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# 2024 capital markets regulatory outlook

Center *for*
**Regulatory Strategy**
**US**

# A message from the Deloitte Center for Regulatory Strategy

2023 confirmed the commitment and enthusiasm of powerful market regulators—active in rulemaking, surveillance, and enforcement. As the industry adapts to this more aggressive posture, we encourage our firms in the industry to enhance their response and leverage the tools assembled for compliance purposes to help drive value and opportunity for their business.

For our capital markets regulatory outlook this year, we've identified four key themes that firms likely will need to navigate in 2024: (1) winning the race for intelligence, (2) adapting to change, (3) navigating uncertainty and (4) investing in core competencies.

Entering 2024, regulators have demonstrated a commitment, focus, and intensity that at times has caught the industry by surprise. They have become more savvy in their approach to data, surveillance, and enforcement. Have you?

This year, we challenge our firms in the industry to pause on the continuous march to react and make space to improve their programs proactively through strategic investments that make the most of this particular moment for the industry—one that includes economic headwinds and heightened regulatory risk.

We hope that you find in our outlook a North Star amid the constellation of regulatory topics (some familiar, others new). We are here to help you set the course.

Sincerely,

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# Winning the race for intelligence

The introduction of open-source generative artificial intelligence (Gen AI) in 2023 was the starting point in a race for a new kind of intelligence—one that is not necessarily reliant on human knowledge or even proprietary AI models. Gen AI has the potential to rapidly scale activities in a cost-efficient manner. It could lower barriers to entry, if employed effectively, and increase competition in certain market segments if incumbent firms are slow to respond. We suggest three tactics to help capital markets firms "win the race for intelligence": (1) be as smart as the regulators and competitors, (2) manage to evolving regulatory expectations, and (3) maximize people resources and process efficiencies. Each of these represents a pillar of an effective AI strategy in the capital markets context that firms should execute on for sustained success.

## Be as smart as the regulators and competitors

Of course, algorithms have long played a crucial role in the capital markets, supporting activities such as trading, order routing and market making. In recent years, regulators have increased their reliance on machine learning and other models to conduct market surveillance. This has enabled regulators to become more effective in their core functions at scale. Now, the challenge for the industry is to ensure that they are a step *ahead* of the regulators. Rather than learning about misconduct from an enforcement action, compliance departments should look to harness the powers of AI and data collected for regulatory purposes to get smarter about their firm's activities. Initiatives like the consolidated audit trail (CAT) have added new levels of depth to regulators' surveillance activities and rising fines have added new urgency to the industry's efforts to be proactive.

Similarly, firms need to stay on top of their competition. As Gen AI pervades industries, processes, and use cases, firms may face lower barriers to entry and increased competition from new and familiar rivals. New entrants may be able to scale faster by effectively leveraging the powers of Gen AI and existing powerhouses should modernize their operations to remain relevant.

## Manage to evolving regulatory expectations

For industry, the challenge is twofold: It should embrace AI for business and compliance purposes and demonstrate to regulators that they effectively oversee their AI models. This has been an increasing focus of regulators and policymakers globally. In late 2021, the Bank for International Settlements (BIS) published a seminal paper on potential regulatory approaches to AI.[1] Among the paper's primary conclusions was the need for a "human in the loop." This principle serves as the foundation for various regulatory approaches under consideration, including the Securities and Exchange Commission's (SEC) predictive data analytics proposal issued last August.[2] Under the proposal, firms would need to evaluate and have policies in place to address any conflicts that may arise from use "or potential use" of "covered technologies" in investor interactions.[3] Under the proposed rule and as discussed by the BIS, firms would not be able to employ "black box" approaches to AI in investor interactions. The implications of the proposal and its application are far-reaching. While a final rule would likely be refined and potentially less far-reaching, this basic principle that firms must understand their models and what they are doing will remain.

Some critics of the proposal may suggest that firms already have obligations to address conflicts of interest under existing rules, such as Best Execution and Reg BI. Firms should be cautioned that, in light of these existing obligations, the market regulators are not dependent on the predictive data analytics proposal becoming final to begin bringing enforcement actions related to firms' use of AI. In fact, we have observed patterns of enforcement leading related rulemakings in many cases, and AI seems like an area primed to follow that pattern in 2024. Thus, firms may want to borrow from what has been proposed—despite not having firm obligations—to bolster themselves against enforcement related to existing requirements.

Beyond the market regulators, the policy landscape for AI regulation is picking up pace. In September 2023, the Biden administration published principles for an "AI bill of rights,"[4] and in October, the president signed an Executive Order outlining the agencies' approach to AI.[5] On Capitol Hill, high-profile hearings have not yet produced a legislative outcome. As the United States has not yet addressed data regulation, it is hard to imagine AI legislation that does not tackle some of those issues, further complicating an already difficult topic. As such, legislation may remain elusive for a number of years and particularly in the face of the 2024 election cycle. Nevertheless, firms should pay close attention to the wider environment and be on alert for impacts to and opportunities for their AI strategy in the broader policy debate.

