

The 2023 FINRA Annual Conference was full of informative concurrent sessions and well timed relevant regulatory topics. This year the FINRA staff gave the attendees a look into the future with the evolution of AI, off channel communications and digital assets.

The Plenary and Fireside chats held by FINRA CEO Robert Cook gave us an inkling as to what is on the horizon and the minds of the regulatory community.

FINRA casted a wide net of topics but yet there was an overlapping theme as certain topics appeared to crossover from session to session. The Asgard Team has identified its key takeaways from the sessions we attended. The following are our key takeaways:

Fireside Chat with SEC Commission Gensler

SEC Commissioner Gensler and FINRA CEO Robert Cook had their annual fireside chat. Commission Gensler addressed a variety of topics in his short session. Regulation Best Interest (“Reg BI”) was front and center. He indicated that Reg BI is working as intended. The SEC staff have several staff bulletins related to Reg BI, but he emphasized that this does not change the rule or its interpretation but rather summarizes the Staff’s view on how firms can meet their compliance obligations.

Next Commissioner Gensler discussed the evolving use of AI within our industry and how blockchain technology and other technological evolutions will impact the securities markets as a whole.

Lastly, Commissioner Gensler discussed digital assets which has become such a controversial topic. He has remained steadfast that Crypto platforms and other digital assets are securities and require those firms to register with the SEC as a broker-dealer.

Asgard takeaway - Commissioner Gensler continues to apply the Howey Test which is approximately 80 years old. The issue remains that this is a new asset class and without clear regulatory guidance innovation will be hindered.

Private Placements: The Latest Regulatory Developments and Compliance Considerations

Surveillance over private placements has increased substantially and FINRA has increased its resources to monitor the explosive growth of private capital raises. The session focused on FINRA Rules 5122 and 5123, a firm’s filing obligations, and conflicts of interest. As mentioned above, there were crossover of topics as the panelists discussed the applicability of Reg BI and a firm’s disclosure obligations to ensure that a private placement was in the best interests of the customer, customer complaint reporting and the accuracy of financial reporting via the Statement of Supplemental Income (“SSOI”).

Current Issues Under Reg Best Interest and Form CRS

Reg BI was perhaps the hottest of the topics discussed during the three-day event. The panel emphasized the delivery requirements of the Form CRS in conjunction when the advice provided is a Reg BI recommendation. Under the care obligation it was the panel’s view that firm’s need to memorialize and document that it sought reasonable alternatives for the individual customer, including documentation surrounding the Investment Advisor’s cost analysis. Further, ongoing training and education and evolution of policies and procedures are critical to a firm’s compliance with all aspects of Reg BI.

The Evolution of Branch Office Inspections

FINRA has refiled with the SEC its proposal for the changes in the definition of branch offices and allow a home office to be considered a non-branch “residential supervisory location” under certain conditions. FINRA Staff has also put out for comment, to which it has received twelve (12) comments thus far, the impact of the changes contemplated under the revised definition and inspection requirements.

The panelists discussed the evolution of smart phones, greater touch points with remote offices, control room supervision, and other tools that may allow for remote office inspections. Additionally, FINRA Staff suggested that each firm would need to weigh the impact of state registration requirements

Crypto Asset Developments

As the digital assets space is growing at a rapid pace, FINRA has deployed resources and key staff into newly formed departments such as the Special Investigations Unit (“SIU) which involves a team of AML and anti-fraud specialists. Within the SIU group is a Blockchain Lab, and the newly formed Crypto Assets Investigations Unit.

The panel was well represented including the Senior Director of Advertising Regulation. The panelists discussed the Sweep Exams that have commenced involving Crypto Asset Communications. FINRA is deploying more and more resources to get in front of this asset class and is investigating issues under customer complaint reporting, advertising and marketing submissions, Reg BI, Off-Channel Communications and personal trading reviews. The panel suggested that guidance will be forthcoming and expect to see certain enforcement actions taken related to books and records deficiencies.

An Exclusive View into FINRA’s Membership Application Process (MAP)

The panelists for this session focused on ways to make the application process more efficient. Attendees were advised that MAP is going through changes to make the application process faster and alluded to improvements coming in the near future which would make the submission process via the gateway more user friendly. One of the topics the panelists discussed was fast tracking applications. The audience was reminded that fast tracking an application is not a codified rule, and the decision to fast track an application is based on the number of business lines, application complexities, Registered Representative history, and Written Supervisory Procedures.

