

# 2017 Annual Regulatory and Examination Priorities Letter

January 2017

## Topics

- High-risk and Recidivist Brokers 2
- Sales Practices 3
- Financial Risks 5
- Operational Risks 6
- Market Integrity 9
- Conclusion 11
- Endnotes 11

## Introduction

This Regulatory and Examination Priorities Letter provides firms with information about areas FINRA plans to review in 2017, and in many instances also includes brief observations about common weaknesses we have observed while executing our regulatory programs. Firms can use this letter to identify priorities applicable to their business and to strengthen their compliance, supervisory and risk management controls to protect investors, the markets and themselves.

FINRA develops these priorities based on observations from our regulatory programs as well as input from various stakeholders, including investor advocates, firms and other regulators. Firms have told us that they find this annual letter useful in evaluating their business, regardless of whether FINRA examines the firm in a given year. Some firms use the letter to help identify applicable priorities and then to define their training program requirements for the coming year, assess programs they may need to strengthen or update, and frame issues that they will address in their annual compliance conferences and other internal communications.

For its part, FINRA has enhanced its risk-based surveillance and examination programs to apply a nationally consistent approach to identify and focus on material conduct at firms based on our assessment of specified sales practice, financial, operational and market-integrity risks. This approach has improved our understanding of each firm's business, permitting us to better tailor examinations and other regulatory responses to conduct that poses the greatest threats to investors or the market. In planning and executing an examination, we consider, among other things, a firm's business model, size and complexity of operations, and the nature and extent of a firm's activities against the priorities outlined in this letter.

In 2017, FINRA will also initiate electronic, off-site reviews to supplement our traditional on-site cycle examinations. This program will enable FINRA to review selected areas, typically those covered in this letter, without going on site to the firm. Instead, FINRA will make targeted and limited information requests to firms and then analyze responses off site. We will conduct these off-site exams only on a select group of firms that are not currently scheduled for a cycle exam in 2017.

FINRA will focus on the following issues and concerns through our regulatory programs in 2017.



## High-risk and Recidivist Brokers

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 is strengthening its already comprehensive approach to high-risk and recidivist brokers in three areas. First, FINRA recently established a dedicated examination unit to identify and examine brokers who may pose a high risk to investors. This group will rigorously review these brokers' interactions with customers, including their compliance with rules regarding suitability, know-your-customer, outside business activities, private securities transactions, commissions and fees.

Second, FINRA will review firms' supervisory procedures for hiring or retaining statutorily disqualified and recidivist brokers. FINRA will examine firms' due diligence on these individuals and that will include determining whether, as part of the verification process, a firm or third-party service provider conducts a national search of reasonably available public records to verify the accuracy and completeness of the information contained in an applicant's Form U4. FINRA also will continue to monitor for the timely submission of disclosures required on Forms U4 and U5.

FINRA will assess whether firms develop and implement a supervisory plan reasonably tailored to detect and prevent future misconduct by a particular broker based on prior misconduct and regulatory disclosures. We will also focus on firms with a concentration of brokers with significant past disciplinary records or a number of sales practice complaints or arbitrations. At the same time, we will continue to scrutinize closely applications by firms to associate with statutorily disqualified persons and will oppose these plans where we conclude that they do not satisfy applicable requirements. Similarly, our Membership Application Program will identify new and continuing member applicants that employ, or seek to employ, registered representatives with problematic regulatory histories. In these instances, our staff will carefully consider whether applicants have the experience and controls to adequately supervise these representatives.

Third, FINRA will continue to evaluate firms' branch office inspection programs as well as their supervisory systems for branch and non-branch office locations, including, but not limited to, independent contractor branches. FINRA's focus for these reviews will include the supervision of account activity; advertising and communications, including the potential use of unapproved email addresses for business; communications with customers, including through the use of social media, seminars, radio shows or podcasts; registered representatives' websites; outside business activities; the use of consolidated account statements; and operational activities such as distribution of funds and changes of address or investment objectives.

