

## Succession Planning

### FINRA Provides Guidance on Succession Planning

#### Summary

Member firms often encourage registered representatives to have succession plans in place to plan for expected or unexpected life events. Succession planning can benefit customers, member firms and registered representatives. This *Notice* discusses these benefits, as well as common types of succession plans. This *Notice* also provides an overview of related FINRA rules and administrative processes and includes questions to consider when developing and implementing succession plans.

Questions regarding this *Notice* should be directed to:

- ▶ Jeanette Wingler, Associate General Counsel, Office of General Counsel, at [jeanette.wingler@finra.org](mailto:jeanette.wingler@finra.org) or (202) 728-8013; or
- ▶ Elena Schlickenmaier, Senior Principal Analyst, Strategic Analysis, Research and Publications, Member Supervision, at [elena.schlickenmaier@finra.org](mailto:elena.schlickenmaier@finra.org) or (202) 728-6920.

#### Background and Discussion

Registered representatives (representatives) often develop close and trusted relationships with their customers. While member firms' different business models create different approaches to managing these relationships with customers, member firms often encourage representatives to have a succession plan in place. The COVID-19 pandemic and industry demographic trends have spurred greater focus on, and adoption of, succession plans in recent years.<sup>1</sup>

Succession plans—which may be referred to as retirement plans, legacy plans, transition plans, sunset plans or other similar names—typically address representatives leaving the brokerage industry due to expected events, such as retirement, or unexpected events, such as death, disability or illness. Particularly for small firms and sole proprietorships, a succession plan may involve the sale of a firm. While plan terms and complexity vary, succession plans typically address the sale of a book of business or firm assets or the reassignment of a representative's customer accounts.

November 1, 2022

#### Notice Type

- ▶ Guidance

#### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Operations
- ▶ Registered Representatives
- ▶ Risk Management
- ▶ Senior Management

#### Notice Key Topics

- ▶ Business Continuity Planning
- ▶ Commissions
- ▶ Customer Accounts
- ▶ Customer Communications
- ▶ Customer Nonpublic Information
- ▶ Membership Application Program
- ▶ Registered Representatives
- ▶ Succession Planning

#### Referenced Rules

- ▶ FINRA Rule 1010 Series
- ▶ FINRA Rule 2010
- ▶ FINRA Rule 2040
- ▶ FINRA Rule 2273
- ▶ FINRA Rule 3110
- ▶ FINRA Rule 4370
- ▶ FINRA Rule 4511
- ▶ FINRA Rule 8311
- ▶ FINRA Rule 9610
- ▶ CAB Rule 204
- ▶ Regulation S-P

This *Notice*:

- ▶ discusses the benefits of proactive succession planning;
- ▶ notes recent industry demographic trends;
- ▶ describes common types of succession plans;
- ▶ provides an overview of related FINRA rules and administrative processes; and
- ▶ lists questions for consideration to aid member firms and representatives in developing, implementing and evaluating succession plans.

This *Notice* does not create new legal or regulatory requirements or new interpretations of existing requirements, nor does it relieve firms of any existing obligations under federal securities laws and regulations. Member firms may consider the information in this *Notice* in developing new, or modifying existing, practices that are reasonably designed to achieve compliance with relevant regulatory obligations based on the member firm's size and business model.

## I. Benefits of Succession Planning for Customers, Firms and Representatives

Succession planning benefits customers, member firms and representatives. Customers can receive a more orderly transition of their accounts. Member firms can minimize operational risk and retain customer relationships. Representatives can plan for life events, receive compensation for their books of business and, where possible, help prepare new representatives to support their customers.

### Customers

Succession plans help ensure that customers do not experience an interruption in service, such as when a representative leaves the industry or retires without connecting customers to another representative, firm staff or other firm resources. Customers can benefit from plans that help to transition their accounts to a new representative or firm in an orderly manner.

### Succession Plan Helps Small Firm to Continue Operations

A small firm's chief compliance officer (CCO) and Financial and Operations Principal (FinOp) unexpectedly died during a weekend; the firm had a succession plan in place that, among other things, promptly notified FINRA of the situation and engaged a recruiting firm to hire a new CCO and FinOp. As a result of the firm's proactive planning for these events, the firm successfully continued operations without any interruptions in service to its customers.

Customer communications in succession planning play a critical role in helping customers understand how and by whom their account will be serviced. These communications help customers make informed choices about working with the new firm or representative or, instead, transferring their accounts to another firm or representative. In addition, succession planning can help representatives to service new customers' accounts by providing background information about the customers.

### Firms

Succession planning can benefit firms by facilitating orderly transitions of customer accounts and providing practice management options for current and departing representatives. Particularly for key firm personnel, small firms and sole proprietorships, succession planning can play a role in minimizing operational and other risks to a firm's business. Succession planning also can help ensure that firms have appropriate staff to respond to regulatory inquiries, including exams, investigations and other engagements with regulators (*e.g.*, where a representative also serves as a compliance officer for the firm).

### Representatives

Like estate planning or insurance, succession planning can be part of a representative's proactive planning for life events. Notably, succession planning can address potential issues and risks related to representatives' retirement, death, disability, illness or cognitive decline.<sup>2</sup> For example, some firms have implemented comprehensive programs to address risks relating to representatives with diminished capacity and developed succession plans that are triggered by unexpected or emergency events, such as a representative's death.

Moreover, succession planning allows retiring representatives with longstanding and close relationships with their customers to transition customer accounts to a new representative who will assist and benefit the customers. These representatives may view successfully transitioning customers to new representatives and preparing representatives to service customers as part of their professional legacy. In addition, representatives may seek the additional benefit of obtaining compensation for their books of business as part of their retirement financial planning.

The professional and customer relationships that can be built through succession planning also can play a valuable role in lowering the barrier to entry for, and retention, of new representatives. Firms and professionals are reminded that FINRA has developed tools to support broker-dealer industry participants' initiatives and programs to help bring new individuals into the industry, including the [Securities Industry Essentials® \(SIE\) Exam](#), a FINRA exam for prospective securities industry professionals,<sup>3</sup> and the [Financial Industry Networking Directory \(FIND\)](#), a FINRA service that connects non-registered individuals with financial services firms that are recruiting for full-time employment and internship positions.<sup>4</sup>

### Contrasting Challenges for Firms and Representatives Without Succession Plans

In contrast, the lack of succession planning can create challenges for customers, member firms and representatives. For example, FINRA has observed the following situations:

- ▶ **Death** – The founding member and co-owner of a firm unexpectedly died, leaving the remaining co-owner without a succession plan or any guidance on servicing customers. After trying to continue the business over a year after the co-owner's death, the firm was not able to hire another representative to continue the business and ceased operations.
- ▶ **Access to Critical Regulatory and Other Systems** – A firm's owner died without a succession plan and the firm's other registered persons had not obtained access to critical firm and regulatory reporting systems. This created numerous operational and regulatory challenges for the firm and the firm ceased operations.
- ▶ **Regulatory Action** – The CEO of a firm without a succession plan was barred and the firm was left with only one registered principal. The firm ceased operations.
- ▶ **Cognitive Decline and Other Life Events** – A firm co-owner without a succession plan called the [FINRA Securities Helpline for Seniors®](#) to discuss concerns that the other co-owner was exhibiting signs of diminished capacity. The caller was unsure how to address this with the other co-owner, transition ownership of the business or discuss this with customers. FINRA staff provided relevant resources to the firm to support them in the transition.

#### Member Firms Address Suspected Diminished Capacity

Some firms implemented a comprehensive approach to address suspected diminished capacity and cognitive decline in representatives, including:

- implementing training on diminished capacity and cognitive decline for all firm staff;
- formalizing an escalation process to raise concerns relating to cognitive issues by staff and other representatives;
- establishing a diminished capacity committee to collectively evaluate these issues and decide on next steps;
- developing an accommodations committee to evaluate representatives' limitations, engage their physicians, protect their privacy and implement working arrangements that complied with relevant employment laws and accommodated their disabilities; and
- engaging with representatives and, depending on the circumstances, supporting the representatives with implementing a new working arrangement, developing a succession plan, providing assistance with performance issues or recommending termination.