Another helpful discussion point was surrounding the scheduling of pre-filing meetings and the early firm meeting process. The panelists encouraged firms to schedule pre-filing meetings with FINRA Staff to review application responses before submitting. This allows firms to understand if there are any gaps in the information being submitted beforehand. To schedule this type of meeting, firms would email membership@finra.org and set up a pre-filing meeting. The early firm meeting process is for firms that are thinking about filing an application but have not begun the process yet and want to know more about what the process entails. Panelists encouraged firms to have a business plan in place so staff can understand the firm’s intended business lines. To schedule this type of meeting, firms would email membership@finra.org and set up an early firm meeting.

The Inside Scoop on Insider Threats and Cybersecurity

During this session, panelists focused on the groups considered insider threats and the most prevalent cybersecurity risks firms are facing. Insiders can be employees, contractors and IT. Panelists made a point of stating that many insider issues are accidents as a result of phishing attempts. A way to combat these types of accidental cyber issues is to ensure training is continuously given to all employees.

Another important topic the panelists covered was minimizing risk related to third-party vendors. As many firms outsource functions, the audience was advised to ensure there are data protection clauses in contracts, access rights are clear and there are cyber breach processes in place.

Access rights was another important topic, and members were advised to have controls in place related to internal access and third-party access. Firms should have offboarding controls, regular access review schedules and understand who has access to critical functions at all times.

It was made clear that cybersecurity is not simply an IT problem, but also a human problem. Cyber risk must be taken seriously by senior management and there must be a process in place for escalating cyber related issues. Panelists also encouraged members to establish a relationship between the firm and the FBI to ensure there are open lines of communications in the event of a crisis.

Understanding U4/U5 and 4530 Disclosure Reporting

During this session, panelists had several helpful tips to ensure disclosure is a smooth process. First, relating to 4530 filings, panelists encouraged members to notify their risk monitoring analyst after filing a 4530(b). For Form U5 filings, the panelists encouraged firms to provide FINRA with a description of events if submitting an “other” category Form U5. Members are encouraged to call their risk monitoring analyst if the facts surrounding a Form U5 are complicated.

Current Trends and Threats in Financial Crimes

This session focused on the latest developments in financial crimes and illicit finance risk including new and emerging threats related to money laundering, fraud, securities fraud, cyber-crime, digital assets and sanctions. After consulting with the U.S. Department of the Treasury, Financial Crimes Enforcement Network (“FinCEN”) issued eight (8) government wide priorities for Anti-Money Laundering and Countering the Financing of Terrorism (the “Priorities”). The Panelists listed these Priorities as:

1. Corruption;
2. Cybercrime, including relevant cybersecurity and virtual currency considerations;
3. Foreign and Domestic Terrorist Financing;
4. Fraud;
5. Transactional Criminal Organization Activity;
6. Drug Trafficking Organization Activity;
7. Human Trafficking and Human Smuggling; and
8. Proliferation Financing

The panelists advised FinCEN is in the process of drafting regulations which would require financial institutions to incorporate these Priorities into their risk-based AML programs.

Enforcement: Latest Developments and Trends

Examination priorities for both the SEC and FINRA continue to focus on:

1. Regulation Best Interest
2. Cybersecurity
3. Best Execution
4. Off-Channel Communications

However, did you know targeted examinations, known as sweeps, are an effective way for the regulators to gather information, carry out investigations and deliver a message to the industry? In fact, FINRA publishes a summary of the information requested in certain sweep letters on their website. The most recent sweep focused on Social Media Influencers, Customer Acquisition and Related Information Protection.

Redefining Communications Compliance for the Digital Age

As we rely increasingly on mobile apps, social media, and other digital channels to communicate, how are firms addressing the compliance challenges and opportunities these media offer? Here are some questions you should be asking to ensure compliance with this topic.

- Do policies and procedures accurately reflect the process being followed?
 - Do policies and procedures specifically state what is permitted and prohibited?
Example: When a Firm has a no texting policy, is a representative permitted to communicate via text message to another representative, specifically to let them know they are running late for a client meeting?
 - Do individuals complete attestations regarding their use of mobile apps, social media, and other digital channels for communication?
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A View into FINRA's Examination, National Cause and Financial Crimes Detection, and Risk Monitoring Programs

FINRA is beginning to conduct on-site examinations again, but how are they determining which firm's they'll be onsite for? Well, for starters, all new members will have an onsite examination, and if you have a new unique business model, you too will have an onsite examination. Otherwise, FINRA assesses each firm, analyzing the below information to determine if the examination will be onsite or not.

- Size/scale of the firm
- Risk rank based on information
- FINRA examination team decides there is benefit of being in person
- FINRA examination team wants to take a physical tour of the office
- Long overdue for an onsite examination
- FINRA examination team is finding it difficult receiving requested information