



Report on Use of 2018 Fine Monies

FINRA is a not-for-profit, self-regulatory organization (SRO) dedicated to promoting investor protection and market integrity in a manner that facilitates vibrant capital markets. One of FINRA’s tools for achieving this objective is fair and effective enforcement of our member firms’ compliance with securities laws and regulations.

FINRA’s highest priority when it identifies misconduct is to seek restitution for harmed investors. However, like many other self-regulatory organizations in the securities industry, FINRA also imposes fines on its member firms to discourage further misconduct. For FINRA, fine amounts are based on public, pre-established [sanction guidelines](#) and the facts and circumstances of the individual case. FINRA does **not** target any minimum amount of fines to be issued. FINRA’s [operating budget](#) does not include fines, and fine monies are not considered in determining employee compensation and benefits.

FINRA’s use of fine monies is governed by FINRA’s [Financial Guiding Principles](#) (Principles), which we first published in January 2018 to provide more transparency about how we manage our financial resources to ensure we fulfill our regulatory responsibilities and further our mission. FINRA’s Board reaffirmed the Principles in December 2018. As the Principles describe, FINRA accounts for fine monies separately, and any use of such monies is approved, separately from other expenditures, by the Board or its Finance, Operations and Technology Committee (Finance Committee). The Board or the Finance Committee may authorize the use of fine monies only for one of four enumerated purposes:

- > capital initiatives or nonrecurring strategic expenditures that promote more effective and efficient regulatory oversight by FINRA (including leveraging technology and data in a secure manner) or that enable improved compliance by member firms;
- > activities to educate investors, promote compliance by member firms through education, compliance resources or similar projects, or ensure our employees are highly trained in the markets, products and businesses we regulate;
- > capital initiatives required by new legal, regulatory or audit requirements; or
- > replenishing reserves in years where such reserves drop below levels reasonably appropriate to preserve FINRA’s long-term ability to fund its regulatory obligations.

Under the Principles, FINRA also makes public a description of the use of fine monies approved by the Board or its Finance Committee during the prior year. This report describes the Board-approved initiatives that were supported by 2018 fine monies.

Summary

FINRA issued \$61.0 million in fines in 2018, and the FINRA Board has determined that there were \$81.1 million in fines-eligible expenditures in 2018 (*i.e.*, capital initiatives, strategic expenditures and other activities eligible to be funded by fine monies based on the criteria set forth above). Because the total of fines-eligible expenditures exceeded the amount of fines issued in 2018, the balance of \$20.1 million was funded from FINRA’s reserves.

:
Fines-eligible expenditures funded by 2018 fines issued
:
\$61.0 million
:
Fines-eligible expenditures funded by reserves

:
\$20.1 million
:
Total 2018 fines-eligible expenditures funded by fines and reserves
:
\$81.1 million

The 2018 fines-eligible expenditures fall under two broad categories that align with the purposes set forth in the Principles:

Initiatives supported by fines and reserves

:
Capital initiatives or nonrecurring strategic expenditures that promote more effective and efficient regulatory oversight by FINRA (including leveraging technology and data in a secure manner) or that enable improved compliance by member firms, and capital initiatives required by new legal, regulatory or audit requirements.
:
\$65.7 million
:
Activities to educate investors, promote compliance by member firms through education, compliance resources or similar projects, or ensure our employees are highly trained in the markets, products and businesses we regulate.
:
\$15.4 million

The fines-eligible expenditures within these categories, which are described in more detail below, furthered FINRA's goals to implement efficient oversight programs that protect investors and the markets, modernize critical securities industry infrastructure, strengthen our ability to track trading across markets, enhance our risk-based analytics to better inform examinations and investigations, enhance the efficiency of FINRA systems, facilitate compliance by member firms and equip investors with knowledge and resources to help them navigate ever-evolving markets, products and services. Some of these projects are ongoing, multi-year initiatives that have extended into 2019 and, in some cases, will continue into future years.

Capital Initiatives and Strategic Expenditures

Modernizing Securities Industry Infrastructure Administered by FINRA

FINRA administers a number of technology systems that support the regulation of brokers and their firms by FINRA, as well as the U.S. Securities and Exchange Commission (SEC), state regulators and other SROs. As the brokerage industry undergoes rapid change, FINRA must ensure that these systems are optimized to adapt to the evolving marketplace. In 2018, we allocated \$25.7 million to initiatives to modernize several systems we administer.

