

Proposed Rule Change by Financial Industry Regulatory Authority  
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial <input checked="" type="checkbox"/>	Amendment <input type="checkbox"/>	Withdrawal <input type="checkbox"/>	Section 19(b)(2) <input type="checkbox"/>	Section 19(b)(3)(A) <input checked="" type="checkbox"/>	Section 19(b)(3)(B) <input type="checkbox"/>
Pilot <input type="checkbox"/>			Rule		
Extension of Time Period for Commission Action <input type="checkbox"/>		Date Expires <input type="text"/>	<input checked="" type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
			<input type="checkbox"/> 19b-4(f)(2)	<input type="checkbox"/> 19b-4(f)(5)	
			<input type="checkbox"/> 19b-4(f)(3)	<input type="checkbox"/> 19b-4(f)(6)	

Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input checked="" type="checkbox"/>
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**Description**  
Provide a brief description of the proposed rule change (limit 250 characters).

**Contact Information**  
Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name	<input type="text" value="Afshin"/>	Last Name	<input type="text" value="Atabaki"/>
Title	<input type="text" value="Assistant General Counsel"/>		
E-mail	<input type="text" value="afshin.atabaki@finra.org"/>		
Telephone	<input type="text" value="(202) 728-8902"/>	Fax	<input type="text" value="(202) 728-8264"/>

**Signature**  
Pursuant to the requirements of the Securities Exchange Act of 1934,  
  
has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date

By  (Name)  (Title)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

**Form 19b-4 Information**

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change**

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

**1. Text of Proposed Rule Change**

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) revisions to the study outline and selection specifications for the Limited Representative—Government Securities (Series 72) examination program.<sup>2</sup> The proposed revisions update the material to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a Limited Representative—Government Securities. FINRA is not proposing any textual changes to the By-Laws, Schedules to the By-Laws, or Rules of FINRA.

The revised study outline is attached. The Series 72 selection specifications have been submitted to the Commission under separate cover with a request for confidential treatment pursuant to Rule 24b-2 under the Act.<sup>3</sup>

(b) Not applicable.

(c) Not applicable.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> FINRA also is proposing corresponding revisions to the Series 72 question bank, but based upon instruction from the Commission staff, FINRA is submitting SR-FINRA-2007-032 for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(1) thereunder, and is not filing the question bank for Commission review. See Letter to Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, from Belinda Blaine, Associate Director, Division of Market Regulation, SEC, dated July 24, 2000. The question bank is available for Commission review.

<sup>3</sup> 17 CFR 240.24b-2.

**2. Procedures of the Self-Regulatory Organization**

At its meeting on January 24, 2001, the Board of Directors of NASD Regulation, Inc. authorized the staff to propose modifications to examination programs, including study outlines, examination specifications, and question banks, and to file the proposed modifications with the Commission, without obtaining further or specific authorization from the Board of Directors of NASD Regulation, Inc. The Board of Governors of FINRA (then known as NASD) had an opportunity to review that action at its meeting on January 25, 2001. No other action by FINRA is necessary for the filing of the proposed rule change.

As further discussed below, FINRA is filing the proposed rule change for immediate effectiveness. FINRA proposes to implement the revised Series 72 examination program on February 12, 2008. FINRA will announce the proposed rule change and the implementation date in a Regulatory Notice (“Notice”) to be published on the same date as this filing.

**3. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

(a) Purpose

Section 15A(g)(3) of the Act<sup>4</sup> requires FINRA to prescribe standards of training, experience, and competence for persons associated with FINRA members. In accordance with that provision, FINRA has developed examinations, and administers examinations developed by other self-regulatory organizations, that are designed to establish that persons associated with FINRA members have attained specified levels of competence

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<sup>4</sup> 15 U.S.C. 78o-3(g)(3).

and knowledge. FINRA periodically reviews the content of the examinations to determine whether revisions are necessary or appropriate in view of changes pertaining to the subject matter covered by the examinations.

Pursuant to NASD Rule 1032(g), each associated person of a member who is included within the definition of representative in NASD Rule 1031(b) may register with FINRA as a Limited Representative—Government Securities if: (1) the individual’s activities in the investment banking and securities business of the member are limited solely to the solicitation, purchase and sale of “government securities,” as that term is defined in Sections 3(a)(42)(A) through (C) of the Act, for the account of a broker-dealer or public customer; and (2) the individual passes the Series 72 qualification examination.