- ▶ **Participation** – A firm implemented a succession planning program for its representatives but did not articulate the personal or financial benefits for participation. Many of the firm’s representatives did not participate in the program.
- ▶ **Customer Challenges and Departure** – A representative had an unexpected medical event, but had not taken part in their firm’s succession planning program and, as a result, did not introduce the new representative to the customers. Many of the customers experienced challenges with the transition and left the firm.
- ▶ **Communication Breakdown** – A customer called and emailed their representative without any response before reaching out to the firm and learning that the representative had recently died. The firm was not aware of the death prior to the customer’s call so it had not notified the representative’s customers. If the representative had participated in the firm’s succession planning program, the representative’s family or other designee could have notified the firm who then could have engaged with the representative’s successor regarding the representative’s customers.

## II. Demographic Trends

Looking at demographic trends across the American labor force, the “Baby Boomer” generation born between 1946 and 1964 have been a sizable cohort of the labor force. More recently, millions of Baby Boomers have retired each year and the pace of these retirements accelerated during the COVID-19 pandemic.<sup>5</sup> Since 2016, the “Millennial” generation born between 1981 and 1996 has been the largest generation in the American labor force.<sup>6</sup>

While the benefits of proactive succession planning are not limited to any age group, succession planning frequently arises in the context of representatives who are considering retirement.<sup>7</sup> Brokerage industry demographics indicate that an increasing number of representatives are at or approaching traditional retirement age. As of December 2021, 16.32 percent of representatives were age 60 or older; 8.20 percent were age 65 and older; and 3.82 percent were age 70 and older.<sup>8</sup> The percentage of representatives in each of these age brackets has increased in recent years.<sup>9</sup>

## III. Common Types of Succession Plans

Though terms and complexity vary across member firms’ business models, succession planning can be divided into two broad categories: (1) internal programs, or (2) an external sale or other transaction. Firms may also develop succession planning-related education, tools or services.

### Internal Succession Planning Programs

- ▶ **Teams** – Organization of representative teams to service customers. This structure is often designed so that the remaining team member(s) are available to service customers if a representative retires or otherwise leaves the firm.
- ▶ **Sale of Book of Business** – Sale of a representative's book of business to another representative at the same firm or at another firm under common ownership.
- ▶ **Junior Representative** – Hiring or developing a junior representative to take over a representative's book of business.
- ▶ **Designation** – A representative designating another representative as successor and informing the firm and customers of the designation, such as a representative designating as successor his son, who also is a representative at the firm. In addition, owners or control persons of small firms and sole proprietorships may agree with and designate another party to wind down the business upon specified events.
- ▶ **Contingency Plans** – Contingency plans for specified events or a signed commitment between representatives for succession upon specified events, such as a representative's incapacity or death.
- ▶ **Reassignment** – A member firm's plan for reassigning customer accounts to new representatives when a representative retires or otherwise leaves the firm.
- ▶ **Firm Support** – A member firm's program where, in some events, such as a representative's death, the firm will ensure customers are serviced by firm staff or other representatives while looking for potential buyers for the representative's book of business.

Firms' internal programs may incorporate agreements to pay continuing commissions to retiring representatives, which are discussed in detail below.

### External Succession Planning Programs

- ▶ **Sale** – An agreement to transfer or sell a representative's book of business to another firm or representative at another firm; or
- ▶ **Merger or Acquisition** – An agreement for a firm to merge into, acquire or be acquired by another firm.

### Related Education, Tools or Services

Firms' succession planning-related education, tools or services may include:

- ▶ **Education** – Firms often take steps to educate representatives about the need for succession plans and the availability of firm programs, such as raising succession planning during periodic firm branch inspections, firm conferences and webinars, firm coaching programs and at events attended by representatives' spouses or heirs. Some firms also maintain dedicated internal websites with education and resources for representatives.

- ▶ **Matching** – Some firm’s internal programs include a tool or service to match representatives who may be interested in succession planning, such as a dedicated matching website. To aid in matching, firms may seek information or data from representatives about their experience, customer accounts and investment approach. Some firms use their diversity, equity and inclusion (DEI) initiatives to facilitate introductions and relationships between representatives who are interested in succession planning. Firm staff, such as branch managers, also may use their personal relationships or knowledge to facilitate connections between representatives. The ability to engage virtually and communicate with customers has enabled some firms to match representatives who live in different geographic areas, which may be particularly helpful for customers and representatives living in less populated areas.
- ▶ **Financing and Valuation** – Some firms provide bridge financing or other financial support to facilitate purchases. Firms may offer an in-house service or technical tools to aid in determining a business’s market value. Firms and representatives also may engage consultants or third-party vendors to aid in determining a business’s market value and identifying potential buyers.

#### **Member Firm Makes Succession Planning a Top Priority**

A firm prioritized succession planning in its business support program for all representatives by:

- explicitly making succession plan adoption a business and compliance goal across the firm;
- leveraging a centralized support function to manage all succession planning-related initiatives and related implementation support;
- recommending all representatives adopt a short-term disaster or contingency plan;
- running an educational campaign across all offices focusing on the benefits of succession planning, including:
  - conducting periodic video and, more recently, in-person meetings;
  - issuing compliance notices and articles;
  - addressing succession planning as part of the firm’s annual conference;
  - profiling succession planning at top producer events and trips, as well as firm leadership and regional conferences;
  - highlighting success stories for current and former representatives with succession plans, as well as challenges unprepared representatives experienced;
  - holding workshops and providing playbooks to teach staff and representatives how to address the emotional aspects of retirement and other questions related to succession planning; and
- hiring consultants for assistance with valuation and matching representatives across the firm and, if needed, across the industry.

#### IV. Related FINRA Rules and Administrative Processes

Depending on the structure and terms, succession planning can intersect with several legal and regulatory areas. Below is an overview of related FINRA rules and administrative processes, which may be helpful for firms developing and implementing succession plans to consider. FINRA recognizes that succession planning may implicate other FINRA rules, as well as non-FINRA legal and regulatory considerations, such as employment law.

##### Business Continuity Planning

While FINRA rules do not require that firms or representatives adopt separate succession plans, member firms are required to adopt business continuity plans (BCPs).<sup>10</sup> FINRA Rule 4370 (Business Continuity Plans and Emergency Contact Information) requires member firms to create, maintain, review at least annually and update upon any material change, a written BCP identifying procedures relating to an emergency or significant business disruption. BCPs must be reasonably designed to enable a member firm to meet its existing obligations to customers and address existing relationships with other broker-dealers and counterparties.

Depending upon their role and responsibilities at the firm, an event involving a key person event (e.g., a registered person's illness, incapacity or death) could be an emergency or significant business disruption that triggers the firm's BCP. This may be more likely to occur if the firm is a sole proprietorship or has a small number of registered persons. Member firms are encouraged to consider the potential impact of these events on their BCPs.<sup>11</sup>

Rule 4370 also requires each firm to provide (and promptly update upon any material change) to FINRA prescribed emergency contact information, including the designation of two emergency contact persons, both of whom must be associated persons. Member firms may register and update their emergency contact persons through the [FINRA Contact System \(FCS\)](#). Member firms are encouraged to review their emergency contact information in FCS for accuracy.

##### Membership Application Program (MAP)

A member firm's succession plan may involve the MAP rules, FINRA Rules 1011 – 1019, that could include filing a Continuing Membership Application (CMA), or engaging in the materiality consultation process (MatCon).<sup>12</sup> Firms are encouraged to have open dialogues with their respective Risk Monitoring Analysts (RMAs) about succession plans.<sup>13</sup>

##### Engaging with RMAs

Member firms are encouraged to contact their RMA for MAP-related questions or whenever a control person or owner departs the firm.

Firms are encouraged to share relevant succession planning-related information for control persons with their RMAs (e.g., that the sale of the firm's assets is related to the co-owner's illness or retirement) to aid staff in better understanding the context and timing of the proposed changes.



