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## REGULATORY FOCUS ON “HIGH-RISK” REGISTERED REPRESENTATIVES AND RECIDIVISM

*Recent studies of “high-risk” registered representatives have revealed deficiencies in firm management of them, and have led to a new regulatory focus on their hiring and supervision. The authors describe FINRA’s focus on high-risk registered representatives through regulatory notices, rules, and enforcement actions. They then describe NASAA’s 2018 Enforcement Report and state enforcement actions brought against firms that failed to adequately supervise recidivist registered representatives. They close by noting steps firms must take in their supervisory plans to meet regulators’ expectations.*

By Corin R. Swift, Benjamin L. Nager, and Jordan S. Schwartz \*

State and federal securities regulators have recently focused registration, examination, and enforcement efforts on “high-risk” registered representatives.<sup>1</sup> Most notably, last year Financial Industry Regulatory Authority (“FINRA”) proposed new rule amendments, which would impose additional obligations on firms that employ high-risk registered representatives.<sup>2</sup> The rule proposal arrives on the heels of recently publicized academic and state-led studies evaluating the likelihood of high-risk registered representatives engaging in future

misconduct, and firms’ supervision of those representatives.

In 2016, economists Mark Egan, Gregor Matvos, and Amit Seru published a study, which revealed that registered representatives with a history of misconduct “are five times more likely to engage in misconduct than the average adviser, even compared with advisers in the same firm, at the same location, and at the same point in time.”<sup>3</sup> After Egan, et al., published their study, the Massachusetts Securities Division (the “Division”) conducted a sweep of certain Massachusetts-registered broker-dealer firms with a higher-than-average

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<sup>1</sup> For the purposes of this article, the term “registered representative” refers to any person registered with FINRA or a state to engage “in the business of effecting transactions in securities for the account of other.” 15 U.S.C. § 78(c)(4)(A)(2018). Depending on the regulator, these individuals may be referred to as “registered representatives,” “brokers,” “agents,” or “salespersons.”

<sup>2</sup> FINRA Regulatory Notice 18-16 (Apr. 30, 2018).

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<sup>3</sup> MARK EGAN, GREGOR MATVOS, AND AMIT SERU, THE MARKET FOR FINANCIAL ADVISER MISCONDUCT (2017), <http://www.nber.org/papers/w22050>. The authors also determined that “[a]lmost 8% of currently registered advisers engaged in misconduct at least once during their career. Of those, 27% are repeat offenders, having two or more disclosures of misconduct.” *Id.* at 12.

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### INSIDE THIS ISSUE

- THE GROWING IMPORTANCE OF FULLY INTEGRATED COMPLIANCE PROGRAMS, Page 105
- CLE QUESTIONS, Page 112