

The Dodd-Frank Wall Street Reform and Consumer Protection Act and other regulatory issues

Top 10 considerations for broker-dealers

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Act) is landmark legislation designed to “restore responsibility in our financial system” and will have a significant impact on broker-dealers for years to come. Grant Thornton LLP’s Financial Services team is well-qualified to assist broker-dealers in addressing changing regulatory requirements. When it comes to evaluating the effect of the Act and other industry regulation, here are the top 10 considerations for broker-dealers, as well as ways Grant Thornton can help broker-dealers address them.

1. Risk management committees

Board risk committees are required for systemically important, publicly traded non-bank financial companies, as well as publicly traded bank holding companies with total assets greater than \$10 billion. The committee must include at least one expert with risk management experience. The current regulatory environment demands a robust risk management process even for firms that are not subject to this requirement.

How Grant Thornton can help: We provide comprehensive enterprise risk management (ERM) solutions and can help your firm implement governance, risk management and compliance systems, perform stress testing, and provide training. We can also evaluate the design and operating effectiveness of compliance, risk and control processes related to existing and new regulations.

2. Payment, clearing and settlement systems (“systemically important”)

The Financial Stability Oversight Council may designate a financial market utility or a payment, clearing or settlement activity as “systemically important.” The council has the authority to assist in determining the scope of, and participate in, on-site examinations of payment clearing and settlement systems by the primary regulators of those systems. This provision of the Act could impact a broad range of back-office activities, similar to the effect of compliance with the Group of Thirty’s clearance and settlement recommendations, which included advancement to a T+3 settlement and immobilization of physical certificates.

How Grant Thornton can help: We can help develop and implement payment, clearing and settlement system changes necessary to comply with emerging regulations. Broker-dealers should be prepared for challenges in implementing system improvements, because these improvements will be required even though specific risk management standards have yet to be defined. Our professionals can also assist in preparing for regulatory examinations of these systems.



Stay up to date on financial reform developments

The Act will make sweeping changes to the broker-dealer industry. Many of the specific rules have yet to be shaped by regulators, and broker-dealers must stay informed. To help broker-dealers navigate this uncharted territory, Grant Thornton has created the **Financial Regulatory Reform Resource Center**. For more information about how the legislation will affect your firm, emerging issues and to discuss your needs with a professional in our Financial Services practice, visit www.GrantThornton.com/financialreform.

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3. Regulatory readiness reviews

New regulatory agencies were created under the Act, such as the Bureau of Consumer Financial Protection (BCFP), an independent regulator within the Federal Reserve Board (Fed). The Office of Thrift Supervision will be eliminated, and its powers will be distributed among the Fed, the Office of the Comptroller of the Currency and the FDIC. The FDIC is now authorized to conduct examinations of systemically important companies.

How Grant Thornton can help: We can perform regulatory readiness reviews to assist broker-dealers in their preparation for regulatory examinations/inspections by identifying potential regulatory gaps and solutions to address them.

4. Significant new disclosures and reporting requirements

All broker-dealers will need to comply with the Act's significant new disclosure and reporting requirements. The Act requires additional notifications to retail customers, clear disclosures to investors regarding the terms of their relationships with broker-dealers and investment advisers, and it also restricts certain sales practices. In addition, the Act has called for a study to gather data for identifying systemic risk. The form and frequency of reporting this data will require a significant investment in systems in order to present this information efficiently to regulators, as well as to support broker-dealers' own risk management functions.

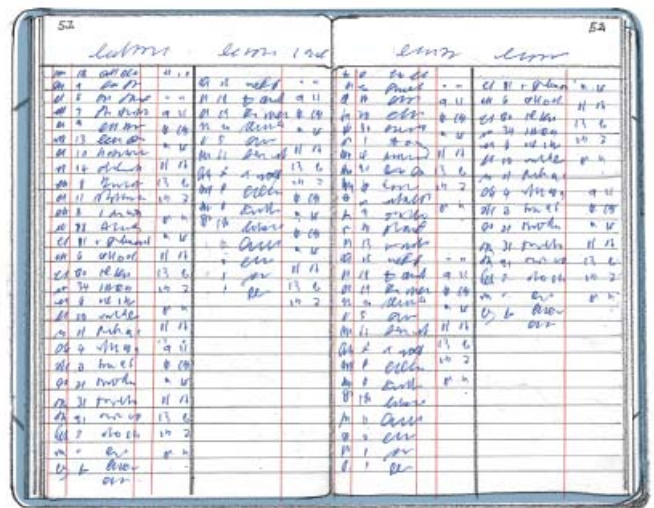
The SEC previously granted an exemption from the Public Company Accounting Oversight Board (PCAOB) requirement for broker-dealers to send reports to customers that were certified by a registered accounting firm. This exemption expired on Jan. 1, 2009; as such, reports must be certified by a firm registered with the PCAOB. It is also worth noting that the Act expands the reach of the PCAOB. Effective immediately, Section 981 of the Act authorizes the PCAOB to share information with foreign oversight authorities.