### *CMA and MatCons*

A change in ownership could trigger an obligation for member firms to file a CMA under FINRA Rule 1017 (Application for Approval of Change in Ownership, Control, or Business Operations).<sup>14</sup> Rule 1017(a) specifies the changes in firms' ownership, control or business operations that require a CMA, such as a merger with another member firm; an acquisition or transfer of 25 percent or more of the member firm's assets;<sup>15</sup> or a material change in business operations as defined in FINRA Rule 1011(m).<sup>16</sup>

Additional requirements under the MAP rules for some proposed changes include:

- ▶ A member firm is precluded from effecting changes in ownership, control or business operations, including business expansions, if there is a Covered Pending Arbitration Claim, as defined in FINRA Rule 1011(c)(2), unpaid arbitration award or unpaid settlement related to an arbitration without first seeking a MatCon.<sup>17</sup>
- ▶ Unless a member firm has submitted a written request to the Department of Member Supervision seeking a MatCon, the member firm is required to file a CMA whenever a natural person seeking to become an owner, control person, principal or registered person of the member firm has in the prior five years, one or more "final criminal matters" or two or more "specified risk events."<sup>18</sup>

### *Principal Registration Requirements*

Member firms, except for sole proprietorships, must have at least two registered principals and one FinOp. As part of succession planning, member firms are encouraged to consider and plan for events that may cause the firm to cease to meet the two principal requirement. Firms may also request a waiver or exemption from the two principal requirement with the MAP Group in accordance with FINRA Rule 9610 (Application). If a waiver is granted, the principal at the firm must be qualified as a FinOp.<sup>19</sup>

### **Researching Professional Backgrounds**

Researching the professional backgrounds of member firms and individuals who are parties to a succession plan is an important part of understanding potential issues and risks. Using the Pre-Registration feature in CRD, firms can research the registration and disclosure history of financial professionals to make informed hiring decisions. Similarly, firms can also check [BrokerCheck](#) and the [Investment Adviser Public Disclosure \(IAPD\)](#) website to research the backgrounds of broker-dealers, investment advisers and financial professionals.<sup>20</sup>

In considering a potential succession plan, member firms are encouraged to consider relevant histories (e.g., where a representative with several customer complaints or a disciplinary history is seeking to team with a more junior representative)<sup>21</sup> and whether any representative is or should be put under heightened supervision.<sup>22</sup> Firms can use this research in evaluating potential risks to investors and in considering whether a representative has the particular training or experience that may be needed to service some customers (e.g., where a customer has a complicated family structure or financial situation or has expressed an interest in working with a representative who has certain expertise).

### **FINRA Disciplines Representative for Permitting His Father, a Former Representative, to Conduct a Securities Business**

FINRA imposed a fine and a nine-month suspension for a representative who permitted and enabled his father, a former representative who had been barred and statutorily disqualified from the securities industry, to conduct a securities business, including attending in-person customer meetings to discuss brokerage account strategy, emailing with customers about their brokerage account statements, maintaining an office within the branch location and sharing a phone line with the branch location.

See [James Alan Schumaker, Letter of Acceptance, Waiver, and Consent \(AWC\) \(Feb. 18, 2021\) \(Case No. 2019061887701\)](#).

#### *Disciplined Persons*

Where a representative is leaving the industry due to a bar or legal or regulatory action, there may be a heightened risk that the representative will seek to sell or transfer their book of business to another representative who will improperly act as a proxy for and share commissions with the former representative. These arrangements may lack a formal written agreement between the current and former representatives or use a written agreement that is intended to mask the improper activity.<sup>23</sup>

An unusually high degree of engagement between the representative and former representative or an unusually low degree of engagement between the new representative and that representative's customers may be red flags of a potentially improper arrangement that may be observed through communications and activity reviews. Firms also may conduct customer check-in calls to assess the transition or to review for improper activity by the terminated or current representative.

### **SEC Takes Action Against Fraud Involving Retiring Representatives**

The SEC filed charges and obtained an asset freeze against defendants who engaged in a fraudulent scheme where they:

- bought or took over books of business of retiring investment professionals from around the country; and
- persuaded (sometimes independently and other times with the assistance of local investment professionals) these newly acquired clients to withdraw their savings from traditional investments and invest in issuers controlled by the defendants or their associates.

See [SEC v. Santillo, et. al., No. 18-cv-5491 \(JGK\) \(S.D.N.Y.\) \(filed June 19, 2018\)](#); see also [SEC Shuts Down \\$102 Million Ponzi Scheme](#).

#### *Bad Actors*

In considering a potential sale, firms should be aware that bad actors may purchase a representative's book of business to obtain access to customers' accounts and information for fraudulent schemes. Bad actors may seek to take advantage of representatives' interest in succession planning or their needs for the proceeds from the sale of their books of business. The selling representative's involvement can range from being unaware of the bad actor's intentions in purchasing the book of business to actively aiding the bad actor in the scheme.

#### **Qualification Examinations**

A representative may engage in succession planning for life events but nevertheless want to leave open the possibility of a future return to the industry (e.g., representatives who are leaving the industry due to illness or transitioning to a role in another part of the financial industry). These representatives are reminded of FINRA's [Maintaining Qualifications Program \(MQP\)](#). The MQP provides eligible individuals who terminate any of their representative or principal registrations with the option of maintaining their FINRA qualifications for certain terminated registrations by completing annual continuing education (CE).<sup>24</sup> Individuals who elect the MQP option have a maximum of five years in which to reregister with a member firm without having to requalify with FINRA by exam or obtain an exam waiver.<sup>25</sup>

#### **Commission Payments to Retired Representatives**

Firms' internal succession planning programs may incorporate agreements to pay continuing commissions to retiring representatives, which must be consistent with the applicable federal securities laws, Securities Exchange Act of 1934 (SEA) rules and regulations and FINRA rules.

*FINRA Rule 2040 (Payments to Unregistered Persons)*

Rule 2040 governs the payment of transaction-based compensation by member firms to unregistered persons.<sup>26</sup> Subject to conditions, under Rule 2040(b), member firms can pay continuing commissions to their “retiring registered representatives,”<sup>27</sup> after they cease to be associated with the firms, derived from accounts held for continuing customers of the retiring registered representative regardless of whether customer funds or securities are added to the accounts during the period of retirement.<sup>28</sup>

*SEC Staff Guidance*

Rule 2040(b) incorporates guidance from prior SEC no-action letters on the payment of commissions to retired registered representatives (referred to herein as SEC Staff Retired Representatives Guidance).<sup>29</sup> Accordingly, firms and representatives who are drafting, reviewing or executing agreements for continuing commission payments to retired representatives should consider the requirements of Rule 2040 and the prior SEC Staff Retired Representatives Guidance.<sup>30</sup>

The SEC Staff Retired Representatives Guidance requires that the retiring representative, representative who will service and receive compensation related to the customer accounts of the retiring representative (the receiving representative), and firm comply with specified terms and conditions, including:

*Retiring Representative*

- ▶ The retiring representative must have been continuously employed by or associated with the firm for a minimum of three years as of the date of retirement (Retirement Date).<sup>31</sup>
- ▶ The retiring representative must have demonstrated appropriate standards of professional and ethical conduct.<sup>32</sup>
- ▶ The retiring representative must not contact former clients for the purpose of soliciting them to enter into securities transactions, discussing any past, present or future transactions, or otherwise providing securities-related services or advice to the extent the services or advice relates to transactions in securities.<sup>33</sup>
- ▶ The retiring representative must comply, to the extent applicable, with federal and state securities statutes and regulations, all policies, procedures and rules of relevant regulatory and self-regulatory bodies.
- ▶ The retiring representative must sever association with the firm and with any municipal securities dealer, government securities dealer, investment adviser or investment company affiliates (except as may be required to maintain any licenses or registrations required by any state) and is not permitted to be associated with any other broker, dealer, municipal securities dealer, government securities dealer, investment adviser or investment company, during the term of the agreement.<sup>34</sup>

- ▶ The retiring representative may recommend a receiving representative but not be personally compensated by that representative for the referral.
- ▶ The retiring representative must certify to the firm compliance with the requirements and conditions of the agreement at least annually.