## Sales Practices

### Senior Investors

Investor protection lies at the heart of FINRA's mission, and protecting senior investors will remain a top priority in 2017. FINRA will assess firms' controls to protect senior investors from fraud, abuse and improper advice. We are seeing numerous cases where registered representatives have recommended that senior investors purchase speculative or complex products in search of yield. While the quest for higher yield is not *per se* problematic, FINRA will assess whether such recommendations were suitable given an investor's profile and risk tolerance, and whether firms have appropriate supervisory mechanisms in place to detect and prevent problematic sales practices.

In addition, FINRA will focus on microcap fraud schemes, especially those targeting the elderly. Microcap (or "penny") stocks are particularly vulnerable to market manipulation given the lack of public information regarding the companies' underlying business and management, as well as the lack of verifiable financial information. In 2015 and 2016, FINRA observed an increase in the use of aggressive boiler room tactics by unregistered persons in pump-and-dump schemes targeting elderly investors. There are a number of controls firms can implement to enhance protection for elderly clients from such financial exploitation. For example, firms can contact an elderly customer in instances where the customer has placed a purchase order for a speculative penny stock through the customer's online brokerage account, can question a customer about inquiries to buy or sell penny stocks held outside the firm and can ask a customer about instructions to transfer funds to persons who may be tied in some way to the issuer.

### Product Suitability and Concentration

FINRA continues to observe instances where firms recommend products that are unsuitable for customers, including situations where customers and sometimes registered representatives do not understand important product features. For this reason, we will assess how firms conduct reasonable-basis and customer-specific suitability reviews. This may include examining firms' product vetting processes, supervisory systems and controls to review recommendations. Firms should be attentive to the adequacy of their supervision and training when new products come to market, new features of existing products are introduced or market conditions change in ways that could affect product performance. Firms that hire registered representatives who sell products with which the firm is not familiar should educate themselves on the products and then carefully evaluate their ability to supervise recommendations. Training should ensure that registered representatives, compliance and supervisory staff understand the objectives, risks and pricing factors of the products sold, including any changes in the features of those products.

In 2017, FINRA will also increase its focus on the controls firms use to monitor recommendations that could result in excess concentration in customers' accounts. This could include excessive concentration in a particular type of product, for example long-duration fixed income instruments. Firms should be attentive to shifts in the interest rate environment and should be prepared to assess and discuss the possible impact of these changes on recommendations to clients. Firms should also monitor for excessive concentration in securities exposed to an industry sector.

The concerns we discuss above can arise with many products. For example, calls to the FINRA Securities Helpline for Seniors<sup>®</sup> (HELPS<sup>™</sup>) have exposed troubling scenarios of senior and unsophisticated investors buying into sales pitches for speculative energy-based investments. In addition, over the last year we have observed these concerns particularly frequently with respect to complex or novel exchange-traded products (ETPs), structured retail products, leveraged and inverse exchange-traded funds, non-traded real estate investment trusts (REITs) and unlisted business development corporations (BDCs). While these products can be appropriate for some customers, certain non-traded REITs and unlisted BDCs, for example, may have high commissions and fees, be illiquid, have distributions that may include return of principal, have limited operating history, or present material credit risk arising from unrated or below investment grade products. Given these concerns, firms should make sure that they perform and supervise customer-specific suitability determinations. More generally, firms should carefully evaluate their supervisory programs in light of the products they offer, the specific features of those products and the investors they serve.

