



May 2017 – Hot Topics

Recent developments that have become, or will likely become, hot buttons.

Rule 3210 – defining the undefinable – because so many of you have asked

Effective April 3, 2017, FINRA Rule 3210 became effective (replacing FINRA Rule 3050) and confusion reigned. The Rule:

- requires all associated persons of the broker dealer to obtain prior written consent of the firm when opening a brokerage account at another broker dealer or financial institution and;
- adds categories of persons subject to FINRA rule 3210 based on beneficial interest.

Rule 3210 specifies the types of accounts in which Associated Persons are perhaps rebuttably presumed to have a beneficial interest, those being:

- the spouse of the associated person; or
- a child of the associated person or of the associated person's spouse, provided that the child resides in the same household as, or is financially dependent upon, the associated person

The Rule treats the following accounts as being subject to its requirements because of their control aspects:

- any other related individual over whose account the associated person has control; or
- any other individual over whose account the associated person has control and to whose financial support the associated person materially contributes.

While FINRA has published FAQs, please see [here](#), we note that they don't seem to cover many possibilities. Examples of these are:

- Associated persons with multiple spouses (is “spice” the plural form of “spouse”?)
- Associated persons who are legally separated from their spouses
- Antagonistic spouses who refuse to be cooperative and who are not subject to FINRA jurisdiction
- Associated persons who have “significant others” but are not married to them
- Etc.

Cybersecurity

The hacking events of the past few days highlight the importance of every firm having cybersecurity policies and procedures. At a minimum, every firm should designate a cybersecurity person, a go-to person for all matters related to hacking, identity theft, lost internet-connected equipment, etc. Additionally, all firms should update their Written Supervisory Procedures as applicable. While large firms will already have such persons in place, many small firms have not yet considered this to be an issue. Please call us to discuss further.

Examiner techniques and priorities

o The Dreaded PAQ

Many of us have been confronted with examiners who aggressively look for certain exceptions. These low-hanging fruit exceptions are annoyances that are often preventable. One technique they use is to ask selected associated persons to complete a Personal Activity Questionnaire which calls for listing securities trading accounts, non-firm email addresses, outside activities and other information. Often the end result of the examiners looking at this information is to determine that the individual has not notified his or her firm about the subject of the requested information. The impact of the examiner queries can be thwarted very simply by **pre-emptively** distributing a similar questionnaire to associated persons. By gathering the information ahead of examiner requests, by the time examiners ask for the same information, the firm's records will be thoroughly complete and up-to-date. It's perfectly OK to frustrate the examiners who should be happy that they are examining a firm that is compliant.

o The OBA problem

FINRA does not define it very well. Form U4 has an item 13 which calls for listing **Other** business activities, which means activities that are not listed as employment in item 12. On the other hand, FINRA Rule 3270 speaks in terms of **Outside** business activities, meaning activities that are outside of a subject member. The terms are not synonymous and examiners regularly confuse the two.

o Rules and Guidance – Vive La Difference

Occasionally examiners have difficulty separating rules from guidance. Guidance is meant to be of a general nature and can and should apply to many firms. On the other hand, rules apply and must be followed unless they contain an exemption. A perfect example is NASD Notice to Members 06-23, which contains guidance about FINOPs visiting the firms. The NtM was written in an era long before people were able to work virtually. As an example, we have people who work for us who haven't been in our office for many months. The guidance is outdated but FINRA examiners persist in thinking that it should be followed even though it is not a rule.

We have looked for a CAB but we haven't seen one

Like many others in our industry, we have advised our clients not to become a Capital Acquisition Broker. All of our clients have listened to us. We're delighted. Call us before you take the plunge into a CAB [here](#).

Tax consequences everyone should care about

The following is not meant to be tax advice but merely a suggestion that a certain fact pattern may necessitate further discussions with tax advisors and preparers.

Lately, we've discovered that often broker-dealers do not necessarily communicate certain necessary information with the professionals who prepare their tax returns. In particular, the breakdown of taxable income for state and local tax purposes is often overlooked since many companies do not bother to record income in their ledgers in a manner that gives consideration to such analysis.

For example, for tax years beginning January 2015, New York State and City reformed their respective **corporate** tax laws (this does not apply to LLC's and partnerships) such that the source of revenue rather than the physical location of the office from which services are provided now defines how those jurisdictions tax the income. Simply put, if a corporate broker-dealer earns money in New York State but the source of the revenue is from a non-New York (even an overseas) location, effectively the revenue would not be taxed by New York State. New York City utilizes a three factor formula for its allocation percentage, however that will be phased down to a single factor (based solely on revenues) in 2018.

The state and local tax laws have become considerably more complex. The end result is that corporations may be subject to unanticipated positive or negative taxation results in various locales.

Some of our clients have amended prior returns to obtain overpayments of their taxes. One of them is expecting a seven-figure refund. That's significant!

Updates for Written Supervisory Procedures – summer is always a good time to update your WSPs or determine whether your firm's operations need additional policies and controls. Please contact us if we may assist you in any way.

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