



Professional Perspective

Digital Communications and FINRA 2020 Exam Priorities

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Digital Communications and FINRA 2020 Exam Priorities

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The Financial Industry Regulatory Authority's Annual Risk Monitoring and Examination Priorities [Letter](#) always provides a jolt of reality, as it signifies a roadmap of key compliance issues for firms to consider in advance of the exam cycle. At first glance, the 2020 letter includes a few topics that will come as no surprise to industry observers—the new Regulation Best Interest, LIBOR transition, and digital assets, among others. Also included is a general focus on communications via digital channels.

With over \$136,000,000 in fines levied globally for communication monitoring failures alone in 2019, it is no wonder that FINRA and other regulators are broadening their lenses to include the new electronic tools firms and their employees use to communicate. Despite appearing under Sales Practice and Supervision, digital communications has significant overlap with, and impact on, several other examination areas.

The exponential growth in the use of collaboration platforms like Zoom and Microsoft Teams have compliance implications for several priorities discussed in the letter, specifically, Regulation Best Interest, cybersecurity, and technology governance. This article examines FINRA's historical approach to digital communications, nuances of new collaboration platforms, and the impact of these applications across 2020 examination priorities.

Although FINRA does not explicitly mention this cross-pollination of digital communications, the connection must be explored to help broker-dealers develop stronger compliance programs and prepare for the 2020 examination cycle.

Digital Communications

FINRA is keenly interested in the risks of digital communications—from email and instant messaging to social media and encrypted chat applications like WhatsApp—given its focus on consumer protection and transparency. As the systems that financial professionals use to communicate with clients and the public evolve, so too must regulation to ensure they are not manipulated to mislead investors or disrupt markets.

In Oct. 2019, FINRA analyzed the risks of digital communications in its 2019 [Report](#) on Examination Findings and Observations, discussing collaboration applications for the first time. The issues FINRA uncovered during 2019 exams paved the way for deeper engagement on the topic in 2020. To understand 2020 priorities, a brief review of FINRA's historical approach to electronic communications and the 2019 report.

FINRA and Securities and Exchange Commission rules require the capture and retention of broker-dealer “business as such” communications under SEC Rules 17a-3 and 17a-4, and FINRA Rule 4510. And, not only must firms identify and capture these electronic business communications, they must also supervise them, according to FINRA Rule 3110, and store them in “non-rewritable, non-erasable” storage, as described in SEC Rule 17a-4(f). In addition, Rule 17a-4(f) includes a host of notification, documentation, and audit requirements that have serious implications for technology governance and vendor management. Selecting and onboarding a communication platform at a regulated broker-dealer is no small feat.

Over the last 20 years, FINRA evolved its definition of electronic communications, gradually expanding the term “communication” to include email, instant messaging, SMS, social media, and, now, collaboration tools. FINRA and SEC views on communications were forced to advance as email challenged pen and paper as the dominant form of client communication.

Over time regulators have tried to square new communication tools like SMS and social media with the notion of a one-to-one written letter. The ascendance of platforms like Zoom and Cisco Webex as well as WhatsApp and WeChat are prompting further transformation of regulators' conceptions of digital communications. Now “communications” are not simply written words, but could extend to information exchanged over video, whiteboards, webcams, and file transfers.

New, genre-bending applications pose unique challenges for regulators who must consider how they fit into existing rule frameworks. And, whether FINRA has mentioned a particular platform by name in a given letter or notice is irrelevant—the regulator will want firms to take a practical approach to reviewing new digital communications systems and enable required controls regardless. As a result, regulators must continuously assess the technology landscape to understand how member firms are using new tools.

Collaboration platforms, in particular, have introduced new and novel types of risks for financial services firms. With applications like Zoom, Cisco Webex, and Microsoft Teams, users can set up dial-ins for phone meetings, exchange documents, and chat, as well as hold videoconferences, share desktops, engage in virtual whiteboarding sessions, and use webcams to display information. The rich feature sets of these collaboration tools has prompted FINRA's interest.