### **Excessive and Short-term Trading of Long-term Products**

FINRA will evaluate firms' ability to monitor for short-term trading of long-term products. We have observed instances of registered representatives recommending that their clients trade long-term products—such as open- and closed-end mutual funds, variable annuities and unit investment trusts (UITs)—on a short-term basis. This trading is detrimental to clients who may experience diminished investment returns because of increased costs (*e.g.*, commissions, underwriting fees, or creation and development fees) or missed dividend payments in the case of UITs. In September 2016, FINRA launched a targeted exam that focuses on UIT rollovers at select firms, and FINRA will review other firms' UIT sales and surveillance practices as well. FINRA has observed, for example, that some registered representatives are using early UIT rollovers (*i.e.*, rollovers prior to the last 30-60 days of the UIT's term) to increase their sales credits to the detriment of clients.

In addition, FINRA urges firms to evaluate whether their supervisory systems can detect activity intended to evade automated surveillance for excessive switching activity. For example, we have observed situations where registered representatives switch customers across products to evade surveillance that focuses on switching within the same product class. Similarly, FINRA has observed situations where registered representatives switch customers through several investments to conceal the source of funds from switching surveillance tools.

### **Outside Business Activities and Private Securities Transactions**

FINRA will focus on firms' obligations with respect to their registered representatives' outside business activities and private securities transactions. We will continue to evaluate firms' procedures to review registered persons' written notifications of proposed outside business activities, including firms' consideration of whether the proposed outside business activities may compromise a registered person's responsibilities to the firm's clients or be viewed as part of the firm's business. FINRA will also focus on firms' procedures for handling associated persons' notifications of proposed private securities transactions and firms' ongoing supervision over associated persons' approved private securities transactions for compensation.

## Social Media and Electronic Communications Retention and Supervision

FINRA will review firms' compliance with their supervisory and record-retention obligations with respect to social media and other electronic communications in light of the increasingly important role they play in the securities business. We note that these obligations apply to business communications irrespective of the medium or device used to communicate. Under U.S. Securities and Exchange Commission (SEC) and FINRA record-retention requirements, firms must ensure the capture of business-related communications regardless of the devices or networks used. A firm must capture and maintain all business-related communications in such a way that the firm can review them for inappropriate business conduct.

## Financial Risks

### Liquidity Risk

During 2016, FINRA assessed liquidity management practices and identified firms that lacked liquidity risk management plans, did not conduct stress tests, applied insufficiently rigorous assumptions in their stress tests or maintained insufficient sources of funding. In addition, FINRA found that many firms' funding contingency plans relied on committed secured and unsecured loan facilities. Contracts for these facilities may contain provisions (*e.g.*, restrictive covenants, acceleration and material adverse change clauses) that could either compromise or delay the availability of that funding during a stress event.

In light of these findings, in 2017, FINRA will review firms' funding and liquidity plans, and assess whether firms adequately evaluate their liquidity needs related to market-wide and idiosyncratic stresses, develop contingency plans so that they have sufficient liquidity to endure those stresses, and conduct stress tests and other reviews to gauge the effectiveness of their contingency plans. Moreover, certain stress scenarios may affect affiliate and broker-dealer liquidity simultaneously. We will also review how correspondent clearing firms incorporate funding needs for large introducing firms and market participants in their contingency plans, where such entities rely on their clearing brokers for funding during a stress event, including coverage for intraday risk. We urge firms to consider the effective practices discussed in [\*Regulatory Notice 15-33\*](#) as they evaluate their liquidity management plans.

### Financial Risk Management

Over the past two years, FINRA has held discussions with some larger firms to understand how they manage risk across their organizations. The discussions focused on the extent of the independence of the firms' risk management governance; the scope, span and focus of key control functions; and the frequency and effectiveness of communication and reporting between parties responsible for monitoring and controlling risk. Similar to the thematic liquidity review that produced *Regulatory Notice 15-33*, and in furtherance of our risk management focus, FINRA will ask a select group of firms to explain how they would react to a specific stress scenario that affects a firm's market, credit and liquidity risks. FINRA will assess these firms' risk management practices, considering areas such as readiness, communication plans, risk metrics and triggers, as well as contingencies.

We will assess these practices to understand whether the approach appears reasonable in light of the risks to the firm's business, not with an expectation of a "right way" or "wrong way" to deal with the scenario.

