms were not able to satisfy the Continuous Net Settlement (CNS) System fail-to-deliver close-out requirements pursuant to Rule 204 because they did not implement a sufficient process to age fails, resulting in fails not being closed out timely. In other instances, firms did not accurately allocate CNS fails to correspondents. For example, some firms faced challenges relating to both inaccurate calculation of pre-fail credits prior to allocating fails to the correspondent, and used inconsistent methods when allocating fails to the correspondents where the share quantities exceeded the CNS fails.

In addition, firms may consider as an effective practice to periodically review their policies relating to rates charged for borrowing, sourcing or locating securities in connection with short sales, including monitoring the aging of short positions and determining whether the rates assigned at the onset of those positions are still appropriate.

Observations on Liquidity and Credit Risk Management

Effective liquidity and credit risk management controls are critical elements in a broker-dealer's risk management framework, and should be documented in a firm's books and records.[19] FINRA routinely reviews firms' practices in these areas, and in *Regulatory Notice* 15-33 (Guidance on Liquidity Risk Management Practices) shared observations on liquidity management practices.

FINRA shares the following practices that some firms used to strengthen their liquidity management programs.

- **Liquidity Contingency Plans –** Small clearing and introducing firms developed contingency plans for operating in a stressed environment and outlined specific steps to address certain stress conditions. Further, firms' contingency plans identified the firm staff responsible for enacting the plan, the process for accessing liquidity during a stress event or standards to determine how liquidity funding would be used.
- **Liquidity Risk Management Updates –** Firms updated their liquidity risk management practices to take into account their current business activities.
- **Stress Tests –** Firms conducted stress tests in a manner and frequency that was appropriate for their business model. In addition, such stress tests evaluated the potential impact of off-balance sheet items on liquidity. Some firms that relied on a shared funding source with affiliated entities for their liquidity stress test and their shared Master Credit Agreement confirmed that source would be ring-fenced for them during a stress event.
- **Credit Risk Management –** Firms maintained a robust internal control framework to capture, measure, aggregate, manage and report credit risk.[20] In particular, firms evaluated their risk management and control processes to review whether they were accurately capturing their exposure to credit risk; maintained approval and documentation processes for increases or other changes to assigned credit limits; and monitored exposure to their affiliated counterparties.

Additional Resources

- 2018 Report – Liquidity
- *Regulatory Notice* 10-57 (Funding and Liquidity Risk Management Practices)
- Funding and Liquidity Topic Page

Segregation of Client Assets

Regulatory Obligations

Exchange Act Rule 15c3-3 (Customer Protection Rule) requires firms that maintain custody of customer securities and safeguard customer cash to segregate these assets from the firm's proprietary business.

Noteworthy Examination Findings

FINRA has continued to identify many of the same concerns noted in the Segregation of Client Assets section of the 2018 Report, including challenges with check-forwarding and possession or control.

- **Omitted or Inaccurate Blotter Information –** Some firms' blotters lacked sufficient information to demonstrate that checks were forwarded in a timely manner or contained inaccurate information with respect to the status of checks.
- **Inadequate Possession or Control Processes –** FINRA noted the following deficiencies:
  - Failure to obtain documentation (no lien letters) from custodians and issuers to show that all securities in a good control location were free of liens that could be exercised by a third party on the firm;
  - Inability to identify deficits in fully paid and excess margin securities when certain firms did not correctly age the deficits due to errors in their formulas;
  - Failure to confirm that fully paid securities were correctly segregated at custodian banks (FINRA notes that firms should consider verifying whether they have sufficient securities positions that exceed possession or control requirements prior to transferring such excess securities from a custodial account); and
  - Failure to combine balances and positions in related customer securities accounts and accounts with the same Taxpayer Identification Numbers in order to determine the extent to which the market value of securities carried for the customer's account exceeded 140 percent of the customer's debit balance.
- **Inaccurate Reserve Formula Calculations –** Some firms did not exclude concentrated margin debit balances[21] because they did not have a process to identify accounts under common control or related customer accounts.
- **Coding Errors –** FINRA noted joint customer and firm officer accounts miscoded as "non-customer" rather than "customer." Some firms also coded foreign bank accounts as "PAB" without obtaining a written agreement acknowledging that the accounts are proprietary transactions of the foreign bank.[22]

Additional Resources

- Interpretations of Financial and Operational Rules
- Customer Protection – Reserves and Custody of Securities (SEA Rule 15c3-3)

Net Capital Calculations

Regulatory Obligations

Exchange Act Rule 15c3-1 (Net Capital Rule) requires firms to maintain net capital at specific levels to protect customers and creditors from monetary losses that can occur when firms fail.

Noteworthy Examination Findings

FINRA has continued to identify some of the same concerns noted in the Net Capital and Credit Risk Assessments section of the 2017 Report and Accuracy of Net Capital Calculations section of the 2018 Report, as well as the following additional issues.

- **Incorrect Inventory Haircuts –** Some firms did not apply correct haircut charges when computing net capital because they did not adequately assess and monitor the creditworthiness of fixed income securities, such as corporate debt and collateralized mortgage obligations (CMOs), to determine whether these products have a "minimal amount of creditworthiness" pursuant to Exchange Act Rule 15c3-1(c)(2)(vi)(I).[23]
- **Incorrect Capital Charges for Underwriting Commitments –** Some firms did not maintain an adequate process to assess moment-to-moment and open contractual commitment capital charges on underwriting commitments and did not understand their role as it pertained to the underwriting (*i.e.*, best efforts or firm commitment).[24]
- **Inaccurate Classification of Receivables, Liabilities and Revenue –** In some instances, firms inaccurately classified receivables, liabilities and revenues, which resulted in inaccurate reporting of a firm's financial position and, in some instances, a capital deficiency. In addition, upon settlement of a customer claim, some firms understated their liability by recognizing the monies due to the customer based on a payment schedule instead of recognizing the full amount owed at the time of settlement.
- **Recognition of Insurance Claims –** Some firms did not recognize on their books and records receivables due from insurance carriers and the corresponding liabilities owed to customers. Other firms did not obtain an opinion of counsel with respect to claims within seven business days, as required under Exchange Act Rule 15c3-1(c)(2)(iv)(D), thereby resulting in the receivables not being allowable for purposes of net capital, and the firm being required to take the full charge for the customer claim.
- **Inadequate Documentation of Methodology for Expense-Sharing Agreements –** Some firms did not maintain sufficient documentation to substantiate their methodology for allocating specific broker-dealer costs to the firm or an affiliate. Some firms were not accurately accruing expenses—such as technology fees, marketing charges, retirement account administrative fees and employees' compensation—on their books and records. Further, some firms incorrectly netted intercompany accounts with different affiliated entities,[25] resulting in books and records that did not accurately reflect the firms' operating performance and financial condition.

Additional Resources

- Interpretations of Financial and Operational Rules
- *Notice to Members* 03-63 (SEC Issues Guidance on the Recording of Expenses and Liabilities by Broker/Dealers)

ENDNOTES

1. *See Regulatory Notice 10-19* (FINRA Reminds Firms of Responsibilities When Providing Customers with Consolidated Financial Account Reports).

2. On June 5, 2019, the SEC voted to adopt a package of rulemakings and guidance, including Regulation Best Interest (Reg BI). This section is intended to provide firms with findings solely related to compliance with existing FINRA suitability and related supervisory obligations and does not address Reg BI. For additional information, please see FINRA's Topic Page on SEC Regulation Best Interest (Reg BI).

3. In addition to the items discussed in this document, FINRA reminds firms to consider the findings FINRA shared previously regarding overconcentration in illiquid securities, reasonable due diligence for private placements and certain variable annuity exchanges.

4. *See* FINRA Rule 2330(d) (Members' Responsibilities Regarding Deferred Variable Annuities).

5. FINRA continued to note many of the challenges we discussed in the Abuse of Authority section of the 2018 Report, including registered representatives engaging in discretionary trading without written authorization.

6. *See Regulatory Notices 17-40* (FINRA Provides Guidance to Firms Regarding Ant-Money Laundering Program Requirements Under FINRA Rule 3310 Following Adopting of FinCEN's Final Rule to Enhance Customer Due Diligence Requirements For Financial Institutions) and *18-19* (FINRA Amends Rule 3310 to Conform to FinCEN's Final Rule on Customer Due Diligence Requirements for Financial Institutions) for additional information.

7. *See Regulatory Notice 19-18* (FINRA Provides Guidance to Firms Regarding Suspicious Activity Monitoring and Reporting Obligations) for a list of potential red flags that firms should consider when designing an effective AML compliance program that is tailored to their business.

8. *See* Frequently Asked Questions (FAQ) Regarding Anti-Money Laundering (AML), Question No. 22.

9. This obligation includes protection against any anticipated threats or hazards to the security or integrity of customer records and information, as well as unauthorized access to or use of such records or information. Also, the rule requires firms to provide initial and annual privacy notices to customers describing information sharing policies and informing customers of their rights.

10. Pursuant to *Regulatory Notice 19-06* (FINRA Requests Comment on the Effectiveness and Efficiency of Its Rule on Business Continuity Plans and Emergency Contact Information), FINRA is conducting a retrospective review of Rule 4370. This section is intended to provide firms with findings solely relating to compliance with existing Rule 4370 and does not address the outcome of that review or any potential revisions to the rule.

