

## FINRA beefs up required procedures for preventing insider trading

A new **FINRA** policy takes effect April 20 that will formally require firms that issue research reports to establish policies and procedures that erect effective barriers between their traders and those working on research reports. The policy is part of a larger rule that addresses trading ahead of research reports.

The change in the barriers provision is among modifications to **NASD** Interpretive Material 2110.4, which FINRA is adopting as new FINRA Rule 5280.

Under the interpretive material, firms had the option of establishing “Chinese Wall” information barriers, FINRA noted in a recent podcast on the topic. Now, firms will be required to set up internal controls reasonably designed to restrict or limit information flow between those who know about the timing and/or content of research reports, and those who work in sales and trading.

FINRA officials emphasized that the trading desk is prohibited from establishing a security’s position if the trading desk has non-public advance knowledge of what’s in a research report about that security, or if it knows when the report will be issued. The same applies to derivatives of that security, they said.

This is FINRA’s back-door way of strengthening insider trading prohibitions, said **Amy Lynch**,

president of **FrontLine Compliance, LLC**, a regulatory compliance consulting firm based in Alexandria, Va. It also comes on top of the requirements for information barriers that are required under Rule 2711, which are designed to prevent the investment banking function from pressuring those who write research reports.

“Firms with good insider trading policies and procedures that specifically address the potential conflicts that arise between research, investment banking, and trading should already be prepared for this rule. It’s the ones that don’t that need to take action now,” Lynch said.

Examples of some of the procedures to establish a Chinese Wall, Lynch said, include: **1)** prohibiting research analysts from discussing proposed or pending research reports or trading objectives with trading staff. Have staff attest annually that they obey this prohibition, and **2)** physically separating research and trading so they’re on different floors or on opposite sides of the room and can’t easily overhear each others’ conversations.

Tips: Conduct trading reviews regularly to look for any front-running. In addition to personal trading reviews of employees of the research and trading departments, conduct detailed firm-wide reviews of trading in customer accounts and proprietary accounts, Lynch advised. “Firms must remember to include ALL of their own proprietary accounts when setting up the cross-reference accounts for electronic personal trading and tracking systems. It’s a simple step that can be overlooked,” Lynch said. ■

### Best practices for approving new products in a time of volatility

LIVE WEBINAR! Tuesday, April 28, 2009  
2:00 p.m. - 3:30 p.m. ET

**REGISTER TODAY!**

Get all the benefits of a seminar without leaving your office!

[www.bdweek.com](http://www.bdweek.com)

800-260-1545

### Note to readers

All *BD Week* articles, dating back to October 1998, are available at [www.BDweek.com](http://www.BDweek.com). Articles are full-text searchable and indexed by topic. ■