### Maximize people resources and process efficiencies

Part of winning the AI race will be using human resources and intelligence wisely. As AI increasingly automates tasks, human managers need to effectively leverage and oversee those tools. As firms take a hard look at staffing, two priorities come into view: (1) the need to use people and tools wisely and in complementary ways, and (2) the need to upskill people resources for the AI future. As already discussed, Gen AI is lowering barriers to entry and creating opportunities to scale rapidly. These pressures are likely to force incumbent firms to reconsider their staffing levels.

At the same time, as reliance on AI tools grows, so does the need to oversee them effectively. Human managers will increasingly rely on non-human "employees" to generate work product. This will require routines and skill sets that are new to most managers. Once a firm's staffing levels reach equilibrium, the task of upskilling people resources should be a focus. The abilities to effectively employ and oversee AI tools are crucial management skills that firms should cultivate in their people resources. As discussed above, regulators have indicated that black-box automation will not be tolerated, which accelerates the imperative for firms to integrate their AI and upskill their people resources to effectively oversee it.

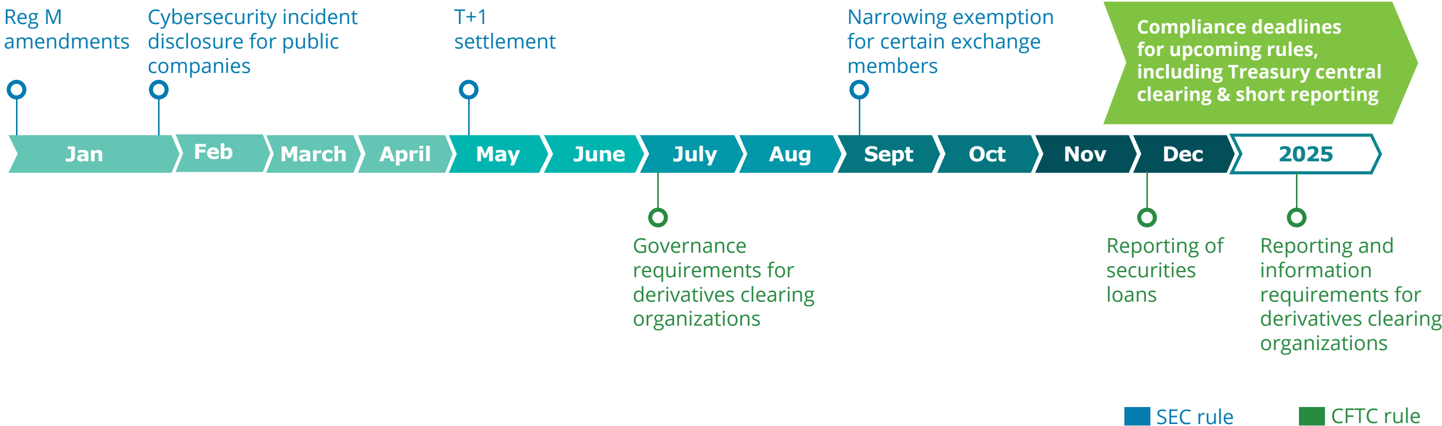
# Adapting to change

For the year following the introduction of open-source Gen AI, it's no surprise that we have identified a theme of "adapting to change" for our annual outlook. Indeed, it seems that tectonic shifts are taking place and, as with movement of the Earth's plates, the pace of change is uneven. In a compliance context, however, changes often come with deadlines, and capital markets firms will have several of those to contend with in 2024.

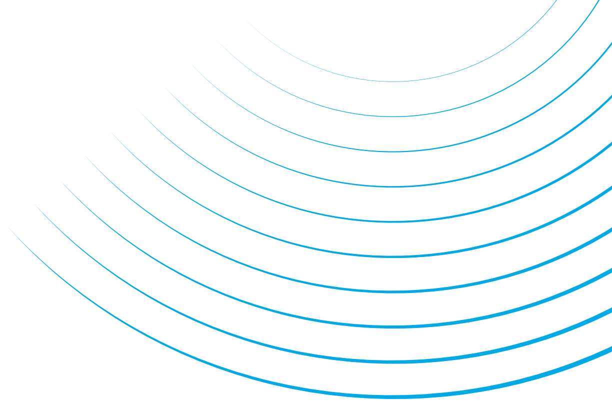
The end of 2023 saw the SEC accelerate its adoption of final rules that will transform capital markets compliance. Several stacked compliance dates in 2024 will keep firms busy throughout the year (Figure 1). These new rules from the SEC and Commodity Futures Trading Commission (CFTC) will affect business lines throughout the organization, from the Board to finance and technology (Figure 2). The capital markets regulatory agenda will have an impact on a wide range of firms, from brokers (impacting and executing) to market makers and swap dealers (Figure 3).