11. *See* FINRA Rule 4370(d).

12. Specifically, the amendments require firms to disclose the mark-up or mark-down for principal trades with retail customers that a firm offsets on the same day with other principal trades in the same security. Disclosed mark-ups and mark-downs must be expressed as both a total dollar amount for the transaction and a percentage of PMP. In addition, for all retail customer trades in corporate, agency and municipal debt securities (other than municipal fund securities), firms must disclose on the confirmation the time of execution and a security-specific link to the FINRA or MSRB website where additional information about the transaction is available, along with a brief description of the information available on the website.

13. *See, e.g.*, Frequently Asked Questions (FAQ) About the Trade Reporting and Compliance Engine (TRACE) FAQ *3.1.33* (stating that prices reported to TRACE should be inclusive of mark-ups and mark-downs).

14. *See* FINRA Fixed Income Confirmation Disclosure: Frequently Asked Questions (FAQ), FAQ 2.3 and MSRB Confirmation Disclosure and Prevailing Market Price Guidance: Frequently Asked Questions, FAQ 2.3.

15. *See* FINRA Fixed Income Confirmation Disclosure: Frequently Asked Questions (FAQ), FAQ 4.2; MSRB Confirmation Disclosure and Prevailing Market Price: Frequently Asked Questions, FAQ 4.2.

16. *See also Regulatory Notice 15-46* (Guidance on Best Execution Obligations in Equity, Options and Fixed Income Markets).

17. *See* U.S. Securities and Exchange Commission, Division of Market Regulation: Staff Legal Bulletin No. 13A Frequently Asked Question about Rule 11Ac1-6, Question 14: Disclosing Internalized Order Flow.

18. *See* U.S. Securities and Exchange Commission, Division of Market Regulation: Staff Legal Bulletin No. 13A Frequently Asked Question about Rule 11Ac1-6, Question 13: Disclosing Payment for Order Flow.

19. *See* Exchange Act Rule 17a-3(a)(23).

20. *See* Financial Responsibility Rules for Broker-Dealers, Exchange Act Release No. 70072 (July 30, 2013), 78 Fed. Reg. 51824 (Aug. 21, 2013), at 51848; *see also* FINRA's Resource Page for the SEC's July 2013 Financial Responsibility Rule Amendments.

21. *See* the SEC's Note E(5) to Exhibit A of SEA Rule 15c3-3 and the associated interpretation, Determination of the Includible Amount of a Customer's Concentrated Margin Debit Balance in the Reserve Formula, Exchange Act Rule 15c3-3, Exhibit A - Note E(5)/01, in the Interpretations of Financial and Operational Rules.

22. Regarding foreign banks, *see* Foreign Banks - Customer and Non-Customer Classification, Exchange Act Rule 15c3-3(a)(1)/032, in the Interpretations of Financial and Operational Rules.

23. These requirements were adopted as part of the SEC's 2013 credit ratings amendments. *See* Exchange Act Release No. 71194 (Dec. 27, 2013), 79 Fed. Reg. 1522 (Jan. 8, 2014).

24. *See* Exchange Act Rule 15c3-1(c)(2)(viii); *see also* Moment to Moment Net Capital, Exchange Act Rule 15c3-1(a)(1)/001, in the Interpretations of Financial and Operational Rules.

25. *See* Netting of Intercompany Receivables and Payables with Affiliates, Exchange Act Rule 15c3-1(c)(2)(iv)(C)/073 in the Interpretations of Financial and Operational Rules.

2020 Risk Monitoring and Examination Priorities Letter

January 2020

Topics

Introduction

This 2020 Risk Monitoring and Examination Priorities Letter describes the areas of focus for FINRA's risk monitoring, surveillance and examination programs in the coming year. Continuing the approach we started in 2019, the letter addresses new and emerging areas in greater depth, and ongoing priorities with shorter summaries. (Information on the latter is available in previous annual priorities letters.)

In addition, we recognize the significant efforts that firms make to comply with federal securities laws and regulations, as well as FINRA rules. To support firms in this important endeavor, the letter includes a list of practical considerations and questions for each of the highlighted topics, which firms may use to evaluate the state of their compliance, supervisory and risk management programs. These considerations are not all-inclusive, may not apply to all firms, and should not be read to create obligations beyond those in federal securities laws and regulations and FINRA rules.

We also encourage firms to avail themselves of the resources offered in the endnotes and the appendix to refresh their understanding of their fundamental compliance obligations.

Sales Practice and Supervision

Introduction

FINRA will continue to evaluate firms' compliance with sales practice obligations to their customers—as well as the supervision of those practices—in areas that we have discussed frequently in previous annual priorities letters, exam findings reports (Reports) and other FINRA publications. These areas of focus include complex products,[1] variable annuities,[2] private placements,[3] fixed income mark-up/mark-down disclosures,[4] representatives acting in certain positions of trust or authority[5] and senior investors.[6] In addition to these topics, FINRA will review firms' compliance with obligations related to several new or emerging areas discussed below.

Regulation Best Interest (Reg BI) and Form CRS

On June 5, 2019, the U.S. Securities and Exchange Commission (SEC) adopted Reg BI, which establishes a "best interest" standard of conduct for broker-dealers and associated persons when they make a recommendation to a retail customer

of any securities transaction or investment strategy involving securities, including recommendations of types of accounts. As part of the rulemaking package, the SEC also adopted new rules and forms to require broker-dealers to provide a brief relationship summary—Form CRS—to retail investors. Firms must comply with Reg BI and Form CRS by June 30, 2020.

In the first part of the year, FINRA will review firms' preparedness for Reg BI to gain an understanding of implementation challenges they face and, after the compliance date, will examine firms' compliance with Reg BI, Form CRS and related SEC guidance and interpretations.[7] FINRA staff expects to work with SEC staff to ensure consistency in examining broker-dealers and their associated persons for compliance with Reg BI and Form CRS.

FINRA may take the following factors, among others,[8] into consideration when reviewing for compliance with Reg BI after June 30, 2020:

- Does your firm have procedures and training in place to assess recommendations using a best interest standard?
- Do your firm and your associated persons apply a best interest standard to recommendations of types of accounts?
- If your firm and your associated persons agree to provide account monitoring, do you apply the best interest standard to both explicit and implicit hold recommendations?
- Do your firm and your associated persons consider the express new elements of care, skill and costs when making recommendations to retail customers?
- Do your firm and your associated persons consider reasonably available alternatives to the recommendation?
- Do your firm and your registered representatives guard against excessive trading, irrespective of whether the broker-dealer or associated person "controls" the account?
- Does your firm have policies and procedures to provide the disclosures required by Reg BI?
- Does your firm have policies and procedures to identify and address conflicts of interest?
- Does your firm have policies and procedures in place regarding the filing, updating and delivery of Form CRS?

Communications with the Public

FINRA will continue to assess firms' compliance with obligations relating to FINRA Rule 2210 (Communications with the Public), as well as related supervisory and recordkeeping requirements set forth in FINRA Rule 3110(b)(4) (Supervision), FINRA Rule Series 4510 (Books and Records Requirements) and Securities Exchange Act of 1934 (Exchange Act) Rules 17a-3 and 17a-4 (Books and Records Requirements).

In addition to ongoing reviews for compliance with these core obligations, FINRA will also focus on the following two areas:

- **Private Placement Retail Communications** – FINRA will review how firms review, approve, supervise and distribute retail communications regarding private placement securities via online distribution platforms[9], as well as traditional channels.

  When reviewing a firm's communication materials, FINRA may consider the following:

  - Do they omit material information necessary to make the communications fair and not misleading by failing to, for example, explain that private placements may involve a high degree of risk, are not liquid and that investors may lose money?
  - Do they balance promotional content with the key risks specific to the issuer offered?
  - Do they contain false, misleading or promissory statements or claims, such as the likelihood of a future public offering of the issuer, claims about the future success of the issuer's new or untried business model, or inaccurate or misleading assertions concerning the regulation or relative risk of the offering?
  - When forecasting issuer metrics, such as revenue, are the presentations reasonable and accompanied by clear explanations of both the assumptions used to create the forecasts and the risks that might impede achievement of such forecasts?
  - Do they contain predictions or projections of investment performance to investors that are generally prohibited by FINRA Rule 2210(d)(1)(F) (Communications with the Public), unless they meet the stated criteria in the rule?

- **Communications via Digital Channels** – Firms', registered representatives' and customers' use of an increasingly broad array of digital communication channels (*e.g.*, texting, messaging, social media or collaboration applications) may pose challenges to firms' ability to comply with obligations related to the review and retention of such communications.

  FINRA may consider the following, among other factors, when reviewing firms' use and supervision of digital channels:

  - Does your firm have a process in place to evaluate new tools available to your registered representatives to determine whether there are digital communication channels that should be captured, included in your firm's routine electronic communications supervisory reviews and stored in accordance with books and records requirements?
  - Is your firm periodically testing its systems to ensure these communications are being captured for review and retention?
  - Do your firm's supervisors know the "red flags" they should keep in mind during their routine supervisory reviews and which indicate a registered representative may be communicating through unapproved communication channels? Are your firm's supervisors following up on such red flags, which include, but are not limited to:
    - email chains that include non-approved email addresses for registered representatives;

- references in emails to communications with a registered representative that occurred outside approved firm channels; or
- customer complaints mentioning such communications?[10]

Cash Management and Bank Sweep Programs

As commission practices change, cash management services that sweep investor cash into firms' affiliated or partner banks or money market funds (Bank Sweep Programs) have taken on a greater significance. Firms' Bank Sweep Programs may offer retail investors a variety of additional services, such as check writing, debit cards and ATM withdrawals.