#### Receiving Representative

- ▶ With limited exceptions, the receiving representative must have been (1) employed in the securities industry in a registered capacity for a minimum of three years as of the Retirement Date and (2) continuously affiliated with the firm in a registered capacity for a minimum of one year as of the Retirement Date.<sup>35</sup>
- ▶ The receiving representative must not be subject to a statutory disqualification resulting from any action of, or proceeding brought by, the SEC or any self-regulatory organization for which the sanction is currently in effect (or was in effect during any part of the three years prior to the Retirement Date).

#### Firm

- ▶ The firm must approve the receiving representative.
- ▶ The firm must establish parameters for up to five years following retirement and a percentage scale (that is either fixed or decreases the percentage the retiring representative receives each year) regarding the sharing of commissions by the retiring representative and the receiving representative.
- ▶ Prior to the Retirement Date, the firm must inform the account holders of the applicable accounts in writing of the retiring representative's departure from the firm and of the transfer of the applicable accounts to the receiving representative.
- ▶ The firm must contact a representative sample of the account holders including a significant set of high grossing customer accounts subject to the agreement at least annually to confirm that the retiring representative has not provided investment advice or solicited trades in securities in any way.

#### *Use of Joint Representative Codes*

The receiving representative may enter into a written agreement with the retiring representative to service customer accounts, including executing trades for those accounts, under a joint representative (or joint production) code that is used to calculate the commissions payable to each representative. FINRA has brought disciplinary actions for violations of FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade) and the books and records requirements of FINRA Rule 4511 (General Requirements) where representatives inaccurately altered or falsified the representative codes on trades in member firms' order entry systems to receive a higher commission and caused the firms' trade confirmations to show inaccurate representative codes.<sup>36</sup>

The risk of improper alteration or falsification of representative codes may be higher when the firm lacks operational controls for altering the representative code assigned to an account or when the representative is unclear whether and, if so, under what circumstances the representative may use a personal, rather than joint representative code.<sup>37</sup>

### Potential Conflicts of Interest

Representatives may encounter conflicts of interest from anticipated commission payments in retirement or the projected proceeds from the sale of the business (e.g., conflicts related to recommending accounts or products that are more likely to generate a higher valuation for the sale of the business or commission payments in retirement). In considering representatives' obligations when making recommendations to retail investors, firms and representatives are reminded of the [SEC Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Account Recommendations for Retail Investors](#), which provides SEC staff views on how broker-dealers, investment advisers and their associated persons can satisfy their obligations, including the SEC's Regulation Best Interest (Reg BI), to retail investors when making account recommendations.

Among other things, the Reg BI Conflict of Interest Obligation requires a broker-dealer to identify and address conflicts of interest that may incline a broker-dealer or representative—consciously or unconsciously—to make a recommendation that is not disinterested. This process “should not be merely a ‘check-the-box’ exercise, but a robust, ongoing process that is tailored to each conflict.”<sup>38</sup> Moreover, even if a broker-dealer complies with its Conflict of Interest Obligation, “it has not fully complied with Reg BI unless it has also satisfied the Care Obligation,” including the requirement “to have a reasonable basis to believe that each recommendation or series of recommendations made is in the best interest of the particular retail customer and does not place their financial or other interests ahead of the interest of the retail customer.”<sup>39</sup>

### Understanding Obligations to Customers and Member Firms

Training and mentorship programs can be valuable tools to integrate representatives into member firms and ensure that representatives understand their obligations to customers and member firms. These programs sometimes include a joint transition period during which both representatives are still registered to introduce the new representative to customers and share the departing representative's knowledge and experience.

Each representative should understand their responsibilities for a customer or account during any transition period. Importantly, each representative also should understand the scope of their permissible activity following registration or termination, including any retired representatives who are continuing to receive commission payments.

The risk of a former representative continuing improper involvement in a securities business may be greater where there is a personal or familial relationship between the representatives or the representative who will be taking over the book of business is less experienced or newly registered. Firms and representatives are reminded that FINRA has brought disciplinary actions against representatives for improper activity and receipt of transaction-based compensation by former representatives.<sup>40</sup>

### Customer Nonpublic Information

Subject to limited exceptions, Regulation S-P prohibits broker-dealers from disclosing nonpublic personal information about a customer to any non-affiliated third party, unless the customer receives notice and an opportunity to opt out of the information disclosure. As part of succession planning, member firms and representatives are encouraged to consider Regulation S-P's limitations on disclosure and use of customer nonpublic information and to review the firm's related procedures and privacy policy.

### Customer Choice

Importantly, customers are not bound by the firm's or representatives' succession planning decisions. Customers may choose not to work with the new firm or representative and instead transfer some or all their assets to another representative or firm. Customers who are interested in transferring their accounts can benefit from FINRA and SEC investor education materials explaining the account transfer process, including the SEC's Office of Investor Education and Advocacy [Investor Bulletin: Transferring Your Investment Account](#) and FINRA's [Understanding the Brokerage Account Transfer Process](#).

### **FINRA Disciplines Retiring Representative Who Improperly Retained and Sold Customer Nonpublic Information**

FINRA brought a disciplinary action against a representative who sought to sell his book of business in anticipation of retiring and:

- his firm advised him that sharing the customer nonpublic information outside of the firm was prohibited;
- without the firm's or customers' knowledge or consent, the representative improperly retained customer nonpublic information after resigning; and
- subsequently sold the information to a representative at another firm.

See [Robert F. Geiler, Letter of Acceptance, Waiver, and Consent \(AWC\) \(Oct. 18, 2021\) \(Case No. 2020067109401\)](#).

### Customer Communications

Member firms should consider how succession plans—and particularly how reassignments of customer accounts—will be communicated to customers.<sup>41</sup> The principle expressed in [Regulatory Notice 19-10](#) (April 2019) that customers should not experience an interruption in service due to a representative's departure is also applicable when a new representative will service a customer's account as part of a succession plan.

In addition, as expressed in *Regulatory Notice 19-10* and consistent with privacy and other legal requirements, member firms should communicate clearly, and without obfuscation, when customers ask questions about the departing representative. These communications may include, when asked by a customer, clarifying that the customer has the choice to retain their assets at the current firm and be serviced by the newly assigned representative or a different representative or transfer the assets to another firm.<sup>42</sup>

Member firms and representatives also are reminded to consider the requirements of FINRA Rule 2273 (Educational Communication Related to Recruitment Practices and Account Transfers) when a representative individually contacts former customers about transferring assets to the representative's new firm. Rule 2273 requires delivery of a FINRA-created [educational communication](#) by member firms that recruited the representative that highlights key considerations for the representative's former customers in transferring assets to the recruiting firms, and the direct and indirect impacts of a transfer on those assets.<sup>43</sup> For example, Rule 2273 may apply where a representative, in anticipation of retiring soon, sells their book of business and transfers to another member firm, and subsequently individually contacts his former customers about transferring their assets to the new member firm.<sup>44</sup>

#### Customer Seeks FINRA's Help Due to Lack of Communication

A customer contacted the [FINRA Securities Helpline for Seniors®](#) concerning his account. The customer noticed a new representative listed on the online profile for his account and several days later received a letter from the firm advising him about the new representative without any explanation about the change. The customer repeatedly contacted the new representative to discuss daily losses in his account, but the new representative and the firm did not respond to his calls.



## V. Questions for Consideration

The following questions—which reflect FINRA rules and administrative processes, firm practices and situations FINRA has observed—are intended to help firms and representatives develop and implement succession plans. This *Notice*, including these Questions for Consideration, does not create new legal or regulatory requirements or new interpretations of existing requirements, nor does it relieve firms of any existing obligations under federal securities laws and regulations. Member firms may consider the information in this *Notice* in developing new, or modifying existing, practices that are reasonably designed to achieve compliance with relevant regulatory obligations based on the member firm's size and business model. Moreover, some questions may not be relevant due to certain firms' business models, size or practices.

