

July 12, 2019

FINRA Provides Supplementary Guidance on Credit for “Extraordinary Cooperation”

On July 11, 2019, the Financial Industry Regulatory Authority (FINRA) issued [Regulatory Notice 19-23](#) (the Notice) “to restate and supplement” existing guidance on the circumstances under which it would award credit for “extraordinary cooperation” in connection with enforcement investigations. As its “restate-and-supplement” language suggests, the Notice does not materially alter the factors that FINRA will consider when deciding whether and how much credit is warranted in a particular case. Rather, the Notice is designed to bring increased transparency as to how FINRA evaluates those preexisting factors by, among other things, citing examples of recent matters where extraordinary cooperation credit was given, and to further contrast the cooperation that is required and expected of all member firms as a matter of course with cooperation that would qualify as “extraordinary” such that it would impact the outcome of an investigation.

I. Background

Prior to this Notice, FINRA had not issued comprehensive guidance regarding cooperation credit since 2008. The Notice acknowledges that subsequent rule changes, including the enactment of FINRA Rule 4530(b), which requires member firms to self-report internal conclusions regarding violations of certain laws, rules, regulations, or standards of conduct, “may have created uncertainty around the continued impact that self-reporting may have on a potential respondent’s ability to receive credit for extraordinary cooperation.” The Notice attempts to provide further clarity on this subject.

II. Factors for Receiving Cooperation Credit

The Notice addresses the four categories of factors that FINRA considers when determining whether credit will be given for extraordinary cooperation, including (1) taking steps to correct deficient procedures and systems; (2) providing restitution to consumers; (3) self-reporting violations; and (4) providing substantial assistance to investigations.

1. Credit for Steps Taken to Correct Deficient Procedures and Systems

The Notice makes clear that FINRA expects that firms will take corrective steps to fully remediate problems involving deficient supervisory systems, procedures, and controls. In order to receive extraordinary cooperation credit, firms must exceed these baseline requirements. The Notice provides the following examples of corrective steps that may result in credit for extraordinary cooperation:

- Conducting an independent investigation or audit that goes beyond the immediate issue and identifying and remediating misconduct that may have occurred;
- Hiring independent consultants to ensure the adoption and implementation of improved supervisory systems, procedures, and controls; and
- Addressing organizational weaknesses that may have led to a violation by dedicating additional resources and making organizational changes by, for example, creating new supervisory positions, adjusting reporting lines, or, if necessary, disciplining responsible individuals.

Notably, the Notice recognizes that there is “some tension between expecting firms to report misconduct promptly and, at the same time, giving priority to corrective measures that a firm takes prior to detection by FINRA or other regulators.” In that regard, FINRA clarifies that it will, in appropriate circumstances, give credit for corrective measures taken “promptly after a firm reports the misconduct.”

2. Credit for Restitution to Customers

In the Notice, FINRA reiterates that it expects firms to make full restitution to injured customers in all cases. In order to receive extraordinary cooperation credit, FINRA will look to whether a firm has proactively taken steps to ensure that restitution is paid as quickly and fully as possible. In complex cases involving systemic failures where identifying impacted customers and calculating each individual's losses can be time-consuming, FINRA will consider extraordinary cooperation credit where a firm "significantly accelerates" the remediation process. Firms can meet this standard by implementing certain methodologies to identify customers for restitution, such as a statistical approach, or by making personnel and structural changes, such as dedicating staff members, hiring temporary help, paying for overtime, or re-prioritizing other projects, so that trade-by-trade reviews can be conducted on an accelerated basis in order that customers can be made whole in a timely fashion. In addition, similar to credit for steps taken to address deficient procedures, the Notice clarifies that even where restitution is paid after FINRA becomes aware of the misconduct, FINRA will still consider whether to award credit where there has been full remediation at the initiative of the firm and prior to any order by FINRA or another regulator.

3. Credit for Self-Reporting Violations

The Notice states that in order to receive credit for self-reporting violations, member firms must "go significantly beyond" what is required under FINRA Rule 4530(b). The following are factors that FINRA will consider in assessing whether to award credit:

- Whether the firm self-reports misconduct that does not fall within the reporting requirements of Rule 4530(b);
- Where a self-report is required under Rule 4530(b), whether the firm provides more information to FINRA than is required by Rule 4530(b), such as, for example, providing summaries of key facts and documents;
- Whether the firm proactively detected the misconduct through compliance, audits, or other surveillance, as opposed to having identified the misconduct only after receiving notice from customers, counterparties, or regulators;
- Whether the firm made diligent efforts to identify and inform FINRA of the relevant facts as soon as they were discovered and kept FINRA updated on new facts learned through continued investigation;
- Whether the firm reported misconduct to the public and other regulators; and
- The firm's level of cooperation with other regulators, particularly where multiple agencies are investigating the misconduct.

4. Credit for Providing Substantial Assistance to FINRA Investigations

Lastly, FINRA also will consider giving credit for providing substantial assistance in its investigation of the underlying misconduct. The Notice specifically emphasizes that there is no one-size-fits-all approach to providing substantial assistance and that the degree of help required is dependent on the firm's overall size and resources. Examples of substantial assistance deserving of credit provided in the Notice include the following:

- Volunteering relevant information that the firm believes would be helpful even if FINRA did not directly request the specific documents or information under Rule 8210;
- Volunteering relevant industry knowledge to help FINRA quickly assimilate information about a complex product or practice;

- Providing demonstrations to FINRA of trading or other systems at issue;
- Identifying witnesses who possess relevant information, including witnesses over whom FINRA lacks jurisdiction, and making those witnesses available for interviews; and
- Conducting a thorough and independent audit or investigation, using counsel or consultants where appropriate, and fully disclosing the findings to FINRA.

III. The Type of Credit to Be Given, Additional Transparency, and Credit for Individuals

FINRA clarified that credit for extraordinary cooperation may take many forms and can range from an outright declination of an enforcement action, to reduced or eliminated fines, to foregoing the imposition of required undertakings, such as hiring an independent consultant. In addition, the Notice contains a commitment by FINRA to provide greater transparency when it awards extraordinary cooperation credit. FINRA will take additional steps to distribute this information, including by adding a new section in Letters of Acceptance, Waiver, and Consent (AWCs), entitled “Credit for Extraordinary Cooperation,” which will describe the factors that resulted in the credit being given, as well as the type of credit. FINRA will also note factors that led the respondent to receive credit and the type of credit in press releases announcing the resolution of cases. Interestingly, in cases that proceed without a formal action – where it traditionally does not make a public statement – FINRA stated that it would determine whether it would be useful to publish an anonymized description of the matter. The Notice also stated that AWCs may include another new section, entitled “Sanctions Considerations,” within which FINRA may identify mitigating or aggravating factors that impacted the sanction determination. Finally, the Notice clarified that the guidance contained therein applies with equal force to individuals but stated that aggravating factors, such as intentional or reckless misconduct or attempted concealment of misconduct, are more likely in the cases of individuals, which run counter to an award of credit for extraordinary cooperation.

IV. Conclusion

Overall, the Notice does not meaningfully alter the traditional factors FINRA uses to evaluate extraordinary cooperation: self-reporting, correcting deficiencies through remediation, and assisting FINRA investigations. It does, however, provide additional clarity on the factors that FINRA will look at to evaluate extraordinary cooperation and provides examples of conduct that FINRA believes constitutes extraordinary cooperation while, at the same time, announcing FINRA’s commitment to continuing to provide further transparency to firms going forward.