

FINRA'S NEW MUSCLE - AMENDED RULE 8210

In December 2012, The Securities and Exchange Commission approved changes to FINRA Rule 8210, which became effective on February 25, 2013. While the changes may appear innocuous at first, they should prompt members to consider the potential expanded access FINRA will have to the records of affiliated entities, vendors, and the outside businesses of the registered representatives. Firms may need to reassess dual employee functions, service agreements, and management and affiliate expense sharing agreements.

The amended Rule significantly broadens FINRA's reach, specifically with regard to its access to books and records belonging to affiliated entities, affiliated persons, and entities owned and controlled by affiliated persons. As described in FINRA Regulatory Notice 13-06, the rule:

"...now specifies that FINRA staff and adjudicators have the right to inspect and copy information in the "possession, custody or control" of the member firm, associated person or person over whom FINRA has jurisdiction."

The key term here is "possession, custody or control." Quoting again from FINRA Regulatory Notice 13-06:

"...the amended rule requires firms, associated persons and other persons over whom FINRA has jurisdiction to provide records that they have the legal right, authority or ability to obtain upon demand."

The significance of this provision cannot be overstated: firms must produce documents that

"they have the legal right, authority or ability to obtain upon demand." The term "control" is construed very broadly.

The new rule also added Supplemental Material .01, which sets forth the broad scope of books, records, accounts and other documents that FINRA now states must be made available and would "ordinarily" be covered by an 8210 request. While it is helpful to get a glimpse of what is intended by FINRA, the broad language does little to limit what FINRA can demand.

Any firm with affiliates, management agreements, vendor agreements, or registered representative agreements, (i.e. virtually every broker-dealer) should begin reviewing these contracts to determine what they have legal authority to obtain from those counterparties. This may entail getting an attorney involved, and if so, it may be money well spent to avoid problems in the future. We suspect that there are many contractual rights that were nice to have before this change to 8210, which now may have to be reassessed.

Let's take this to the next level. Associated persons must also produce documents that "they have the legal right, authority or ability to obtain upon demand." The first scenario that comes to mind is an outside business that a registered representative owns or manages. The rule change appears to permit FINRA, for example, to request a wide range of documents relating to the investment advisory activities of dual registrants or independent broker-dealers that allow their registered representatives to operate their own registered investment adviser business. Even more intrusive could be requests by

Research Services

FINRA for registered representatives to provide documents relating to their other outside business activities that fall under FINRA Rule 3270, which in turn may impact the scope of a member's supervisory efforts.

Another issue that may not be immediately apparent is FINRA's access under the modified 8210 to a broker-dealer's *affiliates* through the ownership of a registered person. FINRA can demand documents from an affiliate through an 8210 request to a registered person, such as a CEO of a broker-dealer, who happens to own or control that affiliate.

In addition to the recommendation to review all of the member's contractual arrangements, firms should consider adding all contractual arrangements of associated persons to their review. It would be prudent to start with upper management and consider all dual employment roles, directorships and other business activities. Senior broker-dealer management should consider whether membership on Boards of affiliates or other entities poses any potential difficulties. For larger organizations, legal and compliance staff in affiliates should be made aware of FINRA's expanded powers so that they can independently assess the potential exposure or impact to unrelated legal entities.

In conclusion, the amendments to FINRA Rule 8210 can dramatically impact what documents FINRA can demand. Upon receipt of an 8210 request, FINRA members must not only carefully consider documents which have historically been responsive, but also what documents may be under the firm's possession and control or which they have the legal right, authority or ability to obtain upon demand. We believe that the requirement to search for and produce those documents could prove onerous.

Careful consideration of these issues now can save potential headaches in the future.

By: Harry Chaffee, CFA, CIPM

Harry Chaffee is the Director of Compliance Support Services for Renaissance Regulatory Services, Inc. He has over twenty years of regulatory and industry compliance experience managing, advising and auditing broker-dealers, investment advisers, funds, banks and bank holding companies relative to federal, state, and self-regulatory rules and regulations.

Mr. Chaffee can be reached in our main office.

Renaissance Regulatory Services, Inc.

Compliance Consultants

To Broker-Dealers and Investment Advisers

(561) 368-2245

350 Camino Gardens Blvd.

Suite 105

Boca Raton, FL 33432

www.RRSCompliance.com

Offices in:

Washington