While these Bank Sweep Programs may offer useful features to customers—and in some but not all cases, offer higher-than-average interest rates—they have also raised several concerns about firms' compliance with a range of FINRA and SEC rules. FINRA will evaluate these firms' compliance with, for example, FINRA Rules 1017 (Application for Approval of Change in Ownership, Control, or Business Operations),[11] 2010 (Standards of Commercial Honor and Principles of Trade), 2210 (Communications with the Public), Exchange Act Rule 15c3-1 (Net Capital Rule) and Exchange Act Rule 15c3-5 (Customer Protection Rule).

FINRA may take the following factors, among others, into consideration when reviewing your firm's Bank Sweep Programs:

- Does your firm clearly communicate the nature of the sweep arrangement?
- Does your firm clearly communicate the alternatives for cash management available to customers, the terms provided by the Bank Sweep Program and any alternatives?
- Has your firm incorrectly implied that a brokerage account is similar to or the same as a "checking and savings account" at a bank?
- Has your firm incorrectly implied that the brokerage accounts themselves are bank deposit accounts insured by the Federal Deposit Insurance Corporation (FDIC)?
- Do your firm's customer statements clearly disclose that the Bank Sweep Program deposits are obligations of the destination bank, and not cash balances held by your firm?
- Does your firm have a documented process to perform reconciliations of customer balances held at each destination bank in the Bank Sweep Program?
- Does your firm include in the Bank Sweep Program customer balances not yet swept into a destination bank as a customer credit in the reserve formula computation?
- Has your firm omitted or misrepresented material information concerning the:
  - amount of FDIC insurance coverage for the deposits;
  - nature and structure of the accounts;
  - relationship of the brokerage accounts to any partner banks in the Bank Sweep Program;
  - amount of time it may take for customer funds to reach the bank accounts;
  - nature and terms of the arrangements; or
  - risks of participating in such programs?

Sales of Initial Public Offering (IPO) Shares

As the IPO market has grown and received additional attention over the past year, FINRA is focusing its attention on firms' obligations under FINRA Rules 5130 (Restrictions on the Purchase and Sale of Initial Equity Public Offerings) and 5131 (New Issue Allocations and Distributions).[12]

FINRA may consider the following factors, among others, when reviewing your firm's IPO practices:

- Does your firm have procedures in place to detect and address potential instances of flipping?
- When acting as book-running lead manager, does your firm provide reports of aggregate retail demand to issuers' pricing committees? How does your firm calculate this aggregate demand?
- How does your firm develop and implement its IPO allocation methodologies?
- What controls does your firm have to prevent allocations to restricted persons?
- What controls does your firm have to detect and address potential instances of "spinning"?
- How does your firm obtain, record and verify customer information for individuals receiving IPO allocations?

Trading Authorization

FINRA will assess whether firms maintain reasonably designed supervisory systems relating to trading authorization, discretionary accounts and key transaction descriptors, such as solicitation indicators. FINRA will review whether firms have reasonably designed supervisory systems to detect and address registered representatives exercising discretion without written authorization from the client, as required under FINRA Rule 3260 (Discretionary Accounts).[13]

FINRA may take the following factors, among others, into consideration when reviewing your firm's procedures and controls:

- How does your firm surveil for potential red flags of registered representatives exercising discretion without written authorization?
- Do your firm's supervisors know the types of red flags that may indicate that registered representatives are exercising discretion without written authorization (*e.g.,* trading in unrelated accounts in the same security in a certain time period, large numbers of trade reneges in the same security in a certain time period)?
- If a red flag is identified, what follow-up steps do your supervisors take to investigate them further (*e.g.,* phone log, email or other digital communication reviews to look for evidence of communications between the customer and the registered representative; non-complaining customer reach-outs)?
- How does your firm identify instances where registered representatives may be marking trades as unsolicited even though they are, in fact, solicited?

Market Integrity

Introduction

In addition to the areas of focus described in greater detail below, we will continue to review firms' compliance with the ongoing obligations discussed in prior years' letters, such as market manipulation, Trade Reporting and Compliance Engine (TRACE) reporting,[14] short sales[15] and short tenders.[16]

Further, FINRA reminds certain firms that they will be required to begin reporting to the Consolidated Audit Trail (CAT) in April 2020. We will continue to work with firms to answer their questions as they prepare for reporting. Once reporting begins, we will initiate our surveillance and investigative program to review firms' compliance with CAT reporting requirements.

We also remind firms to continue devoting necessary resources to ensure continually high levels of accuracy in their Order Audit Trail System (OATS) reporting. At this time, OATS remains a critical part of the audit trail data that FINRA uses to operate its cross-market equity surveillance program and meet its regulatory obligations.

Direct Market Access Controls

The continued growth in automated and high-speed trading increases potential risks to the financial condition of firms, the integrity of trading on the securities markets and the stability of the financial system. We will assess firms' compliance with Exchange Act Rule 15c3-5 (Market Access Rule),[17] focusing on issues relevant to firms' business activities and associated risks.

FINRA may take the following factors, among others, into consideration when reviewing your firm's direct market access controls:

- If your firm is highly automated, how does it manage and deploy technology changes for systems associated with market access, and what controls does it use, such as kill switches, to monitor and respond to aberrant behavior by trading algorithms or other impactful market wide events?
- How does your firm make adjustments to credit limit thresholds for institutional customers (whether temporary or permanent)?[18]
- Does your firm use any automated controls to timely revert *ad hoc* credit limit adjustments?
- If your firm uses third-party vendor tools to comply with its Market Access Rule obligations, does it review during vendor due diligence whether the vendor can meet the obligations of the rule, and how does your firm maintain direct and exclusive control of applicable thresholds?
- What type of training does your firm provide to individual traders regarding the steps and requirements for requesting *ad hoc* credit limit adjustments?

Best Execution

FINRA reaffirms the importance of firms' compliance with their best execution obligations.[19] FINRA will focus on whether firms use reasonable diligence to determine whether their customer order flow is directed to the best market given the size and types of orders, the terms and conditions of orders, and other factors as required by FINRA Rule 5310 (Best Execution and Interpositioning),[20] focusing on:

- **Routing Decisions** – FINRA will continue to review for potential conflicts of interest in order routing decisions, including the impact of the recent increase in zero-commission brokerage activity. FINRA may review, for example:
  - processes your firm implements to handle customer orders, particularly in light of remuneration received by the firm in the form of rebates or payment for order flow;
  - how your firm incorporates enhanced order routing information in its "regular and rigorous" review pursuant to FINRA Rule 5310 (Best Execution and Interpositioning); or
  - whether changing to the zero-commission model resulted in changes to your firm's routing practices, execution quality, regular and rigorous review policies, or the level of trading rebates or payment for order flow. FINRA may also assess disclosures and advertisements related to zero commissions.
- **Odd-Lot Handling** – FINRA has observed a significant increase in odd-lot activity, which has also become an increasing portion of U.S. equity trading volume. Odd lots in listed securities are currently not included in the National Best Bid or Offer (NBBO) distributed by the Securities Information Processors (SIPs), but are included in proprietary data feeds from individual exchanges. FINRA will be assessing whether firms are filling customer odd-lot orders at the NBBO disseminated by the SIPs and offsetting these trades with odd-lot executions at superior prices reflected in the exchanges' proprietary data feeds.
- **U.S. Treasury Securities** – FINRA will assess the reasonableness of firms' policies and procedures for best execution and fair pricing for U.S. Treasury securities. In conducting this assessment, FINRA may consider whether your firm takes into account differences in these securities' characteristics and liquidity, particularly if your firm includes them in more generally applicable fixed income policies and procedures.
- **Options** – FINRA has received complaints alleging large customer option orders received inferior execution prices. The complaints typically involve a number of small volume option executions at various prices (normally electronically), followed by a larger execution for the remainder of the order at inferior price levels for the customer. In response, FINRA initiated surveillance to identify this specific scenario, and we plan to expand our best execution surveillance to include additional scenarios to identify situations where customers may not be receiving best execution for their options orders.

Other considerations FINRA may take into account when reviewing your firm's best execution practices include:

- If your firm engages in fixed income and options trading, has it established targeted controls to perform its best execution obligations for these products?

- Does your firm perform its best execution obligations with respect to trading conducted in both regular and extended trading hours?
- Does your firm consider the risk of information leakage when assessing the execution quality of orders routed to a particular venue?

Disclosure of Order Routing Information

The amended Regulation National Market System (NMS) Rule 606 bolstered the requirements for broker-dealers to publish reports on their routing of held orders in NMS stocks and listed options.[21] The amended rule requires broker-dealers to provide new customer-specific reports for not held orders in NMS stocks. These disclosures serve an important role in enhancing the transparency of the U.S. securities markets with respect to broker-dealers' handling and routing practices for both institutional and retail customer orders.