A committee of industry representatives, together with FINRA staff, recently undertook a review of the Series 72 examination program. As a result of this review, FINRA is proposing to make revisions to the study outline to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a Limited Representative—Government Securities.

Among other revisions, FINRA is proposing to add sections on NASD IM-2210-6 (Requirements for the Use of Investment Analysis Tools), NASD Rule 2370 (Borrowing From or Lending to Customers) and NASD Rule 2790 (Restrictions on the Purchase and Sale of Initial Equity Public Offerings).

FINRA is proposing to change the title of Section 3 of the study outline from “Other Related Securities and Financial Instruments” to “Related Securities and Financial Instruments” and the title of Section 5 from “Legal Considerations” to “Securities

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Industry Regulations and Legal Considerations.” Further, as a result of the revisions discussed above, the number of questions on each section of the study outline were modified as follows: Government Securities, decreased from 25 to 22 questions; Mortgaged-Backed Securities, no changes to the number of questions (remains at 25 questions); Related Securities and Financial Instruments, no changes to the number of questions (remains at 9 questions); Economic Activity, Government Policy and the Behavior of Interest Rates, decreased from 16 to 13 questions; Securities Industry Regulations and Legal Considerations, increased from 10 to 15 questions; and Customer Considerations, increased from 15 to 16 questions.

FINRA is proposing similar changes to the Series 72 selection specifications and question bank. The number of questions on the Series 72 examination will remain at 100, and candidates will continue to have 3 hours to complete the exam. Also, each question will continue to count one point, and each candidate must correctly answer 70 percent of the questions to receive a passing grade.

(b) Statutory Basis

FINRA believes that the proposed revisions to the Series 72 examination program are consistent with the provisions of Sections 15A(b)(6)<sup>5</sup> and 15A(g)(3) of the Act,<sup>6</sup> which authorize FINRA to prescribe standards of training, experience, and competence for persons associated with FINRA members.

**4. Self-Regulatory Organization’s Statement on Burden on Competition**

FINRA does not believe that the proposed rule change will result in any burden

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<sup>5</sup> 15 U.S.C. 78o-3(b)(6).

on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

5. **Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

Written comments were neither solicited nor received.

6. **Extension of Time Period for Commission Action**

Not applicable.

7. **Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)**

The proposed rule change is effective upon filing pursuant to Section 19(b)(3)(A)(i) of the Act<sup>7</sup> and Rule 19b-4(f)(1) thereunder,<sup>8</sup> in that the proposed rule change constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of FINRA. FINRA proposes to implement the revised Series 72 examination program on February 12, 2008. FINRA will announce the implementation date in a Notice to be published on the same date as this filing.

8. **Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission**

Not applicable.

9. **Exhibits**

Exhibit 1. Completed notice of proposed rule change for publication in the

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<sup>6</sup> 15 U.S.C. 78o-3(g)(3).

<sup>7</sup> 15 U.S.C. 78s(b)(3)(A)(i).

<sup>8</sup> 17 CFR 240.19b-4(f)(1).

Federal Register.

Exhibit 3a. Revised Study Outline for the Series 72 Examination.

Exhibit 3b. Revised Selection Specifications for the Series 72 Examination.

FINRA has requested confidential treatment for the Series 72 revised selection specifications, and thus the specifications are omitted from this filing. The Series 72 revised selection specifications have been filed separately with the Commission pursuant to Rule 24b-2 under the Act.<sup>9</sup>

Exhibit 3c. Letter to Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, Inc. from Belinda Blaine, Associate Director, Division of Market Regulation, SEC, dated July 24, 2000.

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<sup>9</sup> 17 CFR 240.24b-2.

**EXHIBIT 1**

**SECURITIES AND EXCHANGE COMMISSION**

(Release No. 34- ; File No. SR-FINRA-2007-032)

Self-Regulatory Organizations: Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Revisions to the Series 72 Examination Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on , Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as constituting a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of the self-regulatory organization pursuant to Section 19(b)(3)(A)(i) of the Act<sup>3</sup> and Rule 19b-4(f)(1) thereunder,<sup>4</sup> which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

**I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change**

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A)(i).

<sup>4</sup> 17 CFR 240.19b-4(f)(1).