## Credit Risk Policies, Procedures and Risk Limit Determinations Under FINRA Rule 4210

In June 2016, the SEC approved amendments to FINRA Rule 4210 to establish margin requirements for covered agency transactions, and on December 15, 2016, the first phase of the new amendments became effective. In 2017, FINRA will review firms' implementation of the obligations established in the first phase of the rule amendment. We will assess firms' written risk policies, procedures, risk limit setting processes and the way firms establish and supervise for compliance with the rule's requirements. Firms should review the new rule requirements to ensure they have appropriately tailored their risk policies and limits to their counterparties and covered agency transactions.

## Operational Risks

### Cybersecurity

Cybersecurity threats remain one of the most significant risks many firms face, and in 2017, FINRA will continue to assess firms' programs to mitigate those risks.<sup>1</sup> FINRA recognizes there is no one-size-fits-all approach to cybersecurity, and we will tailor our assessment of cybersecurity programs to each firm based on a variety of factors, including its business model, size and risk profile. Among the areas FINRA may review are firms' methods for preventing data loss, including understanding their data (*e.g.*, its degree of sensitivity and the locations where it is stored), and its flow through the firm, and possibly to vendors. FINRA may assess controls firms use to monitor and protect this data, for example, through data loss prevention tools. In some instances, we will review how firms manage their vendor relationships, including the controls to manage those relationships. The controls should be informed by a number of factors, including a clear understanding of any customer or employee personally identifiable information or sensitive firm information to which vendors have access. We may also examine firms' controls to protect sensitive information from insider threats. The nature of the insider threat itself is rapidly changing as the workforce evolves to include more employees who are mobile, trusted external partnerships and vendors, internal and external contractors, as well as offshore resources.

We also draw firms' attention to two areas in which we have observed repeated shortcomings in controls. First, cybersecurity controls at branch offices, particularly independent contractor branch offices, tend to be weaker than those at firms' home offices. We have observed poor controls related to the use of passwords, encryption of data, use of portable storage devices, implementation of patches and virus protection, and the physical security of assets and data. Second, in multiple instances, firms have failed to fulfill one or more of their obligations under Securities Exchange Act (SEA) Rule 17a-4(f) that requires firms to, among other things, preserve certain records in a non-rewriteable, non-erasable format, commonly known as write once read many (WORM) format. This includes situations where vendor-provided email review and retention services did not fulfill SEA Rule 17a-4(f) requirements. FINRA recently announced enforcement actions against 12 firms for, among other things, failure to preserve broker-dealer and customer records in WORM format.<sup>2</sup>

## **Supervisory Controls Testing**

FINRA will assess firms' testing of their internal supervisory controls. Regular testing is critical to enabling firms to identify and mitigate gaps or inadequate controls (*e.g.*, poorly set parameters in automated compliance systems) that, left undetected, may lead to significant, systemic control breakdowns. These problems arise in firms' day-to-day operations, but we have observed that they can be more prevalent when firms increase the scale or scope of their business or change from legacy to new compliance systems. Control breakdowns can include record-retention omissions and failures to deliver requisite disclosure or other documents to clients. In addition, FINRA has observed situations where data is inaccurate, for example, with respect to product or order types. This can lead to situations where automated alerts fail to identify activity in client accounts for further review or where extensive manual intervention is necessary to make the data useable. FINRA reminds firms of their obligations with respect to supervisory controls testing and chief executive officer certifications pursuant to FINRA Rules 3120 and 3130.