The end of 2023 saw the SEC accelerate its adoption of final rules that will transform capital markets compliance.

**Figure 1. 2024 compliance dates**




Source: Deloitte analysis of regulatory agenda



## Prepare for T+1

The largest and most significant, of course, is the transition to T+1 settlement. In February 2023, the SEC finalized amendments requiring the industry to transition to a T+1 settlement cycle by May 2024.[6] Presently, some firms are behind in their preparations and may be at risk of missing the compliance date. They are unlikely to meet a sympathetic SEC when the deadline arrives: Despite significant industry pushback on the May 2024 date, the agency proceeded with that deadline anyway given its imperative to reduce marketwide risk associated with longer settlement time frames.

To get back on track for the transition to T+1, firms should refer to projected transition timelines and compare their current progress with what has been put forward.[7] At this stage, firms should be concluding industry-wide testing. Those firms that are significantly behind projected timelines may need additional help to meet what we expect to be a firm deadline from the regulator.

## Central clearing for US Treasuries

On December 13, 2023, the Securities and Exchange Commission (SEC) approved a Final Rule that will require firms to begin centrally clearing eligible trades in Treasury securities by the end of 2025 and repurchase agreement (repo) transactions by June 2026. The Proposed Rule was introduced in fall 2022 to address risks associated with market volatility and liquidity problems, and SEC Chairman Gary Gensler stated that the new rule will "reduce risk across a vital part of our capital markets in normal times and stress times." This rule is part of a package of reforms to the Treasury market the SEC is pursuing that will have a significant impact.

To offset the increased margin requirements for direct and indirect covered clearing agency (CCA) participants, as a result of the Final Rule, the SEC also announced changes to the customer reserve formula outlined in SEC Rule 15c3-3(a). Broker-dealers must now include customer margin required and on deposit at a CCA in the US Treasury market as a debit in the customer reserve formula, subject to certain conditions, thereby freeing up the broker-dealer's cash and securities to meet their margin obligations at the CCA. The amendments follow a phased deadline approach pursuant to the following dates:

- March 31, 2025: Changes regarding the separation of house and customer margin, the broker-dealer customer protection rule (15c3-3(a)), and access to central clearing required.
- December 31, 2025: Eligible secondary market transactions must be submitted through netting.
- June 30, 2026: Cash and repurchase transactions collateralized by US Treasuries.

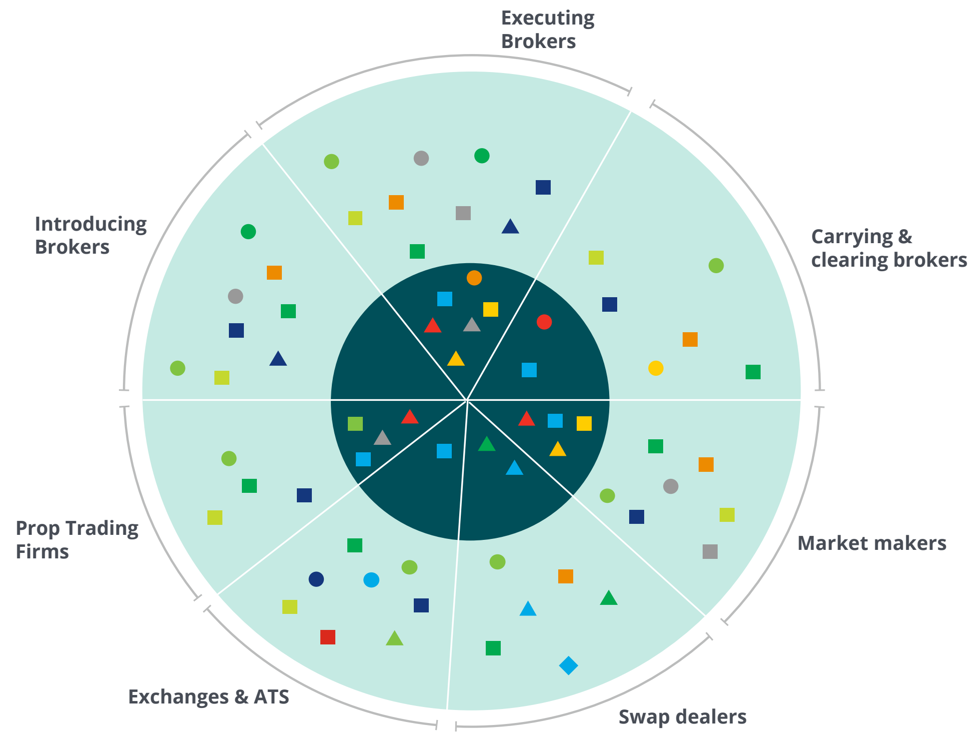
## Register under amended Exchange Act exemption