### Plan Development

- ▶ **Overall** – Has your firm developed and implemented an internal succession planning program for its representatives? As an alternative to an internal program, has your firm considered how to address potential external sales of firm assets or representatives' books of business?
- ▶ **Program Elements** – Does your firm's program address:
  - ▷ succession planning for representatives' life events, such as life events that require catastrophic or contingency plans or permanent departure due to retirement, resignation or relevant regulatory events that may require representatives to terminate their registration;
  - ▷ representatives who plan to return to the industry (*e.g.*, for departures due to illness); and
  - ▷ training for representatives in your firm's program, such as guidance on program requirements, mentoring and practical support for implementing succession plans?
- ▶ **Education, Tools and Resources** – How does your firm support representatives' succession planning, including:
  - ▷ Does your firm:
    - raise the issue of succession planning with representatives (*e.g.*, onboarding at the firm, during branch inspections, during periodic compliance meetings, through webinars, through email newsletters, in video or written testimonials from succession plan representatives or on internal firm websites); or
    - provide education or resources to representatives and other staff to raise awareness of and aid in succession planning?

- ▷ Does your firm maintain business consulting or practice management or similar staff who support representatives with developing and implementing succession plans, including coaching and assistance to those negotiating succession planning agreements?
- ▷ Does your firm provide staff with additional training and resources on succession planning agreements, guidelines for practice valuation, regulatory and other risks and other relevant topics?
- ▷ Does your firm offer any tools or services to aid in introducing or matching representatives who may be interested in succession planning?
- ▷ For introducing firms, have you discussed with your clearing firm whether the clearing firm can facilitate an introduction or suggest another introducing firm that may be interested in joint succession planning?
- ▶ **Key Roles** – Does your firm consider any additional steps that may be necessary for succession planning for key staff, such as the CEO, CFO and staff requiring certain registrations (*e.g.*, FinOP)? If your firm plans to hire new staff for these roles, have you considered the extended timelines that may be required for this process and designated current staff that would temporarily serve in these roles?
- ▶ **Recognition and Incentives** – If your firm does not require succession plans for representatives, does your firm offer special recognition, incentives or benefits to representatives to encourage representatives to participate in succession planning?
- ▶ **Diminished Capacity** – Does your firm address the risks of diminished capacity or health conditions that may impact representatives' ability to meet their obligations to customers and comply with legal requirements and firm procedures? Does your firm train representatives on spotting red flags; provide guidance on how to communicate about these issues with representatives and customers; and have a process for staff to internally escalate concerns?
- ▶ **Third-Party Vendors and Consultants** – Does your firm use third-party vendors or consultants to match representatives with potential succession planning partners, practice management and transition, practice valuation or other services?
- ▶ **Technology and Cybersecurity** – How does your firm address risks relating to technological changes required to support succession planning, such as:
  - ▷ has your firm developed a method for multiple representatives to safely and securely access the firm's transaction, account and compensation systems for the same customers?
  - ▷ particularly for small firms, has the firm addressed access to firm and regulatory reporting systems for continuity of operations, such as designating a back-up point of contact and providing relevant resources following an owner's death, incapacity or retirement?
- ▶ **Ongoing Review** – Does your firm review its and your representatives' succession plans on an annual or other periodic basis to confirm that they are still appropriate and reflect up-to-date information and resources?

### Program Elements

- ▶ **Written Agreements** – Does your firm require formal written succession plan agreements? If so, how does your firm address related requirements, including but not limited to:
  - ▷ Does your firm require succession planning written agreements be identical across all participants or may participants customize the agreements?
  - ▷ If your firm permits representatives to customize agreements, does your firm require some terms and conditions or permit representatives to customize the entire agreement? Moreover, does your firm review and evaluate the agreements for compliance with firm procedures, the federal securities laws and FINRA rules?
  - ▷ Does your firm provide sample succession plan agreements or assist representatives with developing agreements?
  - ▷ Do the written agreements:
    - Address roles and responsibilities for your firm and each representative named in the agreement, including changes to roles and responsibilities during the transition period, and name back-up successors if the representatives named in the agreement are not available or unwilling to continue participating in the plan?
    - Define temporary and permanent incapacity or disability and the related consequences for all representatives named in the agreement?
    - Provide stipulations for death of all representatives named in the agreement, including beneficiaries and successors?
    - Specify compensation prior to, during and after the transition period, including:
      - which accounts will be assigned to joint vs. individual production codes;
      - the percentage of commissions paid to each representative over the transition period; and
      - compensation for new vs. existing accounts and products and new vs. ongoing investments and assets?
    - Note differences in compensation and responsibilities for new clients vs. existing clients and new business vs. existing business?
    - Granting the succeeding representative access to appropriate firm information and firm and regulatory reporting systems?
    - Specify obligations related to non-public customer information for your firm and representatives?
  - ▷ Does your firm provide a process or a mechanism for representatives to address and resolve conflicts relating to their agreements?

- ▷ Does your firm review for representatives' compliance with the terms and conditions of agreements, including monitoring for any red flags of violations of agreements, your firm's procedures, the federal securities laws and FINRA rules?
- ▶ **Disclosure** – Does your firm require representatives to disclose to your firm when they begin or agree to a succession plan? If so, at what time in the process are representatives required to make these disclosures and to whom?
- ▶ **Review and Approval** – Does your firm require review or approval of succession plans?
- ▶ **Sales-Related Tools and Services** – Does your firm help representatives evaluate their own books of business and review potential purchase offers?
  - ▷ Does your firm provide any guidance on expected valuations with considerations for impact of independent consultant evaluations, representatives' commissions, practice expenses or other metrics?
  - ▷ Does your firm provide bridge financing or other financial support to facilitate purchases?
  - ▷ Does your firm help representatives evaluate potential purchase offers for legal and regulatory considerations and potential risks (e.g., bad actors who may be seeking access to customers' accounts and information for fraudulent schemes)?
- ▶ **Transition Period** – Does your firm have specific requirements (e.g., regarding customer engagement and communication) for representatives during any joint transition period during which both representatives are still registered?
- ▶ **Training** – Does your firm provide training on succession planning, such as:
  - ▷ program requirements and representatives' obligations to the firm and each other;
  - ▷ consequences of violating the terms and conditions of your firm's program agreements, the federal securities laws and FINRA rules;
  - ▷ transitioning customers between representatives, including approach, communication with customers, timing and responsibilities;
  - ▷ mentoring by retiring or departing representatives;
  - ▷ risks representatives could consider when evaluating offers to purchase their books of business; and
  - ▷ unique financial considerations for some customers, such as senior investors who may have more complex financial profiles?

- ▶ **Supervision** – How does your firm supervise its succession program or representatives' succession planning activities, including but not limited to:
  - ▷ reviewing email and other communications for red flags relating to succession planning, asset sales or other financial activities that may indicate unauthorized activities or misconduct;
  - ▷ monitoring communications for red flags that may indicate improper continued engagement by former representatives;
  - ▷ monitoring changes in customer trading for red flags that may indicate improper activity;
  - ▷ conducting customer check-in calls or other types of customer engagement to assess representatives' performance or review for improper activity;
  - ▷ reviewing representatives' customer complaints for red flags of misconduct; or
  - ▷ requiring representatives to provide relevant attestations or certifications about their succession planning eligibility or activities (*e.g.*, regarding the criteria specified in the SEC Staff Retired Representatives Guidance)?

#### **Financial Professionals**

- ▶ **Expertise and Experience** – How does your firm's program consider representatives' overall experience, expertise and professional qualifications when they enter into succession plans, including:
  - ▷ How does your firm research the professional backgrounds of the firms and individuals who are or may be parties to a succession plan?
  - ▷ For any newly associated person, as required by FINRA Rule 3110(e) (Responsibility of Member to Investigate Applicants for Registration), has your firm verified the accuracy and completeness of the information contained in an applicant's initial or transfer Form U4 (Uniform Application for Securities Industry Registration or Transfer) no later than 30 calendar days after the Form U4 is filed with FINRA?
  - ▷ Does your firm maintain guidelines or criteria to help representatives make decisions about selecting other representatives to whom they can transition their book of business?
  - ▷ Does your firm consider any familial or personal relationship between the representatives that may be relevant to succession planning?
  - ▷ Does your firm evaluate whether a representative has the training or experience that may be needed to service another representative's customers?

