

## An Inside Look into the FinOp Role

By Janice Parise

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Broker-Dealers vary greatly in size and business activities but one thing that is consistent across the board is that every member firm must have a designated Financial and Operations Principal (FinOp). NASD Rule 1022 mandates that every broker-dealer designate a qualified FinOp. The FinOp obtains this required qualification by passing either the Series 27 examination or the Series 28 examination. The determination of whether the Series 27 or the Series 28 qualification is appropriate for a firm will be based on the firm's activities. While the Series 27 exam qualifies a FinOp for all types of member firms, the Series 28 qualification is more limited and only appropriate for an introducing firm with limited activities as defined by Rule 1022. Ultimately, experience is the best qualification to ensure a FinOp will understand and appropriately apply the various regulatory rules and interpretations.

### What are a FinOp's responsibilities?

According to NASD Rule 1022, the FinOp's responsibilities primarily are:

- Final approval and responsibility for the accuracy of financial reports submitted to any duly established securities industry regulatory body;
- Final preparation of such reports;
- Supervision of individuals who assist in the preparation of such reports;
- Supervision of and responsibility for individuals who are involved in the maintenance of the member's books and records from which such reports are derived;
- Supervision and/or performance of the member's responsibilities under all financial responsibility rules promulgated pursuant to the provisions of the Securities Exchange Act of 1934;
- Overall supervision of and responsibility for the individuals who are involved in the administration and maintenance of the member's back office operations; and
- Any other matter involved in the financial and operation management of the member.

While this list of responsibilities applies to an existing firm, a FinOp also plays an important role in the member application phase of a broker-dealer. The FinOp will participate during the new member application process by assisting with financial projections, reviewing and approving expense-sharing agreements, establishing policies and procedures and approving and directing the funding of the firm.

### It doesn't stop there... requirements, deadlines, laws, and rules

Due to current trends, increased regulation and rule amendments, the FinOp, in practice, is responsible for much more than what is just documented in Rule 1022. There are regulatory requirements, filing deadlines and demands for transparency. A firm's FinOp is responsible for keeping current with federal and state laws as well as other rules relating to net capital and GAAP accounting practices. The FinOp must also keep abreast of regulator priorities, such as the Regulatory and Examination Priorities listing that are published each year by both the Financial Industry Regulatory Authority (FINRA) and U.S Securities and Exchange Commission (SEC).

### The Net Capital Rule basics

Net capital is described as a computation of a broker-dealer's liquidity and it's the responsibility of the FinOp to ensure that the computation is accurate and always current. Under FINRA rules, broker-dealers are expected to demonstrate compliance with the net capital rule on a moment to moment basis. Many firms do a formal net capital

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#### About the Author

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computation less frequently, sometimes only at month end, but it's the FinOp's responsibility to ensure that the member firm maintains sufficient net capital at all times. Depending on a firm's approved lines of business, it will be required to submit financial information and a net capital computation to its regulators, at a minimum, on either a month end or a quarter end basis. This submission is generally done electronically in the form of a Financial and Operational Combined Uniform Single (FOCUS) report due within 17 business days of the period end.

### **FinOp-eration: Cybersecurity**

These days one can't get through a work day without receiving an email or other solicitation for Cybersecurity training or solutions. Although there is no specific rule on the regulators' books regarding Cybersecurity mandates for broker-dealers, this issue is a priority for the regulators to ensure the security of customer and firm information. *The FinOP needs to take all necessary steps to ensure that the firm's books and records are secure.* Based on what we've been seeing in the field, it appears that the regulators are currently taking an information-gathering approach rather than a "gotcha" approach. When the regulators visit, a firm should be able to demonstrate that they are taking a proactive approach to cybersecurity threats. Firms should have written policies and procedures in place to protect firm and customer data from cyber-attacks. They should also be implementing a Cybersecurity testing program including risk assessment, as well as vulnerability and penetration testing. While some larger firms may have big budgets and resources to prepare for this issue, smaller firms may need outside assistance.