In August 2023, the SEC adopted amendments to an exemption under Section 15(b)(8) of the Exchange Act that will require an estimated 64 proprietary trading firms to register as dealers with FINRA by September 2024.[8] In addition to obtaining FINRA membership, these firms will be required to report to FINRA's Trade Reporting and Compliance Engine (TRACE) among other requirements. For regulators, these amendments address a "gap" in their oversight; but for impacted firms, these changes will likely have serious consequences for their compliance programs. Obtaining FINRA membership is the essential first step that affected firms must pursue. The FINRA Form New Membership Application (NMA) process, which is reviewed by FINRA's Membership Application Program (MAP) Group, is an involved undertaking, and firms likely will need outside assistance to successfully guide them through the process.

**Figure 2. Relative impact of regulatory agenda on business lines: Final rules**

Source: Deloitte analysis of regulatory agenda

### Figure 3. Capital markets regulatory agenda by entity type impacted




**Legend**

- Daily computation of reserve requirements
- Prohibition of Conflicted Practices for Broker-Dealers That Use Certain Covered Technologies
- Regulation ATS Modernization
- Clearing Agency Recovery and Wind-Down
- Volume-Based Exchange Transaction Pricing
- Prohibition Against Conflicts of Interest in Certain Securitizations
- Regulation Best Execution
- Regulation Systems Compliance and Integrity
- Reporting of Security-Based Swap Positions
- Definition of exchange
- Disclosure of Order Execution Information
- Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders
- Further Definition of Dealers
- Order Competition Rule
- Special Purpose Acquisition Companies
- Modernization of Beneficial Ownership Reporting
- Regulation S P: Privacy of Consumer Financial Information and Safeguarding Customer Information
- Prohibition Against Fraud, Manipulation, and Deception in Connection With Security-Based Swaps; Prohibition Against Undue Influence Over Chief Compliance Officers
- Rules Relating to Security-Based Swap Execution and Registration and Regulation of Security-Based Swap Execution Facilities
- Removal of References to Credit Ratings From Regulation M
- Electronic Submission of Certain Materials Under the Securities Exchange Act of 1934; Amendments Regarding FOCUS Report
- Short Sale Disclosure Reforms
- Amendments to Exchange Act Rule 3b-16 re Definition of "Exchange"; Regulation ATS and Regulation SCI for ATSs That Trade U.S. Government Securities, NMS Stocks and Other Securities
- Order Competition Rule
- Amendments to NMS Plan for the Consolidated Audit Trail-Data Security
- Loan or Borrowing of Securities
- Standards for Covered Clearing Agencies for U.S. Treasury Securities and Application of the Broker-Dealer Customer Protection Rule With Respect to U.S. Treasury Securities

- Pre-rule stage
- Proposed rule stage

Source: Deloitte analysis of regulatory agenda

2024 capital markets regulatory outlook

# Navigating uncertainty

A significant theme that we identified in last year's outlook was regulatory churn, and at the outset of 2024, the landscape looks familiar. As the Federal Reserve Board (FRB) continues to look for a soft landing, markets face an indeterminate outlook with respect to interest rates and the US economy as well as more frequent geopolitical shocks. At the same time, US regulators have undertaken numerous interventions that profoundly impact market operations. In March 2023, for example, FRB took the unprecedented step of supporting the banking sector and treasury market through the Bank Term Funding Program (BTFP), which allowed banks to exchange US treasuries for their face amount, irrespective of the current market values.[9]

The SEC has amassed a trove of significant outstanding rule proposals (Figure 4), and the fate of many portions of this agenda appears to remain a topic of frequent conjecture by industry. Proposed changes to the treasury and equity markets would have sweeping impacts on market operations. While reducing the settlement cycle for bonds and US equities has been an ongoing and impactful effort in recent years, the SEC is currently weighing major reforms to equity market structure that would upend Regulation NMS and order execution as it currently exists.[10] The most impactful of the proposals under consideration—the order competition proposal—would require all retail orders to be routed to an open auction at an exchange prior to being filled by a wholesaler, market-maker, or internalizer.

