

Broker-Dealer Alert

January 2015

The new year brings a number of important developments for the broker-dealer industry. Last week, FINRA issued its Regulatory and Examinations Priorities Letter for 2015. FINRA has also recently enacted and proposed a number of important rule changes. In addition, the SEC has reported a record number of enforcement actions for fiscal year 2014, including a number of first-ever cases and the advancement of several important initiatives. The following is a summary of these developments.

FINRA'S 2015 REGULATORY AND EXAMINATIONS PRIORITIES LETTER

On January 6, 2015, FINRA issued its Regulatory and Examinations Priorities Letter for 2015. The 2015 Priorities Letter states that FINRA will continue to focus on five key areas of broker-dealer activity: (i) alignment of firms' interests with those of their customers; (ii) standards of ethical behavior; (iii) development of strong supervisory and risk management systems; (iv) development, marketing and sale of novel products and services; and (v) management of conflicts of interest. FINRA's 2015 Priorities Letter also identifies specific areas of concern, including the sale and supervision of interest rate sensitive and complex products, controls around the handling of wealth events in investors' lives, management of cybersecurity risks and treatment of senior investors. The 2015 Priorities Letter further indicates that FINRA Market Regulation will focus this year on a range of key issues, including, among others, abusive trading algorithms, high-frequency trading, cross-market and cross-product manipulation, order routing practices, best execution and disclosure and market access controls.

RECENT FINRA RULE CHANGES

New Carve-Out for Confidentiality Provisions: FINRA recently released Regulatory Notice 14-40, which explains that firms are prohibited from including in arbitration settlement agreements any provisions that bar customers or employees from reporting wrongdoing to regulators. To ensure compliance with Rule 2010, FINRA has approved the following language for inclusion in settlement agreements containing confidentiality provisions: "Any non-disclosure provision in this agreement does not prohibit or restrict you (or your attorney) from initiating communications directly with, or responding to any inquiry from, or providing testimony before, the SEC, FINRA, any other self-regulatory organization or any other state or federal regulatory authority, regarding this settlement or its underlying facts or circumstances."

Highlights of FINRA's Consolidated Supervision Rules: Last month, FINRA's Consolidated Supervision Rules 3110, 3120, 3150 and 3170 went into effect. These Rules provide a comprehensive supervision framework for FINRA member firms and modify requirements relating to, among other things: (i) supervising offices of supervisory jurisdiction and inspecting non-branch offices; (ii) managing conflicts of interest in a firm's supervisory system; (iii) performing risk-based review of correspondence and internal

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communications; (iv) carrying out risk-based review of investment banking and securities transactions; (v) monitoring for insider trading; and (vi) testing and verifying supervisory control procedures.

Broader Authority for Arbitrators to Make Regulatory Referrals: The SEC approved changes to FINRA Rules 12104/13104, which broaden the authority of an arbitrator to make disciplinary referrals during the pendency of an arbitration proceeding. An arbitrator is now permitted to make a mid-case referral if the arbitrator becomes aware of any matter or conduct that the arbitrator has reason to believe poses a serious threat, whether ongoing or imminent, that is likely to harm investors unless immediate action is taken.

PROPOSED FINRA RULES

Proposed Expansion of the Scope of the Non-Public Arbitrator Definition: FINRA has proposed several changes to Rules 12100(p)/13100(p) and 12100(u)/13100(u) of the customer and industry codes of arbitration procedure, which would refine the definitions of "non-public" arbitrator and "public" arbitrator. The proposed rule changes would further restrict certain categories of persons from serving as public arbitrators. The proposed rule changes would permanently limit industry members to the non-public arbitrator roster and would further constrain attorneys, accountants and other professionals who devote at least 20% of their practices to the securities industry from serving as public arbitrators. The comment period for these proposed rule changes ended in November 2014 and the time for the SEC to act currently expires on February 28, 2015.

ENFORCEMENT TRENDS AND ACTIVITY

The SEC reported that, in fiscal year 2014, new investigative approaches and innovative use of data and analytical tools contributed to a record 755 enforcement actions with orders totaling \$4.16 billion in disgorgement and penalties. This is a sharp increase from fiscal year 2013 in which the SEC brought 686 enforcement actions with orders totaling \$3.4 billion in disgorgement and penalties. The SEC's enforcement actions also included a number of first-ever cases, including actions involving the market access rule, the "pay-to-play" rule for investment advisors, an emergency action to halt a municipal bond offering and an action for whistleblower retaliation.

ABOUT US

Sherman Wells Sylvester & Stamelman LLP is a full service law firm with over 30 experienced attorneys, fiduciary accountants and paralegals and offices in Florham New Jersey and mid-town Manhattan. Our attorneys have a wealth of experience practicing in disciplines including Banking and Financial Services Law, Broker-Dealer Litigation and Arbitration, Commercial and Business Litigation, Corporate Law, Estate Planning and Estate Administration, Estate and Fiduciary Litigation, Executive Compensation, Intellectual Property and Technology, Media and Entertainment, Mergers and Acquisitions, Professional Liability Claims and Taxation.

The attorneys at Sherman Wells have extensive experience representing broker-dealers and their employees in a wide range of complex securities litigation matters brought before FINRA and federal and state courts throughout the country. Our attorneys routinely, and successfully, represent brokerage firms and affiliated entities in both pre-arbitration customer disputes and sales practice arbitrations, employment disputes, securities-backed lending matters, anti-money laundering and asset forfeiture cases, subpoenas levies and garnishments and regulatory enforcement matters.

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