- ▶ **Disciplinary History and Other Regulatory Risks** – How does your firm address risks for representatives with a disciplinary history, including:
  - ▷ How does your firm address succession plans where these representatives are entering into plans with more junior representatives or representatives with similar disciplinary histories?
  - ▷ Does your firm permit representatives who are or would be put under heightened supervision to be part of a succession plan? If so, how does your firm address risks relating to these representatives, such as additional informal or formal monitoring or supervision?
  - ▷ Does your firm address risks relating to continued improper involvement by representatives who are leaving the industry due to a bar or legal or regulatory actions?
  - ▷ How does your firm or your firm’s representatives evaluate potential purchasers of representatives’ books of business, including the risk of bad actors seeking access to customers’ accounts and information for fraudulent schemes?
- ▶ **Professional Development and Support**
  - ▷ How does your firm support new representatives taking over retiring representatives’ practices where those retiring representatives may have had a particular focus on or expertise with certain financial issues or types of customers?
  - ▷ If your firm permits representatives to work in teams, does your firm address succession planning among team members, including allocation of responsibilities, timing of retirement or departure and compensation sharing?
  - ▷ Does your firm permit representatives to transition to non-registered roles and remain involved with customers? If so, how does your firm supervise these non-registered individuals to confirm that they are not acting in a registered capacity or providing investment advice or recommendations?
  - ▷ Does your firm communicate the existence of FINRA’s [MQP](#) to representatives who are leaving the firm?
  - ▷ Does your firm provide support, such as a matching service or other opportunities for connection, for representatives seeking to find representatives for succession planning?
  - ▷ Has your firm considered potential alternatives or steps if an issue arises with a designated successor representative (e.g., a termination or disciplinary event)?
  - ▷ If your firm has a DEI initiative, can the initiative or your firm’s program help to facilitate introductions and relationships between representatives who are interested in succession planning?

## Compensation

- ▶ **Continuing Commissions** – Do your firm’s succession plans allow for continuing commission payments to retiring representatives? If so, how does your firm address the following:
  - ▷ Does your firm maintain relevant procedures, including a reasonably designed supervisory system to comply with the applicable federal securities laws, SEA rules and regulations and FINRA rules?
  - ▷ How does your firm address commission-related misconduct (e.g., where representatives inaccurately altered or falsified joint or individual representative codes on trades in firm order entry systems to receive a higher commission)? For example, does your firm engage in additional formal or informal monitoring or surveillance of representatives who have engaged in such misconduct?
  - ▷ Does your firm review the continued eligibility of retired representatives to receive commissions pursuant to Rule 2040 and the SEC Staff Retired Representatives Guidance (e.g., by periodically checking [BrokerCheck](#) and the [Investment Adviser Public Disclosure \(IAPD\) website](#) for association with a new firm or reviewing for receipt of any customer’s complaints after a representative’s retirement)?
  - ▷ Does your firm monitor for improper payments to unregistered individuals, including former representatives?
  - ▷ Does your firm require retiring representatives to provide information about their heirs in case of the retiring representative’s death during the period of continuing commission payments?
- ▶ **Joint Representative Codes** – Does your firm use joint representative (or joint production) codes to calculate and allocate commissions payable to representatives? If so, does your firm:
  - ▷ specify circumstances under which representatives may use personal codes, rather than joint representative codes pursuant to your firm’s requirements and related representative agreements’ terms and conditions;
  - ▷ require representatives to provide justification for and obtain approval prior to making any changes to the code in the firm’s systems;
  - ▷ maintain operational controls to prevent representatives from altering any codes (e.g., technological blocks to prevent changes without approval);
  - ▷ monitor representatives’ code changes, including via surveillance and exception reports for red flags of misconduct; and
  - ▷ review and update your firm’s policies and procedures to address new disciplinary actions, regulatory developments and risks relating to commission sharing?

- ▶ **Compensation Reviews** – Does your firm perform periodic reviews of trade confirmations and compensation statements to confirm that they are consistent with Rule 2040 and the SEC Staff Retired Representatives Guidance, your firm's succession program requirements and related written agreements between representatives?
- ▶ **Conflicts of Interest**
  - ▷ Has your firm considered and addressed potential conflicts of interest for representatives in succession planning decisions (e.g., conflicts related to recommending accounts or products that are more likely to generate a higher valuation for the sale of the business or commission payments in retirement)?
  - ▷ Is there a reasonable basis to believe that each recommendation is in the best interest of the retail customer and does not place the firm's or representative's financial or other interests ahead of the interest of the retail customer?

#### Customer Communications

- ▶ **Methods** – How do your firm or your firm's representatives communicate succession plans to customers, particularly reassignments of their accounts?
  - ▷ What methods are used to communicate with customers (e.g., letters, emails, phone calls or in-person meetings)?
  - ▷ Does your firm provide form letters or other guidance to representatives on communicating succession plans to customers, such as timing of such communication prior to representatives' departures?
  - ▷ If your firm changes the representatives listed on customer account statements, does your firm provide any additional communication addressing this change or information about the new representative?
- ▶ **Content of Communications** – Do your firm or your firm's representatives communicate with customers about:
  - ▷ your firm's approach to succession planning and any relevant details;
  - ▷ what customers can expect from your firm and representatives during the transition period, including how your firm treats transitioning accounts and, if applicable, orphaned accounts;
  - ▷ the representative's departure from the firm and the transfer of the applicable accounts to the receiving representative pursuant to the SEC Staff Retired Representatives Guidance;
  - ▷ actions customers may take when encountering challenges or seeking to address concerns during and after the transition period, including how they can escalate any interruptions in service or other changes; and
  - ▷ customer choice about where and by whom the customers' assets will be serviced?



- ▶ **Required Customer Communications** – Has your firm considered the circumstances where FINRA Rule 2273's educational communication requirements would apply for any individualized contact?

#### Business Continuity Planning

- ▶ **BCP Triggers** – Do your firm's BCP procedures consider and address whether any key person event (e.g., a representative's or co-owner's illness, death or incapacity) could be an emergency or significant business disruption that triggers your firm's BCP?
- ▶ **Small Firms** – Particularly if your firm is a sole proprietorship or small firm, does your BCP address the risks of a key person event on the firm's continued ability to operate and access key systems and maintain your firm's customers' access to their funds and securities?
- ▶ **Emergency Contact Information** – Do your firm's BCP procedures address promptly updating your firm's emergency contact information in the [FINRA Contact System \(FCS\)](#) if a listed person is no longer associated with your firm?

#### MAP

- ▶ **CMAs and MatCons** – Do your firm's procedures consider and address whether a change in ownership would require your firm to file a CMA or MatCon with the MAP Group?
- ▶ **Two Principal Requirement** – Has your firm considered and planned for events that may cause the firm to cease to meet FINRA's requirement for firms to have at least two registered principals and one FinOp (except for sole proprietorships)?
- ▶ **RMA Engagement** – Do your firm's procedures incorporate contacting your firm's RMA for questions about whether to submit a CMA to the MAP Group or whenever a control person or owner departs the firm?

#### Customer Nonpublic Information

- ▶ **Disclosures** – Does your firm address representative succession planning in the firm's Regulation S-P procedures and privacy policy (e.g., by addressing whether a representative may disclose customer nonpublic information with a non-affiliated third party related to the sale of the representative's book of business)?
- ▶ **Succession-Related Risks** – Does your firm address risks relating to representatives who are planning for departure or retirement using customer nonpublic information (e.g., by conducting training on use of customer nonpublic information or monitoring for red flags of improper use of customer nonpublic information)?

## Endnotes

- 1 In addition to this *Notice*, in 2020, FINRA hosted a virtual panel on succession planning for small firms. A video recording of this panel is available for free on FINRA's [website](#).
- 2 While age is a risk factor, diminished capacity or cognitive decline are not limited to any age group. When cognition (*i.e.*, a combination of processes in the brain that includes the ability to learn, remember and make judgments) is impaired, it can have a profound impact on an individual's overall health and ability to perform tasks and responsibilities. See Centers for Disease Control and Prevention (CDC), [Subjective Cognitive Decline — A Public Health Issue](#) and [The Truth About Aging and Dementia](#).  
  