**Figure 4. Forthcoming SEC rules for capital markets**

Approval Date
Proposal Date
Effective Date
Reg-flex Action Date
Comment Deadline
Compliance Date

2022: Q1 Q2 Q3 Q4
2023: Q1 (M1 M2 M3) Q2 (M4 M5 M6) Q3 (M7 M8 M9) Q4 (M10 M11 M12)
2024: Q1 (M1 M2 M3) Q2 (M4 M5 M6) Q3 (M7 M8 M9) Q4 (M10 M11 M12)

Treasury Clearing
Public Company Cybersecurity Risk Governance
Prohibition Against Fraud, Manipulation, and Deception in Connection With Security-Based Swaps; Prohibition Against Undue Influence Over Chief Compliance Officers
Removal of References to Credit Ratings From Regulation M
Narrowing Exemption for Certain Exchange Members
Shortening the Securities Transaction Settlement Cycle (T+1)
Modernization of Beneficial Ownership Reporting
Short Sale Disclosure Reforms
Loan or Borrowing of Securities
Governance Requirements for Derivatives Clearing Organizations
Reporting and Information requirements for Derivatives Clearing Organizations
Swap facilities
Short position
Securities lending

Proposed
Compliance period
SEC Rule
CFTC Rule

Source: Deloitte analysis of SEC regulatory agenda

Other significant reforms are comprised of proposals to enhance risk management for central counterparties in US Treasurys, expanding the definition of dealer, and redefining alternative trading systems. Each of these rules is impactful on its own. Together, these rules could reshape the US capital markets.

The SEC has faced pressure to assess the intersecting impacts of the various proposed reforms more thoroughly. Some observers, including certain members of Congress, have critiqued the agency for pursuing so many significant reforms at once and accused the agency of not understanding the totality of intersecting impacts.[11] Indeed, unintended consequences are not unusual, but some have raised concern that the volume and pace of change could result in more negative externalities than is typical.

Nevertheless, there is much to learn from the agency's prolific work over the past several years. SEC staff have put forward many wide-ranging proposals. Even if some take many years to finalize, the efforts of 2022 and 2023 will form the bedrock of future thinking on many of these topics. The presidential election in 2024 could seal the fate of any unfinished agency work and appears to be already motivating rule timelines. To avoid potential scrutiny under the Congressional Review Act, agencies face a May 2024 cutoff for rule finalization. We expect this deadline to be top of mind for regulators, especially for politically controversial rules.

Significant court cases to be decided in 2024 add an additional layer of complexity. In *Loper Bright Enterprises v. Raimondo*, the Supreme Court has agreed to hear a direct challenge to Chevron deference—a long-standing doctrine that compels federal courts to defer to agencies' interpretation of ambiguous congressional statutes. In recent years, the Supreme Court has indicated that Chevron deference cannot be universally applied but has not yet sought to replace it. If the Supreme Court elects to overturn the 1984 case that established the precedent, there could be wide-ranging and possibly unpredictable impacts on the administrative state. There are also several high-profile enforcement cases being litigated in the digital asset sector that could spill over into broader impacts. At issue in each of these cases is the classification of certain assets as securities, and court opinions may indicate how broadly the agency may apply the Howey test to other use cases, including non-fungible tokens (NFTs) and syndicated loans
among others.

Judicial review serves as an important check on agency overreach, and an evolving or stricter interpretation of agency authorities could put significant portions of the current regulatory agenda in jeopardy. Tensions between tackling an ambitious agenda and protecting the institution are complicating the SEC's path to rule finalization as industry and regulators alike weigh litigation strategy. Additionally, a change in administration in 2024 could result in an abrupt shift in agency priorities. These two slower-moving trends have the potential to capsize the current regulatory environment, though not overnight. More broadly, increasing polarization and a swinging political pendulum present challenges for business regardless of which party is in power. An abrupt pivot in early 2025 away from policies currently being pursued would leave many firms with wasted expenditures, nevertheless.

Regardless, the legislative calendar in 2024 will be hamstrung by the election cycle making sweeping financial services packages unlikely. Certain industries and technologies (e.g., digital assets and blockchain) may suffer from a lack of legal clarity pending the outcome of several high-profile enforcement litigation cases. In recent years, fractured dynamics in both parties have illustrated the challenges of governing even for the party in power. Razor-thin margins in both chambers of Congress can leave outsize power in the hands of very few members. As the fringes in both parties become increasingly anti-business, industry may likely rely on centrist voices of either party to protect its interests.

# Investing in core competencies

## Enhance cybersecurity

CAT is neither the first nor the last cyber target in the financial services industry, and public firms will be under new obligations in 2024 to disclose cyber incidents and demonstrate cybersecurity expertise in their governance. Cybersecurity has long been a business imperative, but the new regulatory requirements place additional pressure on firms to prevent incidents before they occur.

