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KD Financial News Alert: FINRA Sets Its To-Do List for 2017

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On January 4, 2017, the Financial Industry Regulatory Authority ("FINRA") released its 2017 Regulatory and Examination Priorities Letter (the "Letter"), in which FINRA outlined its areas of attention for the coming year. For 2017, FINRA has outlined five main areas on which it will focus: (1) High Risk and Recidivist Brokers; (2) Sales Practices; (3) Financial Risks; (4) Operational Risks; and, (5) Market Integrity. Within the broad areas, FINRA referenced several more narrow topics, such as product suitability and concentration; outside business activities; anti-money laundering ("AML") controls; liquidity risk; market manipulation; and cybersecurity.

The Letter indicates FINRA will devote particular attention to firms' hiring and monitoring of high-risk and recidivist brokers, including whether firms establish appropriate supervisory and compliance controls for such persons. FINRA will concentrate its efforts in this regard in three areas. First, FINRA plans to utilize a recently established examination unit to identify and examine brokers who may pose a high risk to investors. Second, FINRA will review firms' supervisory procedures for hiring or retaining statutorily disqualified and recidivist brokers. In doing so, FINRA will pay particular attention to the accuracy and completeness of the information contained in an applicant's Form U4, and will continue to monitor for the timely submission of disclosures required on Forms U4 and U5. FINRA will pay particular attention to firms with a concentration of brokers with significant past disciplinary records or a number of sales practice complaints or arbitrations. Third, FINRA will continue to evaluate firms' inspection programs and supervisory systems for branch and non-branch office locations, including, but not limited to, independent contractor branches.

FINRA will also concentrate on Sales Practices, particularly in relation to senior investors, product suitability and concentration, and outside business activities of registered representatives. Protecting senior investors will remain a top priority for FINRA in 2017. FINRA will continue to assess firms' controls to protect senior investors from fraud, abuse and improper advice, based largely on cases where registered representatives have recommended that senior investors purchase speculative or complex products in search of yield. More generally, FINRA will continue to concentrate on suitability issues and situations where registered representatives do not fully or properly understand important product features. FINRA will also continue to evaluate outside business activity review procedures with attention on whether such OBAs may compromise a registered person's responsibilities to clients, or be viewed as part of the firm's business.

Two of FINRA's priorities are not new for 2017 but remain on FINRA's hot-button issues list: AML and cybersecurity. AML compliance was a priority for FINRA in 2015 and 2016, and will continue to be in 2017. This year, FINRA will focus on areas where it has observed shortcomings in the previous two years, including gaps in automated trading and money movement surveillance systems caused by data integrity problems, and poorly set parameters or surveillance patterns that do not capture problematic behavior such as suspicious microcap activity. With respect to cybersecurity, FINRA will review methods for preventing data loss, including understanding the sensitivity of customer data, as well as its flow through the firm and to third-parties. In addition, FINRA will continue to examine two areas in which it has observed repeated shortcomings: (1) cybersecurity controls at branch offices, and (2) failures to fulfill one or more obligations under Securities Exchange Act Rule 17a-4(f)(regarding record retention and availability for review or audit).

FINRA's priorities for 2017 are, once again, extensive and are sure to present many challenges for firms to stay abreast of the relevant developments within the enumerated issues. The attorneys of Kaufman Dolowich & Voluck are poised to bring the ever-changing regulatory environment into focus for your member firm.

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