

FINRA Conference 2018

The annual FINRA Conference, held May 21 through May 23 in Washington D.C., offered a diversity of subject discussions hosted by Robert Cook, FINRA's President and CEO. Panels consisted of SEC and FINRA staff, as well as member firm leaders and subject matter experts. The Conference was highlighted by a fireside chat and Q&A with SEC Chairman Jay Clayton and Robert Cook. Session topics included AML, Cybersecurity, Mock examination and common exam findings, Advertising, FinTech and related compliance topics. FINRA also provided "office hours" to meet one on one with staff and ask firm specific questions related to member broker dealer firms issues.

Crypto currency and coin offerings

Chairman Jay Clayton, in his chat with FINRA President and CEO Robert Cook, said his biggest surprise during the first year into his tenure has been the activities related to the crypto-asset space, including crypto currencies and ICOs. Clayton is concerned that some firms issuing ICOs are not always adhering to the rules related to private placements and public offerings, but are taking advantage of broad dissemination and the promise of secondary trading of public offerings, while providing none of the protections that would be required in private offerings. Clayton encouraged everyone to direct questions and comments related to ICOs (and how best to conduct their offerings) to the SEC.

The panel discussing Cryptocurrencies and ICOs, composed of FINRA, SEC and member firm staff active in the space, reiterated Chairman Clayton's points and positions. SEC staff continues working to effectively manage offerings but cited the difficulty in regulating these offerings in some cases because not all that should be registered are registering, which of course raise concerns regarding manipulation and liquidity, among other issues. The panel stated that there were approximately 1600 crypto currencies and a market cap of \$340 billion today.

The panel also highlighted the effectiveness of the SEC's recently launched "spoof" website, "HoweyCoins.com". The site mirrors marketing material published by actual cryptocurrency promoters. They were surprised by the large number of hits the site received in the relatively short period of time it has been up. Visitors to the site are routed to the Investor.gov, which outlines the spoof and the elements commonly used by ICO schemes to lure and trick investors. The SEC is using the site as another avenue of investor education and awareness and, based on the activity, they feel it has been effective.

Small firm focus

During several panel discussions, the subject of one-size-fits-all regulations and its application came up and how it can be challenging to small firms that may not necessarily have the infrastructure to efficiently comply with some rules. FINRA offered sessions on common examination findings focusing on small firms to highlight what areas to review to ensure adequate supervision. Small Firms should confirm that they are addressing the common findings related to their business and have adequate controls in place. The common small firm exam findings discussed include: cybersecurity program findings (such as lack of risk assessment and adequate system access controls) and third party vendor due diligence; outside business

activity and personal securities transaction supervision; limited or no OBA or PST compliance programs requiring disclosure, pre-approval and ongoing review of this activity; anti-money laundering programs that were inadequate or lacked testing, lacked review of systems or delegations to third parties; product suitability related to UITs and share classes; and market access controls, best execution and trade reporting; net capital related findings.

Also, to ease broker-dealers and registered representative cost for regulatory reporting, effective July 9, FINRA will be implementing a new public records search within 15 days of filing a U-4. This will provide BDs with information that should have been reported on the applicant's U-4. This will also assist small firms by reducing costs for hiring vendors to do background checks and assist with receiving more timely potential disclosure information. Another tool to note related to registered person due diligence is the SEC's recently launched "SALI" (SEC Action Lookup for Individuals). This tool allows investors and firms to search whether a person attempting to sell investments has a judgement or order against them in an SEC enforcement action. Again, some additional tools to use making the registration due diligence process easier.

In addition, the panel which was made up of FINRA sales practice directors and small firm principals, also made it a point to highlight additional resources that FINRA provides its membership. FINRA offers a small firm hotline which firms can call to ask FINRA staff questions directly. FINRA's AML Template was offered to assist firms in the development, implementation and execution of an AML program.

Regulation Best Interest

During his fireside chat with Chairman Clayton, Robert Cook made it a point to try and get more clarity on the definition of "best interest". Clayton solicited input and comment from the membership related to the proposed regulation. Clayton said the SEC has examined the relationship a client has with a broker-dealer or with an investment advisor and asked what a reasonable investor would expect of that relationship. In the cases of both broker-dealers and investment advisers, a reasonable investor should expect that an investment professional cannot put his or her interests ahead of the investor's interests. Regarding the proposed regulation, Chairman Clayton also said that he does not like using the word "fiduciary" as it relates to the two different client models. In the broker dealer and investment advisor models, while both relationships involve a fiduciary principle, calling them both "fiduciary" would not make it clear that the relationship models are different. Using the same term, he explained, might lead an investor to believe that the relationship between an investor and a broker-dealer (transaction-based model) and between an investor and an investment adviser (advisory relationship model) are the same.

Conclusion

Based on the topics and themes frequently addressed during the conference, Broker-Dealers can expect additional questions, sweeps and focus related to the crypto asset space going forward. Reg BI and industry comment and debate as Reg BI evolves. Firms should continue to review their compliance program with an eye toward what the regulators are finding at other firms during the examination process and how it relates to their business.