In July 2023, the SEC adopted final rules governing public company cybersecurity disclosure. Among the new requirements, which apply to all public companies and went into effect at the end of 2023, firms are required to disclose material cyber incidents to the SEC within four business days. The SEC's materiality standard, which is central to its disclosure rules for public companies, relies on the presumption that a "reasonable investor" would view the information "as having significantly altered the 'total mix' of information available to them."[12] Said differently, a "reasonable" firm might expect material information to impact stock price at least in the short run. Thus, firms may be challenged to make determinations about the materiality of a specific cyber incident, and more importantly, they have additional incentive to prevent such incidents from occurring in the first place.

These new rules are the first in a series of efforts by the market regulator to set a floor for firms' cyber governance. A trio of cyber-related proposals for broker-dealers are set to be finalized in 2024, including amendments to Reg SP and Reg SCI and a new proposed Rule 10 that would establish cybersecurity standards for broker-dealers.[13] When finalized, these rules will establish stricter standards for broker-dealers and impose overlapping requirements on them. Figure 5 illustrates the interaction among the three rules as proposed.

**Figure 5. Comparison of proposed privacy and cybersecurity rules for broker-dealers**

| | Regulation S-P | Regulation SCI | Proposed Rule 10 |
|---|---|---|---|
| | *Protects customer information by adopting an* ***incident response program*** *and notifying individuals affected by certain types of data breaches* | *To expand the scope of entities subject to* ***Regulation Systems Compliance and Integrity (SCI)*** *and to update other regulation requirements* | *Proposal for* ***new Rule 10, Form SCIR, and related amendments (18a-10)*** *to require entities that perform critical services to support operations of the US market to address their cybersecurity risks* |
| **Purpose** | Reg S-P was adopted to **safeguard customer records and information**, and prevent unauthorized access | Reg SCI was adopted in 2014 to **strengthen the technology infrastructure** of US security markets | The purpose is to **protect market entities and investors** from harmful impacts of cybersecurity incidents |
| **Applicability** | There are **two rules — safeguards rule and disposal rule** — which cover broker-dealers, investment companies, registered investment advisers and transfer agents. The **substituted compliance provisions** in the **safeguards rule will apply to notice for registered broker-dealers** | **Covered entities**- NSE, RCA, RSA, Municipal Securities Rulemaking Board, Alternative Trading System, disseminators of consolidated market data, competing consolidators of market data meeting, certain exempt clearing agencies, broker-dealers registered with the commission **under Section 15b** | **Covered entities** – Broker-dealers, clearing agencies, NSE, MSRBs, transfer agents, and SBS Entities<br>**Non-covered entities** – Subscription-based mutual funds, effecting securities transactions to facilitate M&A or business sales; engaging in private placements for clients or underwriting for issuers |
| **Proposed recordkeeping amendment** | The recordkeeping provision covers institutions that are required to **make and maintain written records documenting compliance** with the requirements of the safeguards rule and disposal rule. | The regulation updates **recordkeeping provision and Form SCI** consistent with the reg amendments. | Proposal to **exclude record maintenance** from its scope and **preserve requirements of Rule 18a-6** as they pertain to the records required to be made pursuant to proposed Rule 10 |

Source: SEC.

### Enhance data collection, governance, and maintenance

Related to cybersecurity, data collection and management present both an obligation and opportunity for firms. CAT and other reporting obligations require firms to assemble treasure troves of data for their regulators. As discussed in our introduction, the market regulators have improved their ability to leverage the masses of data at their fingertips and utilize machine learning and other analytical methods to drive insights. This has allowed them to enhance market surveillance, enforcement, and other core regulatory functions.

This begs the question, how are firms leveraging the tools assembled for regulatory purposes? Are these products treated as simply cost or are firms creative about leveraging the data for other uses? In the spirit of "waste not, want not," we encourage firms to take a second look at these compliance products with an eye toward delivering value. If this information can make regulators better informed, what should it be doing for your business? In a period of tighter monetary policy, leading firms will look for projects that serve multiple business goals and exploit mandatory spend to deliver outsized value.

### Prepare for changes to liquidity risk management and daily computation of reserve requirements

In late summer 2023, the SEC and FINRA released complementary proposals aimed at improving firms' liquidity risk management. The FINRA concept release would establish liquidity risk management requirements for certain FINRA members. The proposal requires member firms to maintain sufficient liquidity on a current basis and identifies eight conditions under which FINRA would consider a member to not have sufficient liquidity and could restrict or suspend their business. Figure 6 summarizes the proposed scenarios under which firms would be presumed to have insufficient liquidity.