In addition, broker-dealers are required by SEC Rule 17a-5 to file monthly and quarterly reports concerning their financial and operational status (FOCUS reports). The Financial Industry Regulatory Authority (FINRA) has proposed additional financial information relating to income and expense line items to improve their review of broker-dealers' business operations. The present requirements have not been modified since 1975, and as a result, many of the activities are classified by default into the "other" line caption.

In July 2010, FINRA released for comment (Regulatory Notice 10-33) its requested supplementary schedule to the Statement of Income (Loss) page of FOCUS report Parts II and IIA. Comments were due by Aug. 18, 2010. In addition to providing detailed information for business activities previously combined in "other" categories, there is now a requirement to identify the top five underwritings for unregistered transactions for equity and debt offerings, including the number of customers to whom they were sold.

How Grant Thornton can help: We can advise on the proper procedures for compliance efforts, as well as perform transaction testing to help broker-dealers adhere to the new regulations and disclosure and reporting requirements.

With regards to FINRA compliance, our Business Advisory Services consultants can evaluate your systems to determine if it can capture to the level of specificity required on an accurate and timely basis. Our Audit professionals can assist in identification of required information, including the related hedges and appropriate netting of interest expense for matched book and conduit transactions. We can help broker-dealers evaluate the consistency of their internal controls, financial reporting and risk management of foreign subsidiaries and affiliates.



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5. Swap trading

Financial services companies will be required to centrally clear swaps. Historically, most broker-dealers have reflected swaps in a non-securities subsidiary in order to avoid significant capital requirements. Each swap entered into before the Act's enactment must be reported no later than 30 days after the date of the SEC or Commodity Futures Trading Commission (CFTC) interim final rule, or a time period determined by the relevant regulator. The use of a derivatives clearing organization will include revised margin and capital requirements for broker-dealers.

How Grant Thornton can help: Our professionals bring significant derivatives and systems experience to assist broker-dealers with the restructuring of swap operations, monitoring margin requirements and compliance with the new regulations, as well as accounting for the transactions going forward.

6. Potential mergers and acquisitions

The new regulatory environment may cause smaller broker-dealers to consider selling to avoid the regulatory burden.

How Grant Thornton can help: We have significant experience in performing accounting, tax, compliance and operational due diligence reviews to assist broker-dealers in identifying risks associated with mergers or acquisitions. We can help broker-dealers evaluate all aspects of merger and acquisition transactions.

7. Enhancing compliance processes and internal audit support

The Act's new rules and regulations will result in increased compliance burdens for broker-dealers.

How Grant Thornton can help: We can advise your firm on the design and performance of its internal audit and compliance programs, as well as share best practices in governance, policies and procedures, training programs, organizational structures, and board reporting.

8. Regulatory remediation

With these increased regulatory requirements, it becomes even more important to ensure any issues arising from regulatory examinations are addressed appropriately in a timely manner. The existing capital requirement will be replaced by a more robust standard by regulators; Treasury Secretary Timothy Geithner indicated that he expects the rulemaking process to move more swiftly than in the past.

How Grant Thornton can help: We can assist broker-dealers with remediating issues noted in regulatory examinations, including developing remedial action plans and performing testing to help address the issues properly.



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9. New and enhanced compensation and corporate governance oversight

The Act includes a number of key corporate governance and SEC provisions that impact public companies, including independence of compensation committees, nonbinding shareholder vote requirements (“Say on Pay”), enhanced compensation disclosures and clawback provisions.

How Grant Thornton can help: We can advise public company boards, audit committees, compensation committees and executive management on compliance with the new regulations.

10. Regulation D and Custody Rule

Broker-dealers must establish best practices for due diligence procedures with respect to Regulation D offerings and ensure a reasonable investigation (FINRA RN 10-22). Registered investment advisers who have custody of a client’s funds or assets must also comply with the SEC’s *Custody of Funds or Securities of Clients by Investment Advisers* (Custody Rule), which requires annual surprise examinations, internal control reports and the submission of Form ADV. Registered investment advisers must now report all related persons who are broker-dealers in Item 7 and Section 7.A of Schedule D of Form ADV.

How Grant Thornton can help: Our Valuation professionals can review and perform due diligence procedures, provide recommendations on the proper procedures for compliance efforts, provide training, identify and address red flags, and share best practices. We can also perform security counts, internal control testing and physical examination of customer securities in nonqualified control positions as required by the Custody Rule. In addition, our professionals can conduct readiness assessments to help investment advisers prepare for internal control testing.



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