

FINRA Announces its 2018 Regulatory and Examination Priorities

On January 8, 2018, the Financial Industry Regulatory Authority (“FINRA”) published its 2018 Regulatory and Examination Priorities Letter to highlight areas of focus for FINRA’s upcoming examinations of registered broker-dealers. Significant areas of focus include financial technology innovations, including cybersecurity and supervision of transactions involving cryptocurrencies and initial coin offerings (“ICOs”), and oversight of illicit activity involving the exploitation of senior investors. FINRA priorities list include:

- **Fraud:** FINRA will focus on schemes that target senior investors, as well as microcap fraud schemes.
- **High-risk Firms and Brokers:** FINRA will focus on firms’ hiring and supervisory practices for high-risk broker-dealers, including firms’ remote supervision arrangements and branch inspection programs. FINRA will also focus on the risks these broker-dealers pose to unsophisticated or senior investors.
- **Operational and Financial Risks:** In this area, FINRA will focus on (1) the effectiveness of firms’ Business Continuity Plans in light of recent events, such as Hurricanes Harvey and Maria; (2) the protection of customer assets in compliance with Securities Exchange Act Rules 15c3-1 and 15c3-3; (3) the effectiveness of firms’ information and technology change management policies and procedures; (4) the effectiveness of firms’ cybersecurity programs; (5) the adequacy of firms’ anti-money laundering programs; (6) the adequacy of firms’

liquidity stress tests; and (7) firms' policies and procedures for monitoring the rates charged to customers for short sales.

- **Sales Practice Risks:** In this area, FINRA will focus on (1) the adequacy of firm's suitability controls, with particular attention paid to firms' new product vetting processes, recommendations made to participants in employer-sponsored retirement plans and recommendations to switch from a brokerage account to an investment adviser account when that switch disadvantages the customer; (2) the mechanisms firms use to ensure compliance with relevant securities laws when dealing with cryptocurrencies or ICOs; (3) firms' disclosure and supervisory practices related to margin loans; and (4) firms' compliance with sales practices and operational obligations related to securities-backed lines of credit.
- **Market Integrity:** In this area, FINRA will focus on (1) aggressive trading surrounding the open or close and collusion among market participants engaged in layering; (2) broker-dealers' best execution obligations when they receive order routing inducements; (3) firms' compliance with Rule 201 of Regulation SHO; (4) firms' transaction reporting in Treasury securities in light of the launch of Treasury securities reporting to the Trade Reporting and Compliance Engine; (5) manipulative option transactions, including "front running" activity and "marking the close" activity; (6) firms' compliance with Securities Exchange Act Rule 15c3-5, which requires broker-dealers to establish pre-trade financial controls; and (7) the adequacy of alternative trading systems' supervisory systems for detecting manipulative quoting and trading activity.

FINRA is also changing the manner in which it schedules and

performs examinations. FINRA is implementing additional changes to improve its new risk-based framework for determining examination schedules, which is designed to align FINRA examination resources with the risk profile of registered broker-dealers. In addition, FINRA is incorporating machine learning techniques to aid in the detection of manipulative trading activity.

[FINRA's 2018 Regulatory and Examination Priorities Letter is available here.](#) The letter should be used as a point of reference for registered broker-dealers when designing compliance programs or preparing for FINRA examinations.