**Figure 6. Requirement to maintain sufficient liquidity on a current basis**

Members are required to have and **maintain sufficient liquidity on a current basis.** The Rule specifies the following **conditions (1) through (8)** that, if they occur, would **result in the presumption that a Member does not have sufficient liquidity** on a current basis. For such Members who satisfy either of these conditions, FINRA may restrict or suspend the Member's business, unless the Member rebuts the presumption. While **EPR firms** are required to maintain sufficient liquidity on a current basis, the requirement to satisfy trigger conditions don't apply to them.

| Conditions that will trigger presumption of insufficient liquidity on a current basis | | | |
|---|---|---|---|
| 1 | 2 | 3 | 4 |
| Member **borrows funds from a nonbank affiliate**, unless the member can demonstrate that the non-bank affiliate has sufficient and stable liquidity to maintain the loan for the time required to meet the member's funding obligations. | Member **borrows an amount in excess of 70% of its customer debit balances** and such amount is secured by assets that are the property of its customers. | Member **performs a reserve computation** on ad hoc basis **more than once** during a rolling 90-calendar-day period for making a withdrawal from its Special Reserve Bank Account, **or the member requests extraordinary regulatory relief** to make a withdrawal without reserve computation. | Member's **bank lines of credit**, including bank loan facilities other than intraday credit facilities at a settlement bank, **are reduced by 50% or more** of the total of such available bank lines of credit during a rolling 90-calendar-day period. |
| 5 | 6 | 7 | 8 |
| Member's **total funding** derived from securities financing arrangements is **reduced by 50% or more** during a rolling 90-calendar-day period. | Member's **intraday credit facility at a settlement bank is reduced by 50% or more** of its aggregate settlement bank credit facilities, during a rolling 90-calendar-day period. | Member is **notified** that it has **lost or will lose access to the services** of one or more of its settlement banks and the member has **not replaced the settlement bank** 90 days prior to the termination of such access. | Member is subject to **revocation of a CCP membership or any material restrictions by a Central Clearing Counterparty (CCP)** or settlement bank. |

Source: FINRA, "Regulatory Notice 23-11: FINRA Seeks Comment on Concept Proposal for a Liquidity Risk Management Rule" June 12, 2023.

The proposal would also require affected firms to have reasonable liquidity risk management programs that include liquidity stress tests and contingency funding plans. Firms that are likely to be impacted by a final rule should assess their current liquidity risk management capabilities and consider enhancements to their program.

### Remember existing regulatory requirements

In a period of aggressive rulemaking, it is easy for firms to lose sight of their existing obligations, and the challenge is re-doubled when regulators take action. In 2023, we saw the enforcement arms of the market regulators seemingly reborn. Enforcement actions increased, fine amounts increased, headline-stealing actions seemed to become the norm. Many firms were not prepared. As the industry attempts to push back, firms should also expect that some of this is the new normal. For years, regulators have taken an eye toward bringing fines up to levels that they see as an effective deterrent for noncompliant behavior. These analyses have led regulators to set new thresholds for fines, and while the topics of interest or number of actions may vary from year to year and administration to administration, the pecuniary penalties for falling short of regulatory expectations may not.

Thus, it becomes essential for firms to invest in what regulators refer to as “the baseline”—that is, all existing regulatory burdens. We call on firms to evaluate their own baseline. Where are the gaps? Where are things comfortable? Where has technology introduced new regulatory risk that may not be accounted for in existing compliance programs? The more firms go “back to basics,” the more they can protect themselves from steep penalties that drain their pool of resources available to adapt to ever-changing regulatory expectations.

From an enforcement perspective, regulators have been evaluating fine amounts and their effect as an economic deterrent. In the past few years, we have seen regulators begin to increase their fines in accordance with this thinking. Penalties for some complex compliance obligations have ballooned.[14] Although enforcement activity ebbs and flows, firms should understand that regulators see recently elevated fine levels as “rightsizing” what they perceived to be insufficient consequences for noncompliance. It appears market regulators’ goals with recent elevated fine amounts is partly to create an effective deterrent in hopes of avoiding widespread industry compliance failures in the future. Thus, firms should not consider fines of recent years to be temporary, but rather an indication of future amounts, even if overall fine levels fluctuate with the general approach to enforcement.

In addition to continued heavy enforcement, next year we anticipate a retail-focused enforcement agenda. Regulators have repeatedly voiced their concern for the end retail investor.[15] Indeed, many outstanding rule proposals seek to protect retail in the capital markets.[16] Similarly, we expect the 2024 enforcement agenda to keep an eye toward the end investor. Best execution, Reg BI, and other conflicts-of-interest rules and practices are likely to be at the forefront of regulators’ thinking in exams and enforcement referrals. As already discussed, rulemaking can be an indication of where enforcement is headed. Thus, we anticipate scrutiny of existing compliance with many of the topics we have already covered, including cybersecurity, order routing, trade reporting, and recordkeeping. Staying a step ahead of the regulators by studying their current thinking as laid out in the numerous proposals of recent years can help firms avoid more steep penalties or expensive litigation.