- > *Enterprise Cloud Migration*—FINRA invested \$16.0 million to migrate various technology applications from existing FINRA-managed data centers to cloud-based platforms. Since 2013, FINRA has used cloud-based infrastructure to increase the effectiveness and efficiency of our Market Regulation programs and reduce operating costs. We are continuing to migrate more FINRA applications to the cloud to reduce the long-term costs of maintaining our own data centers and improve our ability to add data processing and storage capacity as necessary.
- > *Registration, Testing and Continuing Education Systems*—In 2018, FINRA [launched](#) a multi-phased effort to overhaul its registration and disclosure programs, including the Central Registration Depository (CRD) system, the central licensing and registration system for the U.S. securities industry and its regulators. The transformation, which is expected to be complete in 2021, is intended to increase the utility and efficiency

of the registration and disclosure process for firms, investors and regulators, and to reduce compliance costs for firms. FINRA invested \$9.7 million to transform the legacy registration systems to modern systems that use an open source architecture and cloud-based infrastructure, and support CRD enhancements tied to the restructuring of the exam qualification and registration program. We also launched the Securities Industry Essentials exam, the restructured representative-level registration exam, and implemented registration rule harmonization. Enhancements of the Registration and Disclosure, Testing and Continuing Education, and Dispute Resolution systems and corporate websites were also undertaken or completed.

Strengthening Regulators' Ability to Track Trading Across Markets

FINRA has developed a comprehensive regulatory audit trail as an essential part of our work to monitor the integrity of the markets. FINRA's systems processed on average 66.7 billion equity, options and fixed income market events per day in 2018 and generated billions of additional derived market events by standardizing trading activity across the markets. This included spikes in volume as high as 135 billion records in a single day, and sustained activity averaging more than 100 billion records per day for weeks at a time.

With the foundation provided by our regulatory audit trail, in 2018 FINRA conducted cross-market surveillance for approximately 99 percent of all trading in U.S.-listed equities markets and 50 percent of all trading in U.S.-listed options. FINRA is also responsible for the surveillance of the unlisted equity market and fixed income instruments that trade in the over-the-counter market, and conducts examinations and investigations to identify potential market manipulation or other misconduct. In 2018, we allocated \$25.6 million to a range of initiatives to strengthen the ability of FINRA and other regulators to monitor equity market activity and to expand the audit trail for Treasury securities.

- *Market Surveillance Patterns and Reviews*—FINRA invested \$11.8 million to enhance the sophisticated computer programs or “patterns” that we use to detect a wide variety of compliance issues and suspicious conduct across markets, and to enhance our reviews of the results of those patterns. We enhanced existing fixed income patterns to address new and updated FINRA rules and Municipal Securities Rulemaking Board rules. We also migrated fixed income patterns to FINRA's MarketSpace platform in response to a recommendation from the SEC's Office of Compliance Inspections and Examinations. We enhanced existing equity patterns to improve our surveillance of the markets and to address new and updated rules. In addition, we automated examination reviews, implemented a cognitive surveillance program and expanded our use of “machine learning,” where we use algorithms that “train” themselves to identify specific instances of behavior of interest—as well as additional instances in new data sets—and that are informed by surveillance analysts reviewing their output.
- *Trade Reporting for Treasury Securities*—FINRA invested \$5.8 million in the continuing implementation of and ongoing support for the reporting of trades in Treasury securities to FINRA's Trade Reporting and Compliance Engine (TRACE), as well as FINRA's surveillance of the Treasuries market. FINRA implemented the Treasury securities reporting program in 2017 in response to a request by the U.S. Department of the Treasury and the SEC.
- *Case Management*—FINRA invested \$4.2 million to support the ongoing modernization of the platform we use to manage Market Regulation cases from the initial alert FINRA receives to its ultimate disposition. These changes will improve FINRA's ability to conduct repeatable and accurate yield tracking of the surveillance program.
- *Reporting to/Use of Consolidated Audit Trail Data*—In 2018, FINRA invested \$2.0 million to comply with requirements that it report certain data to the Consolidated Audit Trail (CAT), the SEC-mandated system to track orders throughout their life cycle and identify the broker-dealers handling them. The costs also include investments necessary for FINRA to comply with requirements that it use CAT data for the first phase of the implementation of CAT. (These investments and others described herein do not include expenses related to FINRA's membership in the CAT consortium or its selection or performance as the plan processor of the CAT.)
- *Trade Transparency Systems*—FINRA invested \$1.8 million in trade transparency systems. This included work related to improvements to the Multi Product Platform (MPP), which facilitates the gathering and dissemination of trade execution and quotation data that will support a multi-year initiative to upgrade the platform to better handle current market requirements at reduced costs. FINRA's investment in this area

also supported the implementation of FINRA Bond Facts, an investor-focused bond website that combines bond-specific data, including recent trade data, with bond education materials.