FINRA may take the following into consideration, among other factors, when reviewing firms' compliance with amended Rule 606:

- Does your firm use the required layout and format and include all components of the detailed customer-specific not held order reports required by Rule 606(b)(3)?
- What policies and procedures does your firm have in place to address the accuracy and timeliness of published reports?
- If your firm claims an exemption from providing not held order reports required by Rule 606(b)(4) or (5), what policies and procedures does it have in place to determine if customers' order activity falls below the relevant reporting thresholds?
- Has your firm considered whether it should assess and analyze its use of third-party order routing and execution services (*e.g.,* algorithms and smart order routers) and determine how your firm's traders use these services?
- Has your firm considered how it will obtain the necessary data from downstream venues to prepare the new reports?

Vendor Display Rule

Capturing and reporting the current consolidated NBBO helps customers evaluate firms' routing decisions. Rule 603 of Regulation NMS (Vendor Display Rule) generally requires broker-dealers to provide a consolidated display of market data for NMS stocks for which they provide quotation information to customers. FINRA will evaluate the adequacy of firms' controls and supervisory systems to provide their customers with the current consolidated NBBO as required by the Vendor Display Rule.

FINRA may take the following factors, among others, into consideration when reviewing your firm's controls related to the Vendor Display Rule:

- Which firm systems or platforms provide quotation information to customers?
- How does your firm monitor whether the current quotation information is distributed to customers?
- Does your firm make the quotation information available to customers when they are placing their orders?
- Does your firm review the quotation information received from the SIP or vendors to determine whether that information is in compliance with all the requirements of Rule 603?

Financial Management

Introduction

In addition to our focus on the new areas noted below, FINRA will continue to evaluate firms' compliance programs relating to Exchange Act Rule 15c3-3 (Customer Protection Rule) and Exchange Act Rule 15c3-1 (Net Capital Rule), as well as firms' overall financial risk management programs.

Digital Assets

Digital assets raise novel and complex regulatory issues under federal securities laws and regulations,[22] as well as FINRA rules.[23] FINRA is receiving an increasing number of New Member Applications (NMAs) and Continuing Member Applications (CMAs) from firms[24] seeking to engage in business activities related to digital assets. For example, some firms are seeking to facilitate private offerings of digital asset securities, operate secondary trading platforms or facilitate trades of indirect investment products, such as private funds investing in cryptocurrencies.[25] Some firms' proposals also involve clearance and settlement of securities transactions related to digital assets, even when the firm does not plan to provide custody.[26]

FINRA continues to work closely with the SEC to understand firms' business plans and determine how securities laws apply to those plans. In July 2019, SEC and FINRA staff released a joint statement addressing certain non-custodial services, as well as challenges related to custody and critical Exchange Act Rule 15c3-3 obligations for digital assets.[27]

FINRA may take the following factors, among others, into consideration when reviewing your firm's digital asset activities:

- If your firm is considering engaging in digital asset activities, has it filed a CMA with FINRA?
- Does your firm provide a fair and balanced presentation in marketing materials and retail communications, including addressing risks presented by digital asset investments, and not misrepresenting the extent to which digital assets are regulated by FINRA or the federal securities laws or eligible for protections thereunder (such as Securities Investor Protection Corporation coverage)?
- Do your firm's communications misleadingly imply that digital asset services offered through an affiliated entity are offered through and under the supervision, clearance and custody of a registered broker-dealer?
- If your firm is engaging in digital asset transactions, what controls and procedures has it established to support facilitation of such transactions, including initial issuance or secondary market trading of digital assets?

Liquidity Management

FINRA will continue to review firms' liquidity management practices, as they are a critical control function and should be documented in a firm's books and records.[28] FINRA will focus on areas that we have addressed in *Regulatory Notice* *15-33* (Guidance on Liquidity Risk Management Practices), as well as those that may create challenges for clearing and carrying firms' contingency funding plans.

FINRA may take the following factors, among others, into consideration when reviewing your firm's liquidity management practices:

- Do your firm's liquidity management practices include steps to address specific stress conditions and identify firm staff responsible for addressing those conditions? Does your firm have a process for accessing liquidity during a stress event and determining how the funding would be used?
- Does your firm's contingency funding plan take into consideration the quality of collateral, term mismatches and potential counterparty loss of your financing desks (in particular, in repo and stock loan transactions)?
- If your firm is also a Fixed Income Clearing Corporation (FICC) member, how would it manage operational risks—for example, different credit limits and trading hours—that may arise if it needs to rapidly move large amounts of bi-lateral or tri-party U.S. Government or agency securities financing trades to the FICC repo platform?

Contractual Commitment Arising From Underwriting Activities

FINRA will review firms' compliance with their obligations under Exchange Act Rule 15c3-1(c)(2)(viii) when they engage in underwriting activities. FINRA may take the following into consideration when reviewing your firm's compliance with these obligations:

- Does your firm understand the nature of the underwriting (in particular, best efforts versus firm commitment underwriting) and maintain a list of all deals in which it is involved?
- Does your firm maintain evidence of the appropriate contractual commitment charges?
- What processes does your firm use to assess moment-to-moment and open contractual commitment capital charges when it engages in underwriting commitments?
- How do your firm's regulatory reporting groups track the appropriate net capital treatment of the underwritings in which your firm is involved?
- How is your firm documenting your compliance with the relevant requirements?

London Interbank Offered Rate (LIBOR) Transition

FINRA will engage with firms—outside the examination program—to understand how the industry is preparing for LIBOR's retirement at the end of 2021,[29] focusing on firms' exposure to LIBOR-linked financial products; steps firms are taking to plan for the transition away from LIBOR to alternative rates, such as the Secured Overnight Financing Rate (SOFR); and the impact of the LIBOR phase-out on customers.

Firm Operations

Introduction

In addition to the new areas of focus described below, FINRA will also assess firms' supervisory controls relating to Exchange Act Rule 10b-10 and FINRA Rule 2232 (Customer Confirmations) and firms' compliance with FINRA Rule 3310 (Anti-Money Laundering Compliance Program)[30].

Cybersecurity

As firms leverage technology for their business systems and infrastructure, as well as engaging with customers and business partners, cybersecurity has become an increasingly large operational risk. Firms should expect that FINRA will thoroughly assess whether their policies and procedures are reasonably designed to protect customer records and information consistent with Regulation S-P Rule 30. [31] FINRA recognizes that there is no one-size-fits-all approach to cybersecurity, but expects firms to implement controls appropriate to their business model and scale of operations.

Technology Governance

Firms' increasing reliance on technology for many aspects of their customer-facing activities, trading, operations, back-office and compliance programs creates a variety of potential benefits, but also exposes firms to technology-related compliance and other risks. In particular, problems in firms' change- and problem-management practices, for example, can expose firms to operational failures that may compromise firms' ability to comply with a range of rules and regulations, including FINRA Rules 4370 (Business Continuity Plans and Emergency Contact Information), 3110 (Supervision) and 4511 (General Requirements), as well as Exchange Act Rules 17a-3 and 17a-4.

FINRA may take the following into consideration, among other factors, when reviewing your firm's technology governance programs:

- If there have been material changes in your firm's business, what modifications, if any, has it made, or considered, to its BCP?
- During a BCP event, how will your firm maintain customers' access to their funds and securities, as well as manage back-office operations, to prevent delays or inaccuracies relating to settlement, reconciliation and reporting requirements?
- What controls does your firm implement to mitigate system capacity performance and integrity issues that may undermine its ability to conduct business and operations, monitor risk or report key information?
- How does your firm document system change requests and approvals?
- What type of testing does your firm perform prior to changes being moved into a production environment?
- What are your firm's procedures for tracking information technology problems and their remediation? Does your firm categorize problems based on their business impact?

* * *

If you have general comments regarding this letter or suggestions on how we can improve it, please send them to Steven Polansky, Member Supervision, at *Steven.Polansky@finra.org*, or Elena Schlickenmaier, Member Supervision, *Elena.Schlickenmaier@finra.org*.

Endnotes

1 *See also* the Product Suitability section of the 2017 Report on Examination Findings (2017 Report); Suitability for Retail Customers section of the 2018 Report on Examination Findings (2018 Report); Suitability Topic Page.

2 *See also* FINRA Rule 2320 (Variable Contracts of an Insurance Company); FINRA Rule 2330 (Members' Responsibilities Regarding Deferred Variable Annuities); Suitability for Retail Customers section of the 2018 Report; Variable Annuities Topic Page.

3 *See Regulatory Notice 10-22* (Obligations of Broker-Dealers to Conduct Reasonable Investigations in Regulation D Offerings); Reasonable Diligence for Private Placements section of the 2018 Report; Private Placements Topic Page.

4 *See* FINRA Rule 2232 (Customer Confirmations); MSRB Rule G-15; *Regulatory Notice 17-24* (FINRA Issues Guidance on the Enhanced Confirmation Disclosure Requirements in Rule 2232 for Corporate and Agency Debt Securities); *Regulatory Notice 17-08* (SEC Approves Amendments to Require Mark-up/Mark-down Disclosure on Confirmations for Trades With Retail Investors in Corporate and Agency Bonds); Fixed Income Confirmation Disclosure: Frequently Asked Questions (FINRA); Confirmation Disclosure and Prevailing Market Price Guidance: Frequently Asked Questions (MSRB); Fixed Income Mark-up Disclosure section of the 2018 Report; Fixed Income Mark-up Disclosure section of the 2019 Report on Examination Findings and Observations (2019 Report); Municipal Securities Topic Page; Fixed Income Topic Page.