FINRA first put firms on notice that collaboration tools were considered regulated communications in the 2019 report, which stated that if "a firm permits its associated persons to use a particular application—for example, an app-based messaging service or a collaboration platform—the firm must preserve records of business-related communications and supervise the activities and communications of those persons on the application."

These comments in the 2019 report are a definitive statement on the status of collaboration platforms—FINRA made it clear that applications like Zoom and Webex fall squarely within recordkeeping and supervision mandates. In the 2019 report, FINRA also observed that firms needed processes for detecting and preventing use of platforms that could not be supervised.

Jump ahead, and digital communications appear front and center in the 2020 letter. At the outset, FINRA notes "Firms', registered representatives' and customers' use of an increasingly broad array of digital communication channels (e.g., texting, messaging, social media or collaboration applications) may pose challenges to firms' ability to comply with obligations related to the review and retention of such communication." FINRA highlights several important considerations to prepare firms for 2020 exams, including evaluating new communication tools to ensure they meet retention and supervision requirements, testing and monitoring the proper functioning of collaboration tools, and detecting improper use of collaboration applications.

As firms deploy applications like Teams, Webex, or Zoom, they must be mindful of how they do so in compliance with SEC and FINRA rules. The new communication functionalities of these systems pose unique technology and compliance challenges. In parallel, a small group of innovative technologies are emerging to help firms align with regulatory expectations by offering tools to analyze the risks in video and audio data to facilitate retention and supervision of these new content types at scale. Without supporting compliance and oversight mechanisms, firms face challenges in developing a comprehensive strategy for deploying collaboration platforms.

Compliance teams must FINRA comply with the digital communication guidance FINRA provides, and they must also understand how digital communications intersect with FINRA's other 2020 examination priorities. Looking at the compliance issues related to digital communications and collaboration platforms in isolation misses the forest for the trees.

Regulation Best Interest

Given significant SEC efforts around the development and implementation of [Regulation Best Interest](#)—the new standard of conduct for securities transactions and investment strategies—it is absolutely no surprise to see it front and center as a priority for 2020. While exams in the first part of the year will focus on how firms have prepared for Reg BI by surveying policies and procedures, post-implementation exams will delve deeper into details of compliance with the rule.

Although requirements like the delivery of Form CRS and developing tailored trainings are important, the true test for firms will be the manner in which they provide investment advice to clients and if that advice comports with Reg BI mandates. So, for example, did a financial professional exercise "[reasonable diligence, care, and skill](#)" when offering transactional or strategic advice?

The complexity here is that, based on recent [SEC FAQs](#), the content of any given investment conversation is determinative for the applicability of Reg BI, not its form. The SEC stated, whether "your communication is subject to Regulation Best Interest depends on whether you make a 'recommendation,' not on the location or setting of the communication." Put more bluntly, a conversation—via Zoom, Webex, or even at a baseball game or barbecue—will fall into Reg BI territory if it constitutes a recommendation under the Rule regardless where or how it happens.

As firms use collaboration tools to supplement and, in many cases, replace face-to-face conversations with clients, they must ensure that conversations conducted on those platforms also comply with Reg BI. Firms looking to demonstrate Reg BI compliance on a programmatic basis are evaluating and implementing these new supervisory technologies. As mentioned above, new applications are available to enable firms to implement technical controls on collaboration platforms to determine what was spoken, shown, or shared, during a conversation.

Since the essence of Reg BI compliance lies in how financial professionals discuss their product and service offerings, a holistic Reg BI strategy must consider the platforms employees will use to conduct these conversations. Firms must be careful about the procurement and use of new digital communications tools—not only must applications align with existing recordkeeping and supervision requirements, they must facilitate Reg BI compliance as well. Thinking about digital communications in isolation will lead to gaps in a firm's Reg BI compliance program.

Cybersecurity

Cybersecurity has been included in Exam Priorities Letters for years, and as financial activity migrates to online and digital platforms, it will remain a core priority for the foreseeable future. Protection of customer information, particularly in the context of [Regulation S-P Rule 30](#), is highlighted in the 2020 letter. The SEC also considers cybersecurity an important issue as evidenced by a series of OCIE Risk Alerts dating back to 2014 and, most recently, in a set of examination [Observations](#) that reinforce relevant governance, technology, and vendor management risks.