See also [North American Securities Administrators Association \(NASAA\) Report on Financial Professionals with Diminished Capacity](#) (July 2020). Among other things, the NASAA report recognizes concerns about compliance and employment requirements and highlights firms' emphasis on the proactive use of succession planning for financial professionals of all ages.
- 3 The [SIE](#) is an introductory-level exam that assesses a candidate's knowledge of basic securities industry information. The SIE is open to anyone aged 18 or older, including students and prospective candidates interested in demonstrating basic industry knowledge to prospective employers. Association with member firms is not required to take the SIE, and results are valid for four years. Passing the SIE alone does not qualify an individual for registration with a FINRA member firm or to engage in securities business. To become registered to engage in securities business, an individual must pass the SIE and a qualification exam appropriate for the type of business the individual will engage in. The individual must be associated with a member firm to take a qualification exam.
- 4 [FIND](#) allows eligible individuals to opt-in and share information with recruiting financial services firms. Participating firms can use FIND data to discover and contact candidates whose profiles match the firm's needs.
- 5 See, *e.g.*, Pew Research Center, [The Pace of Boomer Retirements has Accelerated in the Past Year](#) (Nov. 9, 2020).
- 6 See, *e.g.*, Pew Research Center, [Millennials are the Largest Generation in the U.S. Labor Force](#) (Apr. 11, 2018).
- 7 See, *e.g.*, [The Impending Succession Cliff: Implications and Insights for Advisors](#), Cerulli Associates (2019).
- 8 Demographic data reflects self-reported ages as of each representative's most recent annual registration with FINRA. To further explore the data collected by FINRA in the course of its work, FINRA's [2021 FINRA Industry Snapshot](#) provides a high-level overview of the industry, including information on the number of FINRA member firms and individuals entering and leaving the industry. In addition, to improve the transparency and utility of data FINRA collects, starting in 2021, FINRA provides access to the [data](#) behind the Industry Snapshot in an interactive grid format.
- 9 For example, as of January 2017, 13.57 percent of representatives were age 60 or older; 6.80 percent were age 65 and older; and 2.74 percent were age 70 and older.

The percentage of representatives at or approaching traditional retirement age is higher at small firms. As of the end of 2021, the percentage of representatives age 60 and older is 20.72 percent at small firms; 15.77 percent at mid-size firms; and 18.16 percent at large firms. FINRA defines small firm to include firms with between one and 150 representatives; mid-size firm to include firms with between 151 and 499 representatives; and large firm to include firms with 500 or more representatives. See FINRA By-Laws, Article I.

- 10 In 2015, NASAA adopted a [model rule on business continuity and succession planning](#). In 2020, NASAA adopted a model rule that consolidated and updated several existing NASAA model rules for state-registered investment advisers, including the model rule on business continuity and succession planning. The [press release](#) and [updated model rule](#) are available on NASAA's website. In addition, NASAA's Investment Adviser Resources and Publications Project Group published [Business Continuity & Succession Planning: Where to Start](#) as a resource for state-registered investment advisers.

In 2016, the SEC proposed adopting a rule under the Investment Advisers Act of 1940 to require SEC-registered investment advisers to adopt and implement written business continuity and transition plans reasonably designed to address operational and other risks related to a significant disruption in the investment adviser's operations. The proposed rule would have required advisers to adopt a transition plan that accounted for the possible winding down of the adviser's business or the transition of the adviser's business to others in the event the adviser was unable to continue providing

advisory services. See [SEC Release No. IA-4439](#) (June 28, 2016). The proposed rule was not adopted.

- 11 In 2021, FINRA published a revised [Small Firm Business Continuity Plan Template](#) to modernize the template and incorporate feedback received during the Rule 4370 retrospective review (e.g., to reflect increased use of remote work arrangements). The template is an optional tool for member firms.

For additional information on Rule 4370, see FINRA's [BCP key topic webpage](#) and [Regulatory Notice 21-44](#) (Dec. 2021) (summarizing FINRA's retrospective rule review of Rule 4370, the predominant themes that emerged from stakeholder feedback and resulting actions, and providing guidance to member firms).

- 12 Some MAP matters may be eligible for Fast-Track Review. The MAP Group's dedicated front-line team of examiners (the Triage Group) conduct an initial assessment of each New Member Application, CMA, MatCon, Membership Agreement Change and Two Principal Waiver Request to evaluate the risk, complexity, regulatory significance, completeness, scale and scope of each incoming matter. Matters determined to be low-risk, low-complexity, with little additional information needed may be deemed eligible for Fast-Track Review and expedited completion. Member firms must agree in writing to abbreviated turnaround times for responding to FINRA staff's requests for information for any matter deemed eligible for Fast-Track Review. See [Fast-Track Approval Process](#) for additional information on the factors used by the MAP staff in determining eligibility.

- 13 In April 2022, FINRA announced in [Information Notice 4/19/22](#) certain key operational changes in MAP to improve its effectiveness and efficiency, including establishing a centralized application intake function and aligning the program with the firm grouping model developed by FINRA's Member Supervision Department during its recent transformation. As part of these changes, MAP created a new centralized resource for firms when they are completing their applications with a dedicated telephone number for MAP Intake at (212) 858-4000 (Option 5 – Membership Applications) and email address [MAPIntake@finra.org](mailto:MAPIntake@finra.org). RMAs remain firms' main point of contact on changes to firms' business operations, but firms completing a CMA are encouraged to contact MAP Intake with any questions.
- 14 Firms are also reminded that they must promptly update [Form BD](#) by submitting amendments whenever the information on file becomes inaccurate or incomplete. This includes any change in ownership.
- 15 This type of CMA event has a unique timing consideration. A firm seeking to effect such change must file the CMA at least 30 days before making the change. Unlike the other events set forth under Rule 1017(a), a firm may effect the ownership change any time after 30 days has passed as long as the firm is not subject to an interim restriction that prohibits the transaction from closing before the MAP Group approves the CMA. See Rule 1017(c)(1); see also [Changes of Ownership or Control](#).
- 16 In a separate proposal, FINRA is considering amending Rule 1017 to require the submission of a CMA for a change in control person because the MAP Group has encountered situations where member firms changed their control person without filing a CMA. Under the proposed rule, submission of a CMA would be required for a direct or indirect change of member firms' control person (other than the appointment or election of a natural person as a partner, officer, director, principal of the member firm, or any person occupying a similar status or performing similar function, in the normal course of business) regardless of whether the change resulted from a change in equity ownership or partnership capital. See [Regulatory Notice 18-23](#) (July 2018) (seeking comment on a proposal regarding the MAP rules).
- 17 See Rule 1017(a)(6) and [Regulatory Notice 20-15](#) (May 2020).
- 18 See Rule 1017(a)(7) and [Regulatory Notice 21-09](#) (March 2021). The terms "final criminal matter" and "specified risk event," which are defined in FINRA Rule 1011, are based on events that are disclosed, or are or were required to be disclosed, on any applicable Uniform Registration Forms. See also [Mapping of Disclosure Categories for FINRA Rule 1017\(a\)\(7\)](#).
- 19 See [Two Principal Waiver Request](#).
- 20 Where there will be a newly associated person as part of succession planning, FINRA reminds member firms of the obligation under Rule 3110(e) to 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 U4 is filed with FINRA.
- 21 See, e.g., [Regulatory Notice 21-09](#) (March 2021) and [Regulatory Notice 21-34](#) (Sept. 2021).
- 22 See [Regulatory Notice 18-15](#) (April 2018) and [Regulatory Notice 21-09](#) (March 2021).