## **Customer Protection/Segregation of Client Assets**

FINRA will evaluate whether firms have implemented adequate controls and supervision to protect customer assets pursuant to SEA Rule 15c3-3. FINRA will assess firms' compliance with the specific requirements of the rule, for example, whether firms properly include customer securities positions and money balances on multiple platforms in the reserve formula and in the possession or control calculations. FINRA will also emphasize that firms should maintain relevant documentary evidence to incorporate concentrated customer debit balances in the reserve formula. We will test whether the Special Reserve Bank agreements with banks, regardless of their size, location or the amount on deposit with them, have the required no-lien language. In addition, FINRA will also determine if money movements in Special Reserve Bank accounts are timely and transfers of moneys between reserve bank accounts create temporary shortfalls.

We will review whether firms maintain sufficient documentation to demonstrate that securities are held free of liens and encumbrances, especially for alternative investment products in customer retirement accounts. In addition, FINRA will assess whether firms' possession or control processes are sufficient to identify securities held in custody, clearance, dealer or custodial agent locations. We will also evaluate the adequacy of firms' supervision and controls to identify, and where appropriate prevent, manual overrides of automated possession or control calculations. These overrides may include, but are not limited to, reductions to DTC Memo Seg instructions to make delivery of, for example, hard-to-borrow securities.

Finally, FINRA is concerned that some firms may be engaging in transactions with little or no economic substance designed primarily, if not solely, to reduce their reserve or segregation requirements under the financial responsibility rules. This would put customer cash or securities at risk if, for example, a firm went out of business and held its customers' securities in an account subject to a lien or if a firm artificially reduced the reserve computation through such transactions. FINRA will review for this behavior from two perspectives. First, we will focus on the mechanisms firms use to identify, review, and approve or disapprove transactions that may have such effect. Second, we

will review client transactions that result in outsized profit for a client when compared to transactions of similar risk as well as transactions that shift profit or loss between a broker-dealer and its affiliates that are not supported by the economics of the situation.

### **Regulation SHO – Close Out and Easy to Borrow**

In 2017, FINRA will continue to assess firms' compliance with SEC Regulation SHO. In light of recent SEC enforcement actions, FINRA will focus on the locate process to ensure firms have reasonable grounds to believe securities are available for borrowing prior to accepting a short sale. FINRA will assess firms' preparation and use of the easy-to-borrow list as well as evaluate the adequacy of firms' automated locate models. FINRA has observed fails-to-deliver on settlement date, when locates are granted without the requisite reasonable grounds to believe that the security could be borrowed. Firms should continue to monitor their close-out processes and ensure that they appropriately close out fails-to-deliver by the designated close-out date pursuant to Rule 204 of Regulation SHO.

### **Anti-Money Laundering and Suspicious Activity Monitoring**

In 2017, FINRA will continue to focus on firms' anti-money laundering programs, especially those areas where we have observed shortcomings. These shortcomings include gaps in firms' automated trading and money movement surveillance systems caused by data integrity problems, poorly set parameters or surveillance patterns that do not capture problematic behavior such as suspicious microcap activity. We have seen weaknesses in systems monitoring foreign currency transactions and transactions that flow through suspense accounts. Firms may perform anti-money laundering suspicious activity monitoring using the same trading surveillance they use for supervisory purposes, but that surveillance must also include alerts tailored to the firm's anti-money laundering red flags. FINRA will also continue to focus on firms' controls around accounts held by nominee companies. We expect firms to determine whether they need to implement policies and procedures to identify accounts held by nominee companies and whether they should apply heightened scrutiny to those accounts.

### **Municipal Advisor Registration**

State and local governments that issue municipal securities to raise funds for various public projects may rely on municipal advisors to advise them on the structure, timing and terms of the issuance of securities or the investment of proceeds from the sales. FINRA has found that some firms are not registering correctly with both the SEC and Municipal Securities Rulemaking Board (MSRB) or are not properly updating their registration information as it changes. Further, firms may not be identifying all individuals who are engaged in municipal advisor activity as required for submission to EDGAR on SEC Form MA-I. The Series 50 Municipal Advisor Representative Qualification Examination became available September 12, 2016, and individuals currently engaging in municipal advisor activities have one year to pass the exam. Firms that do not wish to register as municipal advisors may still provide services to municipal customers under certain statutory exclusions and regulatory exemptions. We will assess whether these firms properly apply the exemptions and exclusions<sup>3</sup> to municipal advisor registration requirements under SEC rules.<sup>4</sup>