By way of brief background, Reg S-P Rule 30 requires firms to develop policies and procedures to address administrative, technical, and physical safeguards to protect customer information. Although historically Reg S-P has not been invoked as an enforcement mechanism, 2018 saw the [SEC reach its first Reg S-P-related settlement](#) with Voya Financial Advisors, Inc. for violating both Reg S-P and Reg S-ID. Firms are now on notice that violations of these Regs, which are rooted in cybersecurity controls related to protecting the confidentiality, availability, and integrity of customer information, are core to the SEC and FINRA's missions. The Reg S-P reference in the 2020 letter is a shot across the bow, of sorts.

Again, the conceptual linkage between cybersecurity and digital communications is strong, but isn't mentioned explicitly by FINRA. As discussed above, Webex, Teams, and other collaboration tools have made conversations and information sharing easier and more efficient. Not only can collaboration tools be leveraged for one-to-one or one-to-many conversations, participants can exchange spreadsheets and documents containing financial data, share desktops, create virtual whiteboards to discuss investment strategies, and use native chat features to conduct ad hoc conversations. Given the depth of these functionalities, the implementation of new collaboration tools must account for and guard against potential cybersecurity risks like the exfiltration and leakage of confidential and proprietary customer and firm data.

Any basic information security policy will discuss cybersecurity controls related to data classification, protection, and use. Similarly, a comprehensive cybersecurity strategy for technology assessment must address these concerns as well. The rise of data breaches from Equifax to Capital One have heightened concerns about data protection, particularly in the financial services sector. FINRA will expect to see documented protocols and measures for considering and managing cybersecurity concerns when selecting and deploying digital communication platforms during 2020 exams.

Technology Governance

FINRA includes technology governance on its list of operational priorities for 2020 and, again, there are connections between this priority and digital communications that must be considered.

FINRA reiterates Supervision Rule 3110 as well as SEC Rules 17a-3 and 17a-4 on electronic recordkeeping at the outset of the section. As with Reg BI and cybersecurity, the link between technology governance and digital communications isn't explicit, but the references to these Rules should give compliance officers pause about the probable depth and breadth of 2020 examinations. Compliance teams should continually assess and strengthen technology governance pertaining to new electronic communications platforms to ensure that they align to meet relevant SEC and FINRA rules. Moreover, technology governance must also incorporate related privacy and security mandates like those under the GDPR, the CCPA, and the NYDFS Cybersecurity Rule.

From a practical perspective, considering the broad compliance and technology considerations of deploying new communication platforms are essential to technology governance processes. Since the SEC's electronic recordkeeping rules proscribe specific storage criteria, ensuring that collaboration platforms are compatible with record keeping requirements is key. Moreover, SEC requirements for firms to notify their designated examining authority in advance of deployment and appointment of a third party to access and download information on the firm's behalf reinforce that robust governance processes must be established to meet compliance requirements. Furthermore, ensuring that collaboration tools can be supervised in a manner deemed satisfactory under Rule 3110 must factor into technology oversight as well.

A nuanced technology governance process must be built with digital communication compliance requirements in mind. It seems likely that FINRA will consider how firms are managing the selection, and deployment, and maintenance of new collaboration tools during 2020 exams.

Conclusion

Taking a hard look at FINRA's 2020 letter demonstrates that one of the major challenges facing compliance teams will be the assessment, implementation, use, maintenance, and supervision of new digital communications channels. Although discussion of these tools is isolated in a single section of the report, the practical ramifications of their use ripple throughout the Reg BI, cybersecurity, and technology governance sections.

Compliance teams should ensure that they have broad, inter-disciplinary coverage to manage the appropriate deployment and oversight of new systems like Microsoft Teams and Zoom as their advisers, representatives, and other regulated staff use them to communicate with clients and prospects. Digital communications can create significant risks across different business units within an organization, and FINRA will likely devote substantial efforts to exploring and testing these interconnected risks during the 2020 examination cycle.

Firms should take a long, hard look to honestly assess if they are doing enough to address record keeping and supervision of their digital communication stack to pass a meaningful exam assessment, because that test will happen in 2020.