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*Smaller firms might want to check out [FINRA's "Small Firm Cybersecurity Checklist"](#) or hire an outside consultant to assist with testing and written procedures.*

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### **Your First line of Defense**

With the trend towards more regulation, the FinOp is on the front lines, serving as an integral liaison with the FINRA coordinator on a day-to-day basis, the regulatory examiners during an exam, and the independent auditors. To be able to liaise effectively, the FinOp must be well versed in the firm's activities, operations, and financial information. They need to be able to provide "color" and fully explain details regarding the firm's activities and supporting documentation for financials and net capital computations.

### **Making sure all hands-on deck are registered with the regulators**

FINRA Rule 1230(b)(6) requires that certain personnel conducting "back office" operations must be registered and pass a qualification exam to ensure that customers are protected in all areas of the member's business. Such individuals are known and registered as "Operations Professionals".

The three types of back office personnel that must register and/or pass a qualification exam to be considered an Operations Professional are:

- Senior management with direct responsibility over certain covered back office functions
- Supervisors responsible for approving or authorizing work or including work of other persons
- Other personnel with "the authority or discretion to materially commit a member's capital"

Therefore, any person with the authority or discretion to supervise back office functions needs to be registered with FINRA and pass a qualification exam. This could mean the person who has financial control based on their responsibility to prepare the books and records, to supervise those assisting in preparing the books and records or anyone with access to directly disburse funds of the member firm.

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The registration and qualification requirement might be the Series 27 (FinOp) or Series 99 exam (Operations Professional). However, a person that is in a support position, performing an ancillary or clerical function to assist in these covered functions, may need only submit fingerprints to FINRA to be considered as Non-Registered

Fingerprinted (NRF) personnel. This is a key distinction and the FinOP must ensure that all the financial back office functions are performed by personnel who are properly registered or fingerprinted.

### **Looking through the glass**

On the other side of things, it's important to ensure proper supervision of the member firm's FinOP. The other principals of the firm should periodically review the firm's Written Supervisory Procedures (WSP) as it relates to the supervision of the FinOP. A firm's WSP is described in FINRA Rule 3110 as "a system to supervise the activities of its associated persons that is reasonably designed to achieve compliance with the applicable securities laws and regulations and FINRA rules." The review of the WSP will give the principals an opportunity to ensure that the firm is in full compliance regarding the activities and supervision of the FinOP and other supporting personnel assisting the FinOP.

### **Why outsource the FinOp role?**

Based on statistics generated by FINRA, as of October 2017, there were 3,784 broker-dealers and 90% were considered small firms. Small firms are defined as 150 or less registered representatives, however most small firms have 20 or fewer representatives. Many small firms don't have the resources or manpower to keep up with changing accounting practices and regulation. Regardless, a small firm is subject to complying with the same rules and regulations as large firms that have more resources. Fortunately, FINRA allows certain member firms to use a part-time or outsourced FinOp. There are many benefits to using the services of an outsourced FinOp. A smaller firm may not have the resources to hire a qualified FinOp with the experience and level of talent they desire, usually due to the high price of the desired skill set. An outsourced FinOp may be a more cost-effective solution than an in-house full-time employee covering the same responsibilities. Adding a level of comfort, an outsourced FinOp is subject to the same rigorous supervision rules as a full-time employee of the broker-dealer. An outsourced FinOP can often add an added dimension of knowledge and experience based on their diverse client base where a full time FinOP's experience may be limited in scope.

### **FINRA's list of providers**

In an effort to assist the smaller firms, FINRA has launched a directory of Professional Providers called the "Compliance Vendor Directory". This is a listing of Compliance and Accounting professionals that specialize in providing services to broker-dealers. This directory can be a beneficial resource for firms and serve as a valuable listing to the professionals who provide the Financial and Operations Principal services described in this article.

In conclusion, the FinOp is an integral part of any firm's accounting and compliance effort and it's a tough job, but someone must do it.