## Market Integrity

### Manipulation

Detecting and deterring manipulation remains a critical priority for FINRA, and it should be a priority for firms too. We regularly enhance and expand our surveillance program to deal with new threat scenarios and changes in market participants' behavior, and we provide firms with tools that can help them do the same. For example, we are enhancing our layering<sup>5</sup> pattern to look for even larger groups of market participants potentially engaging in manipulation. In addition, we have amended our Order Audit Trail System (OATS) rules to require alternative trading systems (ATs) to submit broader order book activity to OATS and to require FINRA members to capture in their OATS reports the identity of non-FINRA member broker-dealers participating in the over-the-counter market. It is important that FINRA members comply with these new order reporting requirements as OATS data helps FINRA to better reconstruct the markets for surveillance purposes. In addition, we are closely monitoring whether market participants are trading in a potentially manipulative manner surrounding the open or close through the use of, among other tactics, aggressive and dominant trading on one side of the market to benefit a position on the other side of the market.

Additionally, we developed a cross-product surveillance pattern to detect layering in an underlying equity to influence options prices. In 2017, we will expand surveillance for cross-product manipulation to trading in ETPs and related securities, and improper trading strategies directed at unique attributes of ETPs.

Finally, in 2016, FINRA introduced the Cross Market Equity Supervision Report Cards for layering and spoofing<sup>6</sup> activity as a compliance tool to complement firms' supervisory systems and procedures to detect and deter manipulative conduct by the firm or its customers. The purpose of the report cards is to proactively alert firms when it appears that they or their customers are engaging in potentially manipulative conduct. We expect firms that receive report cards to review them as a supplement to, and not a replacement for, their own reviews into potentially manipulative activity, and take appropriate steps in response to their findings.

### Best Execution

In November 2015, FINRA issued *Regulatory Notice 15-46* to remind firms of the best execution obligations they owe customers when they receive, handle, route or execute customer orders in equities, options and fixed income securities. Firms should consider how the continuing automation of the markets for equity securities and standardized options, and recent advances in trading technology and communications in the fixed income markets, affect their order-handling decisions and factor those changes into their review of the execution quality they provide customers. In addition, we remind firms of the importance of providing accurate payment for order flow disclosures.

## **Audit Trail Reporting Early Remediation Initiative and Expansion**

FINRA's Audit Trail Reporting Early Remediation Initiative identifies and alerts firms to potential equity audit trail issues not typically detected through routine compliance sweeps and reviews. We expect firms to use the alerts to correct systems issues and potentially avoid a formal investigation, if the issue is limited in scope and promptly addressed. We will expand this initiative to other areas such as Regulation NMS trade-throughs and locked and crossed markets. We believe it would be a more effective use of both FINRA's and firms' resources to alert firms to potential problems and only open formal investigations when the problem is widespread and long-standing, or the firm does not take timely or sufficient steps to address the issues.

## **Tick Size Pilot**

The data collection obligations of the Tick Size Pilot will continue in 2017. To assist with this initiative, FINRA consolidates broker-dealer and exchange data to satisfy the exchanges' and FINRA's data collection requirements and, through a market maker transaction reporting mechanism, collects trade data on behalf of tick size market makers. Because of the importance of this data to the SEC's and self-regulatory organizations' analysis of the program, it is critical that firms submit accurate OATS and market maker data. FINRA will review for compliance with the data requirements of the Tick Size Pilot, as well as compliance with its quoting and trading restrictions.

