# Bond Case Briefs

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## FINRA 2017 Exam Priorities Include MA Registration, Best Execution.

WASHINGTON – The Financial Industry Regulatory Authority's enforcement priorities for 2017 include ensuring municipal advisors are properly registered with regulators, checking broker-dealers' compliance with best execution requirements, and monitoring firms' efforts to avoid unsuitable recommendations of securities.

FINRA's new president and chief executive officer Robert Cook laid out the priorities in a letter released this week that he said is meant to give firms a framework under which to review their compliance and supervisory programs as well as address their internal training and communications. FINRA arrived at the priorities after taking input from member firms, regulators, and investor groups, among others.

Cook announced in the letter that, starting this year, FINRA will be publishing a report that outlines key findings from examinations in selected areas, after numerous prior requests for such summaries. The report will be designed to show firms what the self-regulator is seeing from a national perspective so that the firms can adjust their own processes, he said.

The letter said one of the enforcement priorities will be monitoring municipal advisor registration. FINRA is responsible for examining dealer MAs while the Securities and Exchange Commission examines non-dealer MAs.

"FINRA has found that some firms are not registering correctly with both the SEC and Municipal Securities Rulemaking Board or are not properly updating their registration information as it changes," Cook wrote in the letter. "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."

FINRA will be monitoring firms that choose not to register as MAs but still provide MA services under statutory exclusions or regulatory exemptions, like the exception given when an issuer has an independent registered municipal advisor, Cook said.

"We will assess whether these firms properly apply the exemptions and exclusions to municipal advisory registration under SEC rules," he said.

FINRA's examinations will also touch on best execution, a long-time requirement for taxable securities but something that only took effect for munis on March 21 of last year. MSRB Rule G-18 on best execution requires dealers, whether acting as agents or principals, to use "reasonable diligence" to determine the best market for a security and to then buy or sell the security in that market so the price for the customer is as favorable as possible under prevailing market conditions. The best execution standard does not necessarily mean a dealer must find the best price.

Dealers are exempted from the rule if their customer is considered a sophisticated municipal market professional under MSRB rules. The rule also does not apply to trades between dealers, but it covers trades that are cleared through other dealers.

“Firms should consider … how 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,” Cook wrote.

FINRA additionally will focus on concerns about the suitability of investments that Cook said can arise in connection with numerous products.

“Firms should make sure that they perform and supervise customer-specific suitability determinations,” he wrote. “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.”

One area of particular interest for FINRA over the last several years has been the over-concentration of Puerto Rico residents’ investments in closed-end funds that hold a significant amount of the commonwealth’s bonds. FINRA has found that some firms, including UBS, ignored investors’ risk profiles when concentrating investors’ assets into funds that held a lot of these increasingly risky bonds. When the commonwealth’s economy started its steep decline over the last few years, many of the investments suffered losses.

The largest FINRA award to date related to the failed investments from overconcentration was $18.5 million that went to two individuals. Mercedes Imbert De Jesus and Rafael Vizcarrondo had originally requested UBS pay more than $20 million over losses the two Puerto Rico residents experienced after investing in closed-end mutual funds concentrated in Puerto Rico bonds.

UBS has since challenged the $18.5 million arbitration finding in Puerto Rico federal court, arguing that the award should be vacated because two of the three individuals who sat on the FINRA arbitration panel had engaged in misconduct before sitting on the panel.

One panel member, Susan Meek, had not disclosed that a jury had found her guilty of fraud while the other, Frances Wright, did not disclose that she had been a lead plaintiff in a securities fraud class action, according to the UBS filing.

“Wright’s failure to disclose her involvement as a plaintiff in a securities fraud case similar to Vizcarrondo’s not only supports [vacating the finding and award] … but is strong evidence of partiality toward claimants in general,” UBS said in its filing. The bank added that Meek and Wright’s failures “prevented UBS from selecting a neutral and qualified panel to which it was entitled, and from receiving a fundamentally fair hearing.”

**The Bond Buyer**

By Jack Casey

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