# Securities Regulation Daily Wrap Up, TOP STORY—Robinhood hit with $70M in sanctions in largest-ever FINRA penalty, (Jun. 30, 2021)

Securities Regulation Daily Wrap Up

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FINRA found that the FinTech firm communicated misleading information to millions of customers, including misrepresenting their ability to trade on margin and the risks of options trading.

FINRA has fined Robinhood Financial LLC $57 million and ordered the broker-dealer to pay almost $13 million in restitution for distributing false and misleading information to customers and failing to supervise critical technology, among other FINRA rule violations. In levying the largest financial penalty ever imposed by the SRO, FINRA stated that the sanctions reflect the scope and seriousness of Robinhood's violations, which affected millions of customers. In executing a Letter of Acceptance, Waiver, and Consent, Robinhood neither admitted nor denied the charges but consented to the entry of FINRA's findings (*In re Robinhood Financial LLC*, No. 2020066971201, June 30 2021).

"This action sends a clear message—all FINRA member firms, regardless of their size or business model, must comply with the rules that govern the brokerage industry, rules which are designed to protect investors and the integrity of our markets. Compliance with these rules is not optional and cannot be sacrificed for the sake of innovation or a willingness to 'break things' and fix them later," said FINRA Department of Enforcement head Jessica Hopper in a news release.

The FINRA enforcement action reflects the latest in a series of regulatory setbacks for the broker-dealer. In December 2019, FINRA fined Robinhood $1.25 million for best execution violations related to its customers' equity orders and related supervisory failures. One year later, in December 2020, Robinhood agreed to pay $65 million in penalties to settle SEC charges that the firm failed to disclose to customers that it took higher payments for order flow while giving customers inferior prices for their orders when compared to the competition.

Robinhood currently faces charges from the Massachusetts Securities Division that the firm violated the state's fiduciary duty rule by aggressively marketing itself without regard for the best interests of its customers. In the first enforcement action brought under the new rule, Massachusetts regulators have accused Robinhood of employing aggressive tactics to attract new and inexperienced investors while also using "gamification" and other manipulative strategies to entice investors to make continuous use of Robinhood's mobile trading application.

**Misleading information.** Headquartered in Menlo Park, California, Robinhood offers commission-free, self-directed trading for retail investors through its mobile applications and website. The firm, which launched online trading in December 2014, has over 31 million customer accounts serviced by approximately 770 registered representatives and six branch offices.

FINRA alleged that despite Robinhood's self-proclaimed mission to "democratize and de-mystify finance for all," the firm violated FINRA Rules 2010, 2210, and 2220 by negligently communicating a "wide array" of false and misleading information to its customers during certain periods since September 2016.

For example, FINRA found that Robinhood falsely told its "Robinhood Instant" customers that they had to upgrade to "Robinhood Gold" to trade on margin when, in fact, Robinhood allowed "Instant" customers to place options trades that could trigger the use of margin. Robinhood also falsely told "Robinhood Gold" customers that they could "disable" margin in their accounts even though the firm allowed "Gold" customers to place options trades that could trigger the use of margin even after they had "disabled" margin.

FINRA further alleged that Robinhood provided false information to customers about the risks associated with certain options transactions, such as telling customers that they would "never lose more than the premium paid" to enter a debit spread when customers could, in fact, lose vastly more than the premiums they paid. In addition, Robinhood displayed inaccurate cash balances to certain customers and issued erroneous margin calls and warnings to others, telling them that they were in "danger of a margin call" when they were not.

**Option account approval bots.** FINRA also found that Robinhood failed to exercise due diligence before approving customers to trade options. Although Robinhood's written supervisory procedures assign registered options principals the responsibility of approving accounts for options trading, in practice, the firm has relied heavily on computer algorithms—known as "option account approval bots"—to carry out the process. Among other problems, the bots were programmed to approve options trading based on inconsistent or illogical information, including approving trading for customers under 21 years old but who claimed to have had more than three years' experience trading options.

The option account approval bots also approved certain customers with a low risk tolerance for options trading, contrary to prohibitions in the firm's written procedures, and were programmed only to take into account the most recent information provided by customers. As a result, Robinhood approved for options trading customers whom it had previously rejected for options trading—often only minutes earlier, according to FINRA.

The Letter of Acceptance, Waiver, and Consent is No. 2020066971201.

Companies: Robinhood Financial LLC

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