AI

# Unlocking value

We hope that the preceding pages present a formula that firms can employ to help them excel in 2024. The ability to stop reacting, pause, and make investments that improve your business can also help improve the efficacy of "must-haves" like compliance over the long run. We believe that AI will be critical to unlocking value in the face of an uncertain economic outlook, compounding regulatory obligations and compressed budgets. Re-doubling efforts to improve baseline activities like cybersecurity and data management should pay dividends with respect to both regulatory oversight and profitability. Firms are likely to encounter operational volatility in the coming year, and the response will require a steady hand. Remaining agile will be critical to meet both anticipated and unexpected compliance deadlines. While the journey will look different for each individual firm, we believe these are some guiding principles that the industry can leverage to navigate an uncertain year ahead.

Each of these rules is impactful on its own. Together, they could reshape the US capital markets.

# Endnotes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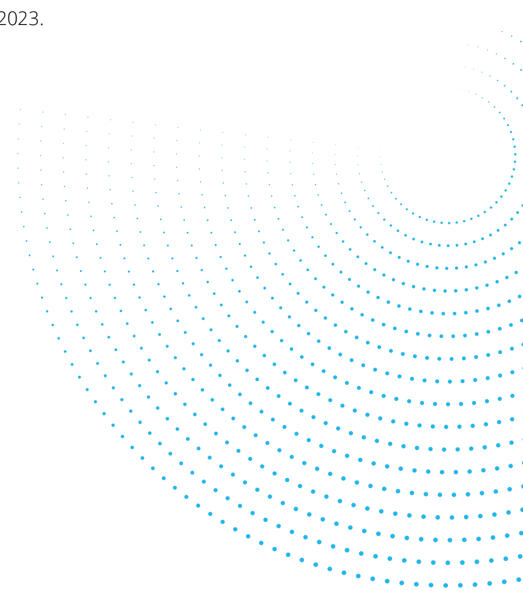

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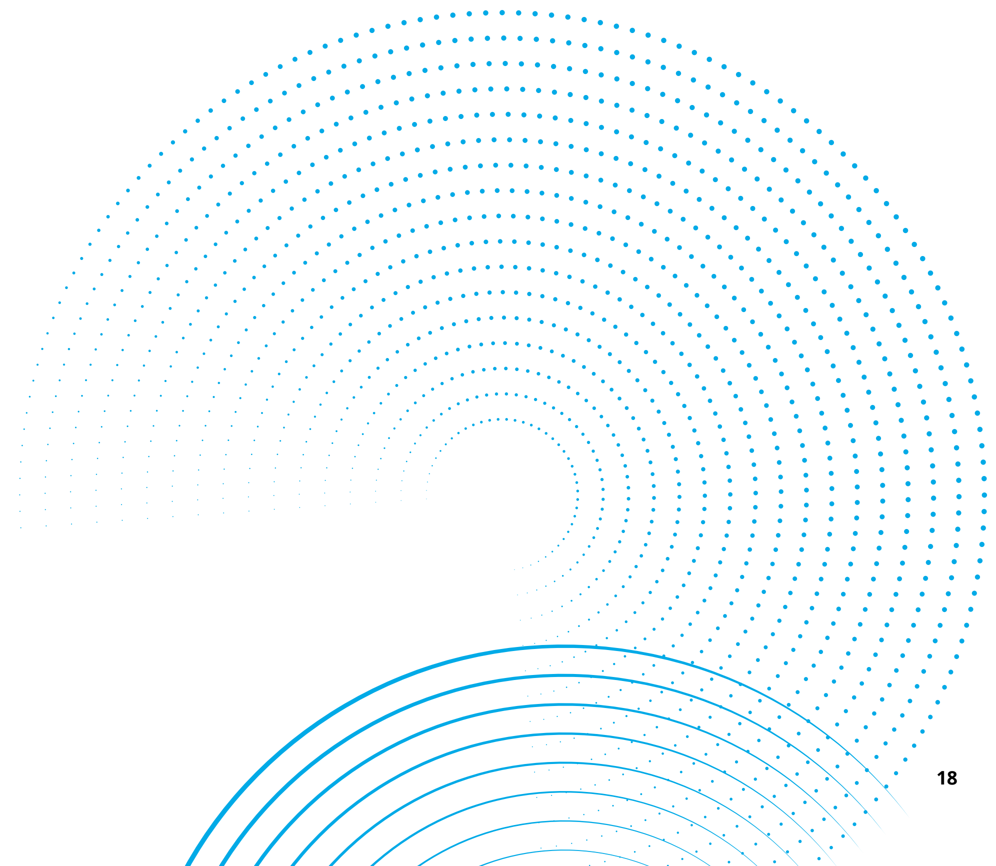

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