5 *See* Abuse of Authority section of the 2018 Report; *Regulatory Notice 19-27* (FINRA Requests Comment on Rules and Issues Relating to Senior Investors); *Regulatory Notice 19-36* (FINRA Requests Comment on a Proposed Rule to Limit a Registered Person from Being Named a Customer's Beneficiary of Holding a Position of Trust for or on Behalf of Customer).

6 *See also Regulatory Notice 19-27* (FINRA Requests Comment on Rules and Issues Relating to Senior Investors); Frequently Asked Questions Regarding FINRA Rules Relating to Financial Exploitation of Senior Investors; Senior Investors Topic Page.

7 For additional considerations, please see the SEC's Federal Register notices for Reg BI, Form CRS and Interpretation of Solely Incidental.

8 *See also,* FINRA's Reg BI and Form CRS Firm Checklist.

9 *See also,* Online Distribution Platforms section of 2019 Annual Risk Monitoring and Examination Priorities Letter (noting concerns relating to certain online distribution platforms that are operated by unregistered entities, which may use member firms as selling agents or brokers of record, or to perform activities such as custody, escrow, back-office and financial technology (FinTech)-related functions).

10 *See also* Digital Communication section of the 2019 Report.

11 FINRA notes that Bank Sweep Programs or bank-like cash management services may require FINRA review, as they may be considered changes to firms' "business operations."

12 *See also Regulatory Notice 19-37* (SEC Approves Amendments to FINRA Rules 5130 and 5131 Relating to Equity IPOs).

13 For additional discussion of FINRA's concerns about discretionary accounts, see Abuse of Authority section of the 2018 Report.

14 *See* TRACE Reporting section of the 2017 Report; TRACE Reporting section of the 2018 Report; Trade Reporting Notice – 7/19/19 (FINRA Reminds Firms of Their Obligations Regarding TRACE Reporting).

15 *See* Regulation SHO section of the 2017 Report; Short Sales section of the 2019 Report.

16 *See* Exchange Act Rule 14e-4.

17 The Market Access Rule requires firms that provide access to trading in securities on an exchange or alternative trading system (ATS) to "appropriately control the risks associated with market access so as not to jeopardize their own financial condition, that of other market participants, the integrity of trading on the securities markets, and the stability of the financial system." U.S. Securities and Exchange Commission, Risk Management Controls for Brokers or Dealers With Market Access, Exchange Act Release No. 63,241, 75 Fed. Reg. 69,792 (Nov. 15, 2010); see also U.S. Securities and Exchange Commission, Division of Trading and Markets, Responses to Frequently Asked Questions Concerning Risk Management Controls for Brokers or Dealers with Market Access (Apr. 15, 2014).

18 *See* Direct Market Access Controls section of the 2019 Report.

19 *See* Best Execution section of the 2019 Report.

20 *See also Regulatory Notice 15-46* (Guidance on Best Execution Obligations in Equity, Options and Fixed Income Markets).

21 *See also* SEC Division of Market Regulation Staff Legal Bulletin 13A and SEC Division of Trading and Markets Responses to Frequently Asked Questions Concerning Rule 606 of Regulation NMS.

22 *See, e.g.,* Exchange Act Regulation D, Regulation S, Regulation A, Rule 15c3-1 (Net Capital Rule), Exchange Act Rule 15c3-3 (Customer Protection Rule), Exchange Act Rule 17a-5 (Financial Reporting Rule), Exchange Act Rule 17a-13 (Quarterly Securities Count Rule), as well as Exchange Act Rule 17a-3 and Rule 17a-4 (collectively, the Recordkeeping Rules).

23 *See, e.g.,* FINRA Rules 3110 (Supervision), 2210 (Communications with the Public) and 3310 (Anti-Money Laundering Compliance Program).

24 In addition, some registered representatives are engaging in outside business activities involving digital assets.

25 As discussed in *Regulatory Notice 19-24* (FINRA Encourages Firms to Notify FINRA if They Engage in Activities Relating to Digital Assets), we note that firms should inform FINRA if they plan to engage in digital asset transactions.

26 FINRA notes that the extent to which a broker-dealer comes into contact with customer funds and securities may impact its Net Capital Rule requirements and implicate the Customer Protection Rule for any assets received, held or deemed to be under the control of the broker-dealer.

27 *See* U.S. Securities and Exchange Commission, Division of Trading and Markets, Financial Industry Regulatory Authority, Office of General Counsel, Joint Staff Statement on Broker-Dealer Custody of Digital Asset Securities (July 8, 2019).

28 *See* Exchange Act Rule 17a-3(a)(23).

29 *See* U.S. Securities and Exchange Commission Division of Corporation Finance, Division of Investment Management, Division of Trading and Markets, and Office of the Chief Accountant, Staff Statement on LIBOR Transition (July 12, 2019).

30 *See also Regulatory Notices 19-18* (FINRA Provides Guidance to Firms Regarding Suspicious Activity Monitoring and Reporting Obligations) and *17-40* (FINRA Provides Guidance to Firms Regarding Anti-Money Laundering Program Requirements Under FINRA Rule 3310 Following Adoption of FinCEN's Final Rule to Enhance Customer Due Diligence Requirements for Financial Institutions).

31 Regulation S-P Rule 30 requires firms to have written policies and procedures that address administrative, technical and physical safeguards for the protection of customer records and information that are reasonably designed to: (1) ensure the security and confidentiality of customer records and information; (2) protect against any anticipated threats or hazards to the security or integrity of customer records and information; and (3) protect against unauthorized access to or use of customer records or information that could result in substantial harm or inconvenience to any customer. Regulation S-P also requires firms to provide initial and annual privacy notices to customers describing information sharing policies and informing customers of their right to opt-out of information sharing. Further, FINRA Rule 3110 (Supervision) requires firms to establish and implement a system that is reasonably designed to comply with Regulation S-P Rule 30, as well as related policies and procedures.

Appendix 1 – Additional Resources

Sales Practice and Supervision

Reg BI and Form CRS

- *Regulatory Notice* 19-26 (Regulation Best Interest: SEC Adopts Best Interest Standard of Conduct)
- Reg BI and Form CRS Firm Checklist
- Regulation Best Interest (Reg BI) Topic Page

Communications with the Public

- *Regulatory Notice* 19-31 (Disclosure Innovations in Advertising and Other Communications with the Public)
- 2018 Report – DBAs and Communications with the Public
- 2019 Report – Digital Communication
- Advertising Regulation Topic Page
- Private Placements Topic Page

Cash Management and Bank Sweep Programs

- 2017 Report – Net Capital and Credit Risk Assessments
- 2018 Report – Accuracy of Net Capital Computations
- 2018 Report – Segregation of Customer Assets
- 2019 Report – Observations on Liquidity and Credit Risk Management
- 2019 Report – Segregation of Client Assets
- Investor Alert – Cash Accounts: What They Are and How to Avoid Problems
- Update a Broker-Dealer Firm Registration
- Advertising Regulation Topic Page

Sales of Initial Public Offering (IPO) Shares

- *Regulatory Notice* 19-37 (SEC Approves Amendments to FINRA Rules 5130 and 5131 Relating to Equity IPOs)
- *Regulatory Notice* 17-14 (FINRA Requests Comment on FINRA Rules Impacting Capital Formation)
- Public Offerings Topic Page

Trading Authorization

- 2018 Report – Abuse of Authority
- 2019 Report – Suitability
- Suitability Topic Page
- Supervision Topic Page
- Books & Records Topic Page

Market Integrity

Direct Market Access Controls

- *Regulatory Notice* 15-09 (Guidance on Effective Supervision and Control Practices for Firms Engaging in Algorithmic Trading Strategies)
- *Regulatory Notice* 16-21 (SEC Approves Rule to Require Registration of Associated Persons Involved in the Design, Development or Significant Modification of Algorithmic Trading Strategies)
- 2017 Report – Market Access Controls
- 2018 Report – Market Access Controls
- 2019 Report – Direct Market Access Controls
- Algorithmic Trading Topic Page
- Market Access Topic Page

Best Execution

- *Regulatory Notice* 15-46 (Guidance on Best Execution Obligations in Equity, Options and Fixed Income Markets)
- 2017 Report – Best Execution
- 2018 Report – Best Execution
- 2019 Report – Best Execution
- Report Center, Equity Report Cards – FINRA's Best Execution Outside-of-the-Inside Report Card

Disclosure of Order Routing Information

- *Notice to Members* 01-30 (Member Obligations to Provide Statistical Information About Order Routing Under SEC Rule 11Ac-6 of the Securities Exchange Act of 1934)
- *Notice to Members* 01-44 (SEC Issues Interpretive Guidance Concerning Exchange Act Rules 11Ac1-5 and 11Ac1-6)
- 2017 Report – Best Execution
- 2018 Report – Best Execution
- 2019 Report – Best Execution
- Report Center, Equity Report Cards section – FINRA's Best Execution Outside-of-the-Inside Report Card

Vendor Display Rule

- *Regulatory Notice* 15-52 (SEC Staff Provides Insight Into Firms' Obligations When Providing Stock Quote Information to Customers)

Financial Management

Digital Assets

- *Regulatory Notice* 19-24 (FINRA Encourages Firms to Notify FINRA if They Engage in Activities Relating to Digital Assets)
- Report on Distributed Ledger Technology: Implications of Blockchain for the Securities Industry
- FinTech Topic Page

