

RULE UPDATE NEWSLETTER

BACKGROUND CHECKS ON REGISTRATION APPLICANTS FINRA Rule 3110(e)

FINRA member firms understand the importance of the requirements to “Know Your Customer”, but now

FINRA Rule 3110(e), Responsibility of Member to Investigate Applicants for Registration, became effective July 2015. This newsletter covers the background investigation responsibilities of FINRA member firms when considering registration of a new individual.

increased emphasis is being placed on firms to develop and enforce procedures to also truly know the firm’s

prospective registered individuals (“Applicant”). FINRA now requires that all member firms strengthen the background investigations/reviews that the firm conducts on any Applicants considered for registration with the firm. The first part of Rule 3110(e), the requirement to determine the “good character, business reputation, qualifications and experience” of an Applicant, is required to be conducted and completed *prior* to any registration (Form U4) filing with CRD. FINRA does not detail how this initial investigation must be completed or define the scope of the investigation, but the firm must ensure that a reasonable process is undertaken for proper and complete evaluation of the Applicant. Information and documentation requested and reviewed during this

TEXT OF FINRA RULE 3110(e)

Responsibility of Member to Investigate Applicants for Registration: “Each member shall ascertain by investigation the good character, business reputation, qualifications and experience of an applicant before the member applies to register that applicant with FINRA and before making a representation to that effect on the application for registration.

If the applicant previously has been registered with FINRA or another self-regulatory organization, the member shall review a copy of the applicant’s most recent Form U5, including any amendments thereto, within 60 days of the filing date of an application for registration, or demonstrate to FINRA that it has made reasonable efforts to do so. In conducting its review of the Form U5, the member shall take such action as may be deemed appropriate.

The member shall also review an applicant’s employment experience to determine if the applicant has been recently employed by a Futures Commission Merchant or an Introducing Broker that is notice-registered with the SEC pursuant to Section 15(b)(11) of the Exchange Act. In such a case, the member shall also review a copy of the applicant’s most recent CFTC Form 8-T, including any amendments thereto, within 60 days of the filing date of an application for registration, or demonstrate to FINRA that it has made reasonable efforts to do so. In conducting its review of a Form 8-T, the member shall take such action as may be deemed appropriate.

In addition, each member shall establish and implement written procedures reasonably designed to verify the accuracy and completeness of the information contained in an applicant’s initial or transfer Form U4 no later than 30 calendar days after the form is filed with FINRA. Such procedures shall, at a minimum, provide for a search of reasonably available public records to be conducted by the member, or a third-party service provider, to verify the accuracy and completeness of the information contained in the applicant’s initial or transfer Form U4.”

investigative stage of the registration process may include, but not be limited to, the following: employment application, reference checks, outside business activities, most recent Form U5, information provided on initial or transfer Form U4, search of Applicant on the CRD system, FBI fingerprint reports, credit reports and/or private background checks. Regulatory Notice 15-05 Background Checks, reminds firms that background investigations must be “conducted in accordance with all applicable laws, rules and regulations, including federal and state requirements, and that all necessary approvals, consents and authorizations have been obtained.”

In addition, if the applicant has been previously registered with FINRA or another SRO, the firm is required to review the Applicant’s most recent Form U5 within 60 days of the date the firm files the Applicant’s Form U4. If the Applicant has been recently employed by a Futures Commission Merchant, the firm should request and review a copy of the Applicant’s most recent CFTC Form 8-T within 60 days of the of the date the firm files the Applicant’s U4. Review of the Form U5 and/or the Form 8-T should be evidenced by the initials of the person responsible for the review and a copy maintained in the Applicant’s file. If for any reason the firm has not been able to receive and review a copy of the Form U5 or Form 8-T, the firm is required to maintain documentation to demonstrate to FINRA that it made reasonable efforts to meet this rule requirement.

The final section of Rule 3110(e) is the requirement for FINRA member firms to create and enforce a

procedure to verify the accuracy and completeness of the information filed in the Applicant’s initial or transfer Form U4. Verification of the information included on an Applicant’s Form U4 must be verified no later than 30 calendar days following the CRD filing of the Form U4 with FINRA. To comply with this requirement the firm, at a minimum, must conduct a search of reasonably available public records. The public record search may be conducted by the member firm or the firm may engage a third-party service provider to conduct the search. For the thorough investigation required by FINRA, it is recommended that the firm utilize the services of a company that specializes in background investigations. Please contact Brokerage Consulting Group if you are interested in the names of companies that provide this type of service.

As required by the previous rule, the firm must request and receive prior written permission from the applicant before conducting any background investigation, including accessing the Applicant’s records maintained on the CRD system. Evidence of written permission must be maintained in the Applicant’s file.

Note: For more detailed information on the background investigation requirements, please see FINRA Rule 3110(e) and FINRA Regulatory Notice 15-05.

If you have any questions, please do not hesitate to contact us.