

FINRA Podcast
2017 Exam Priorities – Part 4

- SP Hello and welcome. I'm Steve Polansky.
- TC And I'm Tory Crane.
- SP This is the last in a four-part podcast series about FINRA's 2017 Regulatory and Examination Priorities Letter. This series gives a brief overview of the topics FINRA is focusing on in 2017, but it is not comprehensive. To get all the details, be sure to read the letter itself on our website.
- TC In previous episodes, we talked about recidivist brokers, sales practices, operational risks and financial risks, and the one remaining topic is market integrity.
- SP Let's start by talking about market manipulation. FINRA regularly enhances and expands its surveillance program to deal with new threats and behavioral changes. For example, in 2016 FINRA enhanced its layering pattern to look for even larger groups engaging in manipulation. Other examples include amending order-audit trail system rules to require alternative trading systems to submit broader order-book activity and more closely watching trading at the open and close.
- TC FINRA also provided a new tool to help firms detect and prevent manipulation by the firm or its customers. It's called the Cross Market Equity Supervision Report Card. The new report cards are sent to firms where FINRA identifies potential spoofing or layering by the firm or entities to which the firm is providing market access.
- SP Next up is Best Execution. In 2017, firms should consider how the continuing automation of the markets for equities and standardized options, as well as advances in trading technology and communications in fixed income, affect their order-handling decisions. And firms should provide accurate payment for order-flow disclosures. You can learn more about firms' obligations for Best Execution in Regulatory Notice 15-46 on our website.
- TC Now let's turn to the next topic, FINRA's Audit Trail Reporting Early Remediation Initiative. It alerts firms to potential equity audit-trail issues not typically detected through routine compliance sweeps and reviews. And FINRA expects firms to use the alerts to correct system issues and potentially avoid a formal investigation if the issue is limited in scope and promptly addressed. FINRA is expanding the initiative to other areas, like Regulation NMS trade-throughs and locked and crossed markets. FINRA believes it would be a more effective use of FINRA's and firms' resources to alert them to potential problems, and only open formal investigations when the problem is widespread and longstanding, or the firm does not take timely or sufficient steps to address the issues.
- SP FINRA also continues its Tick Size Pilot in 2017. It's critical to the Security and Exchange Commission's and self-regulators' efforts that firms submit accurate OATS

market maker data. FINRA is reviewing for compliance with the Tick Size Pilot's data requirements, as well as compliance with its quoting and data restrictions.

- TC In the next topic the letter highlights, FINRA continues to see the need for firms to improve their compliance with the SEC's Market Access Rule. The rule requires firms with access, or that provide access to trading securities directly on an exchange or alternative trading system, to have risk-management controls and supervisory procedures reasonably designed to systematically limit the firms' resulting financial exposure, and to ensure compliance with all applicable requirements. FINRA is looking for some key aspects of the rule at firms, including control documentation and rationales, as well as consistent monitoring of the control's effectiveness. The letter lists more best practices, like supervising algorithmic trading, so you can read it to learn more, or check out an even more extensive list of effective practices in Regulatory Notice 15-09.
- SP Another topic in the letter is Trading Examinations. FINRA is reviewing alternative trading systems to see if they are disclosing to customers how they operate. And FINRA is checking those systems for conflicts of interest and best execution. We are also doing a Pilot Trading Examination Program in 2017. It will help FINRA see if there is value in targeted examinations of some smaller firms that have historically not been subject to trading examinations due to their relatively low trading volume.
- TC And the last topic is a number of enhancements to FINRA's Fixed-Income Securities Surveillance Program. One is adding more manipulation-based surveillance patterns like wash sales and interpositioning. FINRA is continuing to investigate suspicious patterns and has brought enforcement actions against people who used non-bona fide trading to create an artificial bond price. In some cases, the motivation was a scheme to hide excessive markups or reset an aging position held by the firm. We are also continuing to review fixed-income written supervisory procedures at firms. And with new TRACE reporting requirements for U.S. Treasury securities effective July 2017, FINRA is prioritizing developing a data integrity program to monitor the submitted data's accuracy, as well as related customer protection surveillance patterns.
- SP And that about does it for our podcast series about FINRA's 2017 Regulatory and Examination Priorities Letter. Keep in mind, this series did not cover everything, so you can learn more by reading the letter itself on our website.
- TC We hope you found this podcast series helpful as a first step in learning what FINRA will focus on in 2017. If so, share it with your colleagues.
- SP And finally, for all of us at FINRA, thanks for listening.