Liquidity Management

- *Regulatory Notice* 15-33 (Guidance on Liquidity Risk Management Practices)
- *Regulatory Notice* 10-57 (Funding and Liquidity Risk Management Practices)
- 2018 Report – Liquidity
- 2019 Report – Observations on Liquidity and Credit Risk Management
- Funding and Liquidity Topic Page

Contractual Commitment on Underwriting Commitments

- 2019 Report – Net Capital Calculations
- Exchange Act Rule 15c3-1(a)/001 Moment to Moment Net Capital
- Exchange Act Rule 15c3-1(c)(vii)/10 Marketability of Nonconvertible Debt Securities Which Are Not Highly Rated
- Exchange Act Rule 15c3-1(c)(2)(viii)(C)/03 Haircuts on Contractual Commitments
- Exchange Act Rule 15c3-1(c)(2)(viii)(C)/031 Underwriting Commitments
- Exchange Act Rule 15c3-1(c)(2)(viii)(C)/032 Offsetting Sale Commitments
- Exchange Act Rule 15c3-1(c)(2)(viii)(C)/04 Selling Group Participations
- Exchange Act Rule 15c3-1(c)(2)(viii)(C)/06 Underwriting Backstop Agreement

Firm Operations

Cybersecurity

- Report on Cybersecurity Practices - 2015
- Report on Selected Cybersecurity Practices – 2018
- 2017 Report – Cybersecurity
- 2019 Report – Observations on Cybersecurity
- Small Firm Cybersecurity Checklist
- Core Cybersecurity Controls for Small Firms
- Common Cybersecurity Threats
- Customer Information Protection Topic Page
- Cybersecurity Topic Page

Technology Governance

- *Regulatory Notice* 19-06 (FINRA Requests Comment on the Effectiveness and Efficiency of Its Rule on Business Continuity Plans and Emergency Contact Information)
- Business Continuity Plan FAQs
- 2019 Report – Business Continuity Plans
- Small Firm Business Continuity Plan Template
- Business Continuity Planning Topic Page

Regulation Best Interest and Form CRS: What You Need to Know
Thursday, January 23, 2020
1:30 p.m. – 3:00 p.m.

Join panelists as they discuss Form CRS, its impact on the industry and effective practices.

Moderator:
Meredith Cordisco
Associate General Counsel
FINRA Office of General Counsel

Speakers:
Anthony Cognevich
Chief Compliance Officer
Hancock Whitney Investment Services Inc.

Lourdes Gonzalez
Assistant Chief Counsel - Sales Practice, Division of Trading and Markets
U.S. Securities and Exchange Commission (SEC)

Daniel Woodring
Executive Vice President and Chief Compliance Officer
PFS Investment Inc.

Regulation Best Interest and Form CRS: What You Need to Know Panelist Bios:

Moderator:

Meredith Cordisco is Associate General Counsel with FINRA's Office of General Counsel. In this capacity, she provides legal guidance on policy initiatives, rule changes and interpretations in various areas, including regarding suitability, new issues and spinning, private securities transactions and outside business activities. Before joining FINRA in 2015, Ms. Cordisco was counsel in the Securities Litigation and Enforcement group at WilmerHale, where she focused her practice on complex securities enforcement investigations. Ms. Cordisco received her B.S., *summa cum laude*, in International Business and French from Mount St. Mary's University in Emmitsburg, Maryland, and her J.D., *summa cum laude*, and M.B.A., *cum laude*, from Villanova University. Following her studies, Ms. Cordisco clerked for the Honorable Eduardo C. Robreno on the U.S. District Court for the Eastern District of Pennsylvania.

Speakers:

Tony Cognevich began his career with NASD in New Orleans in 1987. During his 24 years at NASD/FINRA, Mr. Cognevich served as an examiner and exam manager primarily focused on Cause and Special Investigations, including high-profile sweeps. In late 2015 Mr. Cognevich joined Hancock Whitney Investment Services, Inc. in New Orleans, and serves as the firm's Chief Compliance Officer. Hancock Whitney Investment Services Inc. is a bank affiliate broker-dealer/RIA with offices from Tampa, FL to Dallas, TX. Mr. Cognevich is a graduate of the FINRA Institute at Wharton CRCP® program and has an MBA from Tulane University.

Lourdes Gonzalez is Assistant Chief Counsel for Sales Practices in the Division of Trading and Markets at the U.S. Securities and Exchange Commission. The Office of Sales Practices has program responsibility for a broad range of broker-dealer sales practice issues, including Regulation Best Interest and Form CRS, as well as broker-dealer supervision, anti-money laundering compliance, and securities arbitration. The Office also has program responsibility for business conduct obligations of security-based swap dealers. During her tenure, Ms. Gonzalez has received numerous SEC awards, including the SEC's Distinguished Service Award in 2017, which is the SEC's highest honorary award and given annually to recognize employees or teams who have made substantial and lasting contributions to the SEC's mission. Prior to joining the Commission, Ms. Gonzalez worked at the U.S. Department of the Treasury. She earned her law degree from George Washington University and her undergraduate degree from Georgetown University.

Daniel Woodring is Executive Vice President and Chief Compliance Officer of PFS Investments Inc. and Primerica Shareholder Services, Inc. Prior to joining Primerica, Mr. Woodring worked in numerous roles within the financial services industry, including brokerage, banking, insurance and consulting firms. He graduated from the University of Georgia earning a B.B.A. with dual majors in Finance and Risk Management. In 2000, Mr. Woodring received his J.D. from the Georgia State University College of Law. He is a member of the Georgia Bar and has served as Chair of the Financial Services Institute's Compliance Council and a member of the FINRA South Region Committee.

South Region Member Forum

January 23, 2020 | Hollywood, FL

Regulation Best Interest and Form CRS: What You Need to Know

FINRA®

Panelists

- Moderator
  - Meredith Cordisco, Associate General Counsel, FINRA Office of General Counsel
- Panelists
  - Anthony Cognevich, Chief Compliance Officer, Hancock Whitney Investment Services Inc.
  - Lourdes Gonzalez, Assistant Chief Counsel - Sales Practice, Division of Trading and Markets, U.S. Securities and Exchange Commission (SEC)
  - Daniel Woodring, Executive Vice President and Chief Compliance Officer, PFS Investment Inc.

Reg BI and Form CRS Firm Checklist

Compliance Date is June 30, 2020

FINRA is providing this checklist to help members assess their obligations under the SEC's Regulation Best Interest (Reg BI) and Form CRS Relationship Summary (Form CRS). This checklist explains key differences between FINRA rules and Reg BI and Form CRS. The checklist is not a substitute for any rule. Only the rule can provide definitive information regarding its requirements. Interpretive questions should be directed to the SEC, at *IABDQuestions@sec.gov*. You should carefully review the SEC's new rules and interpretations, related *Federal Register* notices and the SEC's Small Entity Compliance Guides, which provide important information on the new obligations.[1]

REG BI

1 Do you have procedures and training in place to assess recommendations using a **best interest** standard?

Status
Completed ✔

Securities recommendations must be in the retail customer's best interest. The firm and the associated person (AP) may not place their interests ahead of the retail customer's. This is a change from FINRA's suitability standard, which does not have an explicit best interest requirement. The best interest standard is an overarching obligation, which is satisfied only if you comply with four component obligations: Care, Disclosure, Conflict of Interest and Compliance.

2 Do you apply a best interest standard to recommendations of **types of accounts**?

Status
Completed ✔

Unlike FINRA's suitability rule, the best interest standard explicitly applies to recommendations of types of accounts. A broker-dealer (BD) or AP must have a reasonable basis to believe that a recommendation of a securities account type (*e.g.,* brokerage or advisory, or among the types of accounts offered by the firm, including IRAs) is in the retail customer's best interest at the time of the recommendation and does not place the financial or other interest of the BD or AP ahead of the interest of the retail customer.

In general, when considering recommendations of types of accounts, you should consider: (a) services and products provided in the account; (b) projected cost of the account; (c) alternative account types available; (d) services the retail customer requests; and (e) the retail customer's investment profile.

With regard to IRAs, in addition to the factors above, you should consider: (a) fees and expenses; (b) level of services available; (c) ability to take penalty-free withdrawals; (d) application of required minimum distributions; (e) protections from creditors and legal judgments; (f) holdings of employer stock; and (g) any special features of the existing account.

1 The SEC's *Federal Register* notices for *Reg BI, Form CRS, Interpretation of Solely Incidental and Interpretation of Investment Advisers' Obligations* are available at *https://www.sec.gov/rules/final.shtml*. The SEC's *Regulation Best Interest, A Small Entity Compliance Guide* is available at *https://www.sec.gov/info/smallbus/secg/regulation-best-interest*, and *Form CRS Relationship Summary; Amendments to Form ADV, A Small Entity Compliance Guide* is available at *https://www.sec.gov/info/smallbus/secg/form-crs-relationship-summary*.

3

If you agree to provide **account monitoring**, do you apply the best interest standard to both explicit and **implicit hold recommendations**?

Status
Completed
✔

Reg BI imposes no duty to monitor a customer's account following a recommendation. However, if you agree to perform account monitoring services, you are taking on an obligation to review and make recommendations regarding the account (*e.g.*, to buy, sell or hold) on the specified, periodic basis that you have agreed to with the retail customer. In such circumstances, Reg BI would apply even where you remain silent (*i.e.*, an implicit hold recommendation).