Enhancing FINRA's Risk-Based Analytics to Better Inform Examinations and Investigations

Examinations are central to FINRA's regulatory operations, and they are one of the principal means by which we work to protect investors and promote market integrity. FINRA has continuously worked to improve the effectiveness and efficiency of our examination program, and in 2018, we invested \$12.0 million for improvements to the program. The multi-year initiatives include projects to enhance our framework for examinations and investigations, better align our finite resources with the risks and business practices of our member firms, and better identify the brokers and firms that may present the greatest risk to investors and the markets.

- > *Examination and Risk Monitoring Management Platform*—FINRA invested \$8.5 million to enhance the technology that supports the examination and risk monitoring platform FINRA examiners and regulatory coordinators use to manage their work efficiently. We further streamlined the management of documents and communications related to member firm examinations, enhanced the reporting and search functions that enable us to more readily identify risks, and enhanced the Regulatory Extension (REX) system, which is used to process requests made by member firms for extensions of time to meet margin requirements under Regulation T, SEA Rule 15c3-3 and FINRA Rule 4210.
- > *Enforcement Tools*—FINRA invested \$2.0 million to update the tools used to manage work efficiently under the new, unified Enforcement structure—including a new integrated document management system—and initial work to develop more robust case management and reporting systems.
- > *Examination Analytic Tools*—FINRA invested \$1.5 million to enhance the data analytics program we use to sort and understand the implications of the data we collect, including information about business models and industry relationships, trading activity, disciplinary history, and other disclosures made to FINRA or the public.

Improving FINRA Filing Systems for Member Firms

FINRA helps facilitate member firms' compliance with FINRA rules and the federal securities laws by reviewing documents related to firms' capital-raising activities and arrangements. In 2018, we invested \$2.4 million to improve certain document-review systems on FINRA's external-facing digital platform. These include the Advertising Regulation Electronic Files (AREF) System through which firms submit communications with the public, as well as the corporate financing systems through which firms submit documents related to firms' capital-raising activities and arrangements.

Education, Compliance Resources and Training

Educating Investors

An important part of FINRA's work involves providing investors with unbiased information, tools and resources that can equip them to make informed decisions about their assets and the investment professionals with whom they work. In 2018, we invested \$3.5 million in various investor education programs.

- > *Investor Education Programs*—In 2018, FINRA created, updated and syndicated digital and print publications, and enhanced existing interactive tools, including [BrokerCheck](#). In addition, FINRA delivered in-person education through outreach efforts ranging from widely attended forums to one-on-one assistance. We also leveraged earned media and no-cost social media channels to drive traffic to educational tools and resources.
- > *FINRA Investor Education Foundation*—Throughout the year, FINRA provided management oversight and program and administrative support to the FINRA Investor Education Foundation to carry out its financial capability-building initiatives.* The Foundation undertook a wide variety of projects in 2018. For example, the Foundation's *Thinking Money* exhibition successfully concluded its two-year national library tour, providing nearly 360,000 youth and adults with interactive financial education experiences in 50 communities across the country. In addition, among a wide array of research initiatives, staff fielded, released and disseminated a new study titled "[Uncertain Futures: 7 Myths About Millennials and Investing](#)," debunking common assumptions about millennial investors and exploring the financial attitudes

and behaviors of this important demographic. Staff also continued to lead innovative projects to bring low-income workers into the financial mainstream and to help vulnerable investors avoid fraud.

**Note: The direct program costs of the FINRA Foundation are funded from the assets of the Foundation, rather than from fine monies or reserves.*

Helping Firms Comply With Rules

In 2018, FINRA spent \$7.3 million in part to fund operations and support for various tools and resources to help improve compliance by the firms and individuals it regulates. For example, FINRA continued to offer conferences and educational programs, regional member forums, boot camps and outreach events. Highlights include FINRA's Annual, Small Firm and Fixed Income Conferences, the FINRA Institute at Georgetown Certified Regulatory and Compliance Professional (CRCP)[®] program, as well as newer topic-based conferences focusing on cybersecurity and registration and disclosure, as well as half-day seminars on anti-money laundering (AML). FINRA also invested in developing additional compliance tools and resources for firms—such as enhancements to the Compliance Vendor Directory and the introduction of the Peer-2-Peer Compliance Library—as well as ongoing call center support for questions from broker-dealers, individual brokers and the investing public.

Training FINRA Examination Staff Regarding the Markets, Products and Businesses That FINRA Regulates

FINRA continues to expand the training it provides to staff, including examiners, to ensure staff is prepared for new regulatory challenges. In 2018, we spent \$4.6 million on regulatory-focused training, including training programs for Member Supervision and Market Regulation staff.

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