- 23 *See also* FINRA Rule 8311 (Effect of a Suspension, Revocation, Cancellation, Bar or Other Disqualification) and [Regulatory Notice 15-07](#) (March 2015). Rule 8311 provides that, if a person is subject to a sanction or other disqualification, member firms shall not allow such person to be associated with such firms in any capacity that is inconsistent with the sanction imposed or disqualified status, including a clerical or ministerial capacity. Member firms shall not pay or credit to any person subject to a sanction or disqualification, during the period of the sanction or disqualification or any period thereafter, any salary, commission, profit or any other remuneration that the person might accrue, not just earn, during the period of the sanction or disqualification.
- 24 In September 2022, NASAA [approved model rules](#) (the Exam Validity Extension Program (EVEP)) to extend the validity periods of certain examinations for broker-dealer agents and investment adviser representatives. The model rules align with recent changes to FINRA Rule 1240 (Continuing Education Requirements) that implement the MQP.
- 25 FINRA's [Financial Professional Gateway \(FinPro\)](#) provides individuals (current or former representatives) direct access to resources and tools to manage their securities registration information, including enrolling in the MQP.
- The MQP does not eliminate the two-year qualification termination period. Rather, it provides participants an alternative means of staying current on their regulatory and securities knowledge for up to five years following the termination of their registration(s). *See* [Regulatory Notice 21-41](#) (Nov. 2021) and the related [FAQs](#) for additional information.
- 26 Effective in 2015, Rule 2040(b) replaced NASD IM-2420-2 (Continuing Commission Policy) and codified FINRA and SEC staff guidance on the payment by member firms of continuing commissions to retiring registered representatives. *See* [Regulatory Notice 15-07](#) (March 2015). Pursuant to FINRA Capital Acquisition Broker (CAB) Rule 204 (Payments to Unregistered Persons), all CABs are subject to Rule 2040.
- 27 For purposes of Rule 2040, the term "retiring registered representative" includes individuals who retire from member firms (including as a result of a total disability) and leave the securities industry. In the case of death of the retiring registered representative, the retiring registered representative's beneficiary designated in the written contract or the retiring registered representative's estate if no beneficiary is so designated may be the beneficiary of the respective member firms' agreement with the deceased representative. *See* Rule 2040(b)(2).
- 28 Rule 2040(b) requires that: (1) a bona fide contract between the member firm and the retiring registered representative providing for the payments was entered into in good faith while the person was a representative of the firm and the contract, among other things, prohibits the retiring registered representative from soliciting new business, opening new accounts or servicing the accounts generating the continuing commission payments; and (2) the arrangement complies with the applicable federal securities laws, SEA rules and regulations.
- 29 *See* [SEC No-Action Letter to the Securities Industry and Financial Markets Association](#) (Nov. 20, 2008) and [SEC No-Action Letter to Amy Lee, Chief Compliance Officer, Co-CEO, Packerland Brokerage Services](#) (March 18, 2013).

The latter letter expands on the first letter to provide that the SEC staff would not recommend enforcement action if a firm were to continue to pay commissions to the retired representative (or their estate) for new accounts opened by, or new money received from, existing customers of the retiring representative that were assigned to a servicing representative in connection with the retiring representative's retirement.

While Rule 2040(b) does not expressly list each condition set forth in the prior SEC Staff Retired Representatives Guidance, Rule 2040(b) incorporates the prior guidance by expressly requiring that any proposed arrangement with a retiring representative must comply with the federal securities laws and SEA rules and regulations. See [letter](#) from Kosha Dalal, FINRA, to Brent J. Fields, Secretary, SEC, Re. File No. SR-FINRA-2014-037 (Proposed Rule Change to Adopt FINRA Rules 0190 (Effective Date of Revocation, Cancellation, Expulsion, Suspension or Resignation) and 2040 (Payments to Unregistered Persons) in the Consolidated FINRA Rulebook, and Amend FINRA Rule 8311 (Effect of a Suspension, Revocation, Cancellation, or Bar)) (Dec. 23, 2014).

- 30 In addition to federal law and FINRA rule requirements, firms and representatives should consider the applicability of relevant state law requirements for commission payments to retired representatives.
- 31 Alternatively, the retiring representative must have been continuously a member of a team for a minimum of three years as of the Retirement Date, and that team must have been in continuous existence as part of that, and (if applicable) a prior firm for a minimum of three years as of the Retirement Date.
- 32 For this purpose, appropriate conduct includes a low incidence of investment-related customer complaints, arbitrations or litigation involving the retiring representative and either settled or decided for \$25,000 or more during the three years prior to the Retirement Date and a low incidence of pending investment-related complaints, arbitration or litigation during the three years prior to the Retirement Date. In addition, the retiring representative must not be subject to a statutory disqualification resulting from any action of, or proceeding brought by, the SEC or any self-regulatory organization for which the sanction is currently in effect (or was in effect during any part of the three years prior to the Retirement Date).
- 33 The retiring representative must acknowledge this limitation on customer contact in writing.
- 34 The retiring representative also may not be associated with any bank, insurance company or insurance agency (affiliated with the firm or otherwise) during the term of their agreement if the retiring representative's activities relate to effecting transactions in securities.
- 35 This one-year requirement can be reduced to six months if the firm has established a transition period whereby the retiring representative works with the receiving representative to jointly service the account holders who are subject to the agreement. If there is more than one receiving representative who will be jointly servicing the accounts under the agreement with the retiring representative, and one of the receiving representatives has less than three years of industry experience or has been with the firm for less than one year, then that person can jointly service the client accounts of the retiring representative so long as the firm arranges for a more senior person to mentor that person for at least one year.

- 36 See, e.g., [Richard Matthew Brendza, AWC \(May 3, 2022\) \(Case No. 2018058614301\)](#); [John Patrick Miller, AWC \(Dec. 22, 2021\) \(Case No. 2020068810301\)](#); [Michael Peter Dmytryshyn, AWC \(Jan. 28, 2022\) \(Case No. 2021070570201\)](#); and [Thomas Alva Foster, AWC \(Jan. 31, 2022\) \(Case No. 2021071276801\)](#).
- 37 The SEC Staff Retired Representatives Guidance requires that the firm establish parameters for up to five years following retirement and a percentage scale (that is either fixed or decreases the percentage the retiring representative receives each year) regarding the sharing of commissions by the retiring representative and the receiving representative.
- 38 [SEC Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Conflicts of Interest](#) (Aug. 3, 2022) (SEC Staff Bulletin on Conflicts).
- 39 *Id.*
- 40 See, e.g., [James Alan Schumaker, Letter of Acceptance, Waiver, and Consent \(AWC\) \(Feb. 18, 2021\) \(Case No. 2019061887701\)](#) (where the representative permitted and enabled his father, a former representative who had been barred and statutorily disqualified from the securities industry, to conduct a securities business, including attending in-person customer meetings to discuss brokerage account strategy, emailing with customers about their brokerage account statements, maintaining an office within the branch location and sharing a phone line with the branch location); and [Adam James Makkai, Hearing Panel Decision \(June 3, 2021\) \(Case No. 2018058924502\)](#) (where the representative violated Rules 2010 and 2040 by improperly paying commissions to a former representative who was terminated for misconduct as consideration for the terminated representative's book of business).
- 41 The SEC Staff Retired Representatives Guidance requires that, prior to the Retirement Date, the firm inform the account holders of the applicable accounts in writing of the retiring representative's departure from the firm and of the transfer of the applicable accounts to the receiving representative.
- 42 In [Regulatory Notice 19-10](#), FINRA also recognized that member firms' different business models give rise to different approaches to managing the customer relationship, and that the expectations regarding member firms' handling of a departing representative will vary accordingly.
- 43 See also [Regulatory Notice 16-18](#) (May 2016) and [Frequently Asked Questions Regarding FINRA Rule 2273](#).
- 44 For additional context, FINRA has previously interpreted Rule 2273 as not applying to circumstances where a customer's account is proposed to be transferred to a new member via bulk transfer or due to a change of broker-dealer of record. FINRA believes that the considerations set forth in the educational communication do not have the same application in the context of a bulk transfer as they do when a customer has a viable choice between staying at their current firm with the same level of products and services or transferring assets to the recruiting firm, with the attendant impacts. See [letter](#) from Jeanette Wingle, Assistant General Counsel, FINRA, to Brent J. Fields, Secretary, SEC, Re. File No. SR-FINRA-2015-057 (Proposed Rule Change to Adopt FINRA Rule 2273 (Educational Communication Related to Recruitment Practices and Account Transfers)) (March 17, 2016).

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