For example, if you agree to monitor a retail customer's account on a quarterly basis, the quarterly review and resulting recommendation will be subject to Reg BI, including an implicit recommendation to hold if you are silent as to the securities in the account. In addition, if you agree to monitor the customer's account, you are required to disclose the terms of such account monitoring services (including the scope and frequency of such services) pursuant to the Disclosure Obligation. IA registration requirements also might apply if a BD agrees to conduct ongoing monitoring in a manner not reasonably related to providing buy, sell or hold recommendations.

Importantly, you may voluntarily, and without any agreement with your customer, review the holdings in your retail customer's account for the purposes of determining whether to provide a recommendation to the customer. This voluntary review is not considered to be "account monitoring," and would not create an implied agreement with the customer to monitor the account.

4

Do you consider the elements of **care, skill** and **costs** when making recommendations to retail customers?

Status
Completed
✔

Reg BI incorporates FINRA's reasonable-basis (*i.e.* knowing the product and having a reasonable basis to believe it is appropriate for at least some investors) and customer-specific (*i.e.* knowing the customer and having a reasonable basis to believe a particular recommendation is appropriate for a specific customer based on that customer's investment profile) suitability obligations with important enhancements.

Care, skill and costs (in addition to applying a best interest standard) are new express elements for consideration when making recommendations to retail customers.

Cost must *always* be considered when making a recommendation. Moreover, consideration of cost includes not only the cost of purchase, but also any costs that may apply to the future sale or exchange of the security, such as deferred sales charges or liquidation costs. However, while cost must always be considered, it is not dispositive, and its inclusion in the rule text is not intended to limit or foreclose a recommendation of a more costly product if there is a reasonable basis to believe that product is in the best interest of a particular retail customer.

5

Do you guard against **excessive trading**, irrespective of whether the BD or AP "**controls**" the account?

Status
Completed
✔

Reg BI incorporates FINRA's quantitative suitability obligation (that a series of recommended transactions are appropriate and not excessive). However, in a change from FINRA's quantitative suitability obligation, Reg BI applies the best interest standard to a series of recommended transactions, irrespective of whether the BD exercises actual or de facto control over a customer's account.

6 Do you consider **reasonably available alternatives** to the recommendation?

Status Completed ✔

You should consider reasonably available alternatives, if any, offered by your BD in determining whether you have a reasonable basis for making the recommendation. An evaluation of reasonably available alternatives does not require an evaluation of every possible alternative (including those offered outside the firm) nor require BDs to recommend one "best" product.

A BD should have a reasonable process for establishing and understanding the scope of such "reasonably available alternatives" that would be considered by particular APs or groups of APs (*e.g.*, groups that specialize in particular product lines) in fulfilling the reasonable diligence, care and skill requirements under the Care Obligation.

7 Do you consider how to ensure that **high-risk** or **complex products** are in a retail customer's best interest?

Status Completed ✔

Although not a rule requirement, BDs should consider, as a best practice, applying heightened scrutiny as to whether high-risk or complex investments, such as inverse and leveraged ETFs, are in a retail customer's best interest.

8 Prior to or at the time of the recommendation, do you provide retail customers with full and fair written disclosure of all material facts relating to the scope and terms of the relationship with the retail customer, including:

Status Completed ✔

○ The capacity in which you are acting (BD or IA)?

A standalone BD generally may satisfy this requirement by delivering the Form CRS to the retail customer.

For BDs who are dually registered, and APs who are either dually registered or who are not dually registered but only offer BD services through a firm that is dually registered, providing Form CRS will not be sufficient to disclose their capacity, and they must disclose if they are acting as a BD when making a recommendation.

In addition, an AP of a dual registrant who does not offer investment advisory services must disclose that fact as a material limitation. Similarly, an AP registered in a limited capacity (*e.g.*, a Series 6) must disclose that limitation (*i.e.*, she cannot recommend all available products).

○ Material fees and costs that apply to the retail customer's transactions, holdings, and accounts?

This should build upon the fees and costs disclosure in Form CRS, with more particularity, such as whether fees are deducted from the customer's account per transaction or quarterly. This obligation would not require individualized disclosure for each retail customer. Rather, the use of standardized numerical or other non-individualized disclosure (*e.g.*, reasonable dollar or percentage ranges) is permissible.

The type and scope of services – whether or not the BD will monitor the retail customer's account and, if so, the scope and frequency of those services?

Although Form CRS may disclose that the firm provides account monitoring services, Reg BI requires disclosure about whether or not account monitoring would occur for the particular retail customer and the scope and frequency of those services.

Any requirements for retail customers to open or maintain an account or establish a relationship (*e.g.*, minimum account size)?

This would include any requirements for retail customers to open or maintain an account, or to avoid additional fees when a threshold is crossed, such as a low account balance.

Any material limitations on the securities or investment strategies involving securities that may be recommended to the customer?

Material limitations include recommending only proprietary products or a specific asset class; products with third-party arrangements (revenue sharing, mutual fund service fees); products from a select group of issuers; the fact that IPOs are available only to certain clients; and that an AP of a dually registered firm does not offer investment advisory services or is registered in a limited capacity (*e.g.*, Series 6).

The general basis for the recommendation (*i.e.*, what might commonly be described as the firm's investment approach, philosophy, or strategy)?

This may be standardized or a summary; however, the disclosure should also address circumstances when a standardized basis does not apply, and how the BD will notify the customer when that is the case.

As a best practice, firms should encourage APs to discuss the basis for any particular recommendation with their retail customers and the associated risks, particularly when the recommendation is significant to the customer (*e.g.*, the decision to roll over a 401(k) into an IRA).

Risks associated with the recommendation?

Standardized disclosure is permitted.

9 At or prior to making a recommendation, do you make full and fair written disclosure of all material facts relating to conflicts of interest?

Status
Completed
✔

Material facts regarding conflicts of interest include, for example: conflicts associated with proprietary products, payments from third parties and compensation arrangements. BDs must disclose all material facts relating to conflicts of interest associated with the recommendation. This does not require that information regarding conflicts be disclosed on a recommendation-by-recommendation basis. Standardized written disclosure of this information may be made, provided that it sufficiently identifies the material facts relating to conflicts of interest associated with a particular recommendation.

REG BI

10	Do you ensure that you do not use the term "advisor" or "adviser" unless you are a registered investment adviser, a registered municipal advisor, a registered commodity trading advisor or an advisor to a special entity?
○ Status Completed ✔	Use of the terms "advisor" or "adviser" in a name or title by: (a) a BD that is not also an RIA; or (b) a financial professional that is not a supervised person of an RIA, would presumptively violate Reg BI. Exceptions would include a BD/AP that acts on behalf of a municipal advisor or commodity trading advisor, or an advisor to a special entity. In addition, an RR of a dually registered BD may use firm materials when the BD/IA firm has the term "advisor" or "adviser" in its title.
11	Do APs supplement written disclosures with subsequent oral disclosure?
○ Status Completed ✔	Oral disclosure of a material fact may be required to supplement, clarify or update written disclosure made previously. BDs must maintain a record that oral disclosure was provided to the retail customer (but not the substance of the disclosure). Although not required by Reg BI, the SEC encourages, as a best practice, following oral disclosures with timely, written disclosure summarizing the information conveyed orally.
12	Do you have policies and procedures to **identify** and **address** the firm's conflicts of interest?
○ Status Completed ✔	Firms must have written policies and procedures reasonably designed to identify and, at a minimum, disclose or eliminate all conflicts of interest associated with recommendations covered by Reg BI. A conflict of interest is an interest that might incline a BD or AP – consciously or unconsciously – to make a recommendation that is not disinterested.
13	Do you have policies and procedures to **identify** and **mitigate** the AP's conflicts?
○ Status Completed ✔	Conflicts that create an incentive for the AP to place the BD's or AP's interest ahead of the retail customer's interest must be mitigated. Mitigation measures will depend on the nature and significance of the incentives and a variety of factors related to a BD's business model, such as its size and retail customer base, and the complexity of the security or investment strategy that is being recommended.
14	Do you have policies and procedures to **identify** and **disclose** material limitations on products recommended?
○ Status Completed ✔	Material limitations include, for example, recommending only proprietary products or a specific asset class; products with third-party arrangements; products from a select group of issuers; or making IPOs available only to certain clients.

15

Do you have policies and procedures to **prevent** material limitations from causing the BD or AP to make recommendations that place the BD's or AP's interest ahead of the retail customer's interest?

Status
Completed ✔

Policies and procedures to prevent harm from material limitations could consist of establishing product review processes for products that may be recommended, including establishing procedures for identifying and mitigating the conflicts of interests associated with the product, or declining to recommend a product where you cannot effectively mitigate the conflict, and identifying which retail customers would qualify for recommendations from the product menu.

As part of this process, firms may consider: evaluating the use of "preferred lists"; restricting the retail customers to whom a product may be sold; prescribing minimum knowledge requirements for APs who may recommend certain products; and conducting periodic product reviews to identify potential conflicts of interest, whether the measures addressing conflicts are working as intended, and to modify the mitigation measures or product selection accordingly.