## **Market Access Rule**

FINRA continues to see the need for firms to improve their compliance with the Market Access Rule. For example, firms need to better document their market access controls, provide the rationales for decisions relating to the setting of controls, identify the individuals responsible for monitoring those controls and consistently monitor the effectiveness of the controls they employ. Some best practices firms should consider incorporating into their market access controls include implementing, memorializing and monitoring pre-trade and post-trade controls; implementing procedures for the supervision, development, testing and employment of algorithmic trading, including code development or changes; and maintaining reasonable processes to monitor whether trading algorithms operate as intended, and processes to disable algorithms or systems that malfunction. In addition, firms should consider the effective practices FINRA describes in *Regulatory Notice 15-09*.

## **Trading Examinations**

FINRA's trading examination priorities include reviewing the adequacy of alternative trading systems' disclosures to customers about how they operate, reviewing for potential conflicts of interest, and evaluating whether floor brokers and upstairs firms are handling manual options orders in a manner consistent with their best execution obligations.

Our 2017 priorities include a pilot trading examination program. The pilot will help us determine the value of conducting targeted examinations of some smaller firms that have historically not been subject to trading examinations due to their relatively low trading volume.

## Fixed Income Securities Surveillance Program

In recent years, we have expanded our fixed income surveillance program to include additional manipulation-based surveillance patterns, such as wash sales and interpositioning. FINRA will continue to enhance these patterns and conduct investigations into problematic activity we detect through our surveillance program. We have brought enforcement actions against individuals who engaged in non-*bona fide* trading to create an artificial price level in a bond, in order to hide an excessive mark-up to a customer trade or reset the aging of positions held by the firm. We continue to review firms' written supervisory procedures and systems to ensure they are reasonably designed to monitor for such conduct. We also will continue to review for and investigate potential misrepresentations and misleading conduct by position and sales traders in securitized products.

In addition, with new TRACE reporting requirements for transactions in U.S. Treasury securities scheduled to become effective in July 2017, the development of a data integrity program to monitor the accuracy of the submitted data is a priority for FINRA. FINRA will also develop customer protection surveillance patterns focusing on compliance with rules applicable to U.S. Treasury securities, as well as patterns looking for abusive algorithms.

## Conclusion

FINRA urges compliance staff, supervisors and senior business leaders to consider the topics addressed in this letter. Using the information as part of firms' compliance, supervision and risk management practices can better protect investors, the markets and firms themselves. For our part, we will periodically provide insights into the topics addressed in this letter as well as evolving priorities. FINRA's website ([www.finra.org](http://www.finra.org)), conferences, *Regulatory Notices*, alerts and Weekly Update emails are all excellent sources of timely information and guidance. FINRA regulatory coordinators remain, of course, a key point of contact for firms. Finally, you can send suggestions on how we can improve this letter to Daniel M. Sibears, Executive Vice President, Regulatory Operations/Shared Services, at [dan.sibears@finra.org](mailto:dan.sibears@finra.org).

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## Endnotes

- 1 For information about cybersecurity effective practices and tools, see FINRA's 2015 [Report on Cybersecurity Practices](#) as well as FINRA's [Cybersecurity Topic Page](#).
- 2 See [FINRA December 21, 2016 News Release](#).
- 3 Statutory exclusions and rule-based exemptions from the municipal advisor definition relate to the market participant's activities, rather than registration status.
- 4 See <https://www.sec.gov/rules/final/2013/34-70462.pdf>.
- 5 Layering involves a trading pattern in which multiple, non-*bona fide*, limit orders are entered on one side of the market at various price levels away from the National Best Bid or Offer (NBBO) in order to create the appearance of a change in the levels of supply and demand, thereby artificially moving the price of the security. An order is then executed on the opposite side of the market at the artificially created price, and the non-*bona fide* orders are immediately cancelled.
- 6 Spoofing involves a trading pattern in which multiple, non-*bona fide* limit orders are entered generally inside the existing NBBO, with the intention of briefly triggering some type of market movement or response from another market participant, followed by cancellation of the non-*bona fide* orders, and the entry of an order on the opposite side of the market.