16

Do you have policies and procedures to **identify** and **eliminate** sales contests, bonuses, non-cash compensation and quotas based on the sale of specific securities or specific types of securities within a limited time?

Status
Completed ✔

Reg BI bans these practices. This requirement does not apply to compensation practices based on, for example, total products sold, or asset growth or accumulation, and customer satisfaction.

This requirement would not prevent a BD from offering only proprietary products, placing material limitations on the menu of products, or incentivizing the sale of such products through its compensation practices, so long as the incentive is not based on the sale of specific securities or types of securities within a limited period of time.

The requirement also is not intended to prohibit: training or education meetings, provided that these meetings are not based on the sale of specific securities or types of securities within a limited period of time; or receipt of certain employee benefits by statutory employees, as these benefits would not be considered to be non-cash compensation for purposes of Reg BI.

17

Have you updated your policies and procedures to ensure **compliance** with Reg BI?

Status
Completed ✔

Reg BI's Compliance Obligation requires that BDs establish, maintain and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI.

In addition to the required policies and procedures, depending on the BD's size and complexity, a reasonably designed compliance program generally would also include: controls, remediation of non-compliance, training, and periodic review and testing.

Firms may be able to satisfy the Compliance Obligation by adjusting their current systems of supervision and compliance, rather than creating new ones.

18 Have you updated your policies and procedures and systems to ensure Reg BI's **recordkeeping** obligations are satisfied?

Status Completed ✔

SEA Rules 17a-3(a)(35) and 17a-4(e)(5) codify the recordkeeping requirements associated with Reg BI.

Current recordkeeping practices will not fully satisfy Reg BI. For example, BDs must provide retail customers with additional disclosures that require records. Firms may use a risk-based approach to documenting compliance with Reg BI.

19 Have you implemented **training** to ensure that APs are aware of Reg BI's requirements?

Status Completed ✔

The SEC noted that training generally is an important vehicle to communicate firm culture, specific requirements of a firm's code of conduct and its conflicts management framework.

20 Have you aligned your policies and procedures to the **definitions** in Reg BI?

Status Completed ✔

Retail Customer

Reg BI only applies to recommendations to "retail customers." Reg BI defines a "retail customer" as a natural person, or the **legal representative** of such person, who: (a) receives a **recommendation** for any securities transaction or **investment strategy** from a BD or AP; and (b) **uses** the recommendation primarily for **personal, family or household purposes**.

Legal Representative

"Legal representative" includes the non-professional legal representatives of such a natural person, *e.g.*, a non-professional trustee that represents the assets of a natural person. Reg BI would not apply when the legal representative is acting in a professional capacity as a regulated financial services industry professional retained to exercise independent professional judgment. Therefore, recommendations to registered IAs and BDs or corporate fiduciaries would not trigger Reg BI. On the other hand, recommendations to non-professional trustees, executors, conservators and persons holding power of attorney that represent natural persons are covered.

Recommendation

The final rule release for Reg BI states that this is keyed off of the guidance for FINRA's suitability rule.

Investment Strategy

The final rule release for Reg BI states that this is keyed off of the guidance for the FINRA's suitability rule; however, this will include recommendations of types of accounts.

Receives and Uses

The SEC has stated that "use" means when, as a result of the recommendation:

- the retail customer opens a brokerage account with the BD, regardless of whether the BD receives compensation;
- the retail customer has an existing account with the BD and receives a recommendation from the BD, regardless of whether the BD receives or will receive compensation, directly or indirectly, as a result of the recommendation; or
- the BD receives or will receive compensation, directly or indirectly, as a result of that recommendation, even if that retail customer does not have an account at the firm.

Personal, Family, or Household Purposes

The phrase "primarily for personal, family, or household purposes" covers any recommendation to a natural person for his or her account, other than recommendations to a natural person seeking these services for commercial or business purposes. Reg BI would not cover, for example, an employee seeking services for an employer or an individual seeking services for a small business or on behalf of another non-natural person entity, such as a charitable trust.

Conflict of Interest

A conflict of interest is an interest that might incline a BD or AP – consciously or unconsciously – to make a recommendation that is not disinterested.

Full and Fair

Sufficient information to enable a retail customer to make an informed decision with regard to a recommendation.

FORM CRS

1 Have you developed a two-page (four for dual registrants) **relationship summary known as Form CRS**?

Status Completed ✔

This applies to both IAs and BDs. Firms must write their relationship summaries in plain language, taking into consideration retail investors' level of financial experience. Firms are encouraged, but not required, to use electronic and graphical formatting.

2 Does your **relationship summary** include:

Status Completed ✔

- **An introduction to the firm?**

  This must include: (a) the name of the BD or IA, and whether the firm is registered with the SEC as a BD, IA or both; (b) an indication that BD and IA services and fees differ and that it is important for the retail investor to understand the differences; and (c) a statement that free and simple tools are available to research firms and financial professionals on the SEC's investment education website (Investor.gov/sec), which provides educational materials about BDs, IAs and investors.

- **A description of services and advice that can be provided?**

  The relationship summary must describe all relationships and services offered to retail investors, even if the investor at issue does not qualify for or is not being offered a particular service currently.

- **A description of fees and costs, applicable standard of conduct, and examples of how the firm makes money and conflicts of interest?**

  Firms must summarize the principal fees and costs that retail investors incur with respect to their BD and IA accounts, and the conflicts they create.

- **Relevant disciplinary history?**

  The relationship summary must include a separate section about whether a firm and its financial professionals have reportable disciplinary history and where investors can conduct further research on these events.

- **How additional information may be obtained?**

  Firms must state where retail investors can find additional information about their BD and IA services.

- **Prescribed "conversation starters" for investors to ask?**

  If a required disclosure or conversation starter is inapplicable to your business, or specific wording required by the Form's instructions is inaccurate, you may omit or modify that disclosure or conversation starter.

FORM CRS

3	Do you have a process in place to **file** the Form CRS?
○ Status Completed ✔	Firms must file the relationship summary through Web CRD® (dual registrants will be required to file their relationship summaries using both IARD™ and Web CRD®).
4	Do you have a process in place to **update** the Form CRS?
○ Status Completed ✔	Firms must update Form CRS and file it within 30 days whenever any information becomes materially inaccurate. Firms must communicate any changes in the updated relationship summary to retail investors who are existing clients or customers within 60 days after the updates are required to be made and without charge. Firms can make the communication by delivering the amended relationship summary or by communicating the information through another disclosure that is delivered to the retail investor. Form CRS General Instruction 8 sets forth requirements for updating the relationship summary, including filing and delivering an exhibit that highlights changes to an updated relationship summary.
5	Are you **delivering** Form CRS to each **new or prospective customer** who is a retail investor before or at the earliest of:
○ Status Completed ✔	(a) a recommendation of an account type, a securities transaction or an investment strategy involving securities; (b) placing an order for the retail customer; or (c) the opening of a brokerage account for the retail customer? If included in a packet of information, the relationship summary must be placed first. If the relationship summary is delivered electronically, it must be presented prominently in the electronic medium, for example, as a direct link or in the body of an email or message, and must be easily accessible for retail investors.
6	Do you have a process in place to **deliver** the relationship summary to **existing retail customers**?
○ Status Completed ✔	Firms must deliver the relationship summary to existing retail investor customers before or at the time firms open a new account that is different from the retail investor's existing account. In addition, firms must deliver the relationship summary when they recommend that the retail investor roll over assets from a retirement account, or when they recommend or provide a new service or investment outside of a formal account (*e.g.*, variable annuities or a first-time purchase of a direct-sold mutual fund through a "check and application" process). With respect to existing customers, firms should deliver the relationship summary in a manner consistent with the firm's existing arrangement with that customer and with the SEC's electronic delivery guidance.

FORM CRS

7	Are you posting the relationship summary on your **public website**?

Status
Completed ✔

Firms must post the current version of the relationship summary prominently on your public website, if you have one. The instructions set forth requirements, including design requirements, for a relationship summary that is posted on your website.

8	Have you adjusted your **recordkeeping procedures** to reflect the relationship summary?

Status
Completed ✔

BDs must make and keep current a record of the date that each relationship summary was provided to each retail investor, including any relationship summary that was provided before such retail investor opens an account.

BDs must maintain and preserve, in an easily accessible place, the following records until at least six years after such record or relationship summary is created: (a) all records of the dates that each relationship summary was provided to each retail investor, including any relationship summary that was provided before such retail investor opens an account, as well as (b) a copy of each relationship summary.

Regulation Best Interest and Form CRS: What You Need to Know
Thursday, January 23, 2020
1:30 p.m. – 3:00 p.m.

Resources

U.S. Securities and Exchange Commission Resources

- Instructions for Form CRS

  www.sec.gov/rules/final/2019/34-86032-appendix-b.pdf

- Form CRS Relationship Summary; Amendments to Form ADV

  www.sec.gov/info/smallbus/secg/form-crs-relationship-summary

- Frequently Asked Questions on Form CRS

  www.sec.gov/investment/form-crs-faq

Other Resources

- FINRA Reg BI and Form CRS Firm Checklist (Compliance Date is June 30, 2020)

  www.finra.org/sites/default/files/2019-10/reg-bi-checklist.pdf

- Form CRS Relationship Summary; Amendments to Form ADV, Federal Register, Vol. 84, No. 134 (Friday, July 12, 2019)

  www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12376.pdf