FINRA is filing revisions to the study outline and selection specifications for the Limited Representative—Government Securities (Series 72) examination program.<sup>5</sup> The proposed revisions update the material to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a Limited Representative—Government Securities. FINRA is not proposing any textual changes to the By-Laws, Schedules to the By-Laws, or Rules of FINRA.

The revised study outline is attached. The Series 72 selection specifications have been submitted to the Commission under separate cover with a request for confidential treatment pursuant to Rule 24b-2 under the Act.<sup>6</sup>

**II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

**A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

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<sup>5</sup> FINRA also is proposing corresponding revisions to the Series 72 question bank, but based upon instruction from the Commission staff, FINRA is submitting SR-FINRA-2007-032 for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(1) thereunder, and is not filing the question bank for Commission review. See Letter to Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, from Belinda Blaine, Associate Director, Division of Market Regulation, SEC, dated July 24, 2000. The question bank is available for Commission review.

<sup>6</sup> 17 CFR 240.24b-2.

1. Purpose

Section 15A(g)(3) of the Act<sup>7</sup> requires FINRA to prescribe standards of training, experience, and competence for persons associated with FINRA members. In accordance with that provision, FINRA has developed examinations, and administers examinations developed by other self-regulatory organizations, that are designed to establish that persons associated with FINRA members have attained specified levels of competence and knowledge. FINRA periodically reviews the content of the examinations to determine whether revisions are necessary or appropriate in view of changes pertaining to the subject matter covered by the examinations.

Pursuant to NASD Rule 1032(g), each associated person of a member who is included within the definition of representative in NASD Rule 1031(b) may register with FINRA as a Limited Representative—Government Securities if: (1) the individual's activities in the investment banking and securities business of the member are limited solely to the solicitation, purchase and sale of "government securities," as that term is defined in Sections 3(a)(42)(A) through (C) of the Act, for the account of a broker-dealer or public customer; and (2) the individual passes the Series 72 qualification examination.

A committee of industry representatives, together with FINRA staff, recently undertook a review of the Series 72 examination program. As a result of this review, FINRA is proposing to make revisions to the study outline to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a Limited Representative—Government Securities.

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<sup>7</sup> 15 U.S.C. 78o-3(g)(3).

Among other revisions, FINRA is proposing to add sections on NASD IM-2210-6 (Requirements for the Use of Investment Analysis Tools), NASD Rule 2370 (Borrowing From or Lending to Customers) and NASD Rule 2790 (Restrictions on the Purchase and Sale of Initial Equity Public Offerings).

FINRA is proposing to change the title of Section 3 of the study outline from “Other Related Securities and Financial Instruments” to “Related Securities and Financial Instruments” and the title of Section 5 from “Legal Considerations” to “Securities Industry Regulations and Legal Considerations.” Further, as a result of the revisions discussed above, the number of questions on each section of the study outline were modified as follows: Government Securities, decreased from 25 to 22 questions; Mortgaged-Backed Securities, no changes to the number of questions (remains at 25 questions); Related Securities and Financial Instruments, no changes to the number of questions (remains at 9 questions); Economic Activity, Government Policy and the Behavior of Interest Rates, decreased from 16 to 13 questions; Securities Industry Regulations and Legal Considerations, increased from 10 to 15 questions; and Customer Considerations, increased from 15 to 16 questions.

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## 2. Statutory Basis

FINRA believes that the proposed revisions to the Series 72 examination program

are consistent with the provisions of Sections 15A(b)(6)<sup>8</sup> and 15A(g)(3) of the Act,<sup>9</sup> which authorize FINRA to prescribe standards of training, experience, and competence for persons associated with FINRA members.

**B. Self-Regulatory Organization’s Statement on Burden on Competition**

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

**C. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

Written comments were neither solicited nor received.

**III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

The proposed rule change has become effective pursuant to Section 19(b)(3)(A)(i) of the Act<sup>10</sup> and Rule 19b-4(f)(1) thereunder,<sup>11</sup> in that the proposed rule change constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of the self-regulatory organization. FINRA proposes to implement the revised Series 72 examination program on February 12, 2008. FINRA will announce the implementation date in a Regulatory Notice to be published on the same date as this filing.

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<sup>8</sup> 15 U.S.C. 78o-3(b)(6).

<sup>9</sup> 15 U.S.C. 78o-3(g)(3).

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A)(i).

<sup>11</sup> 17 CFR 240.19b-4(f)(1).

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2007-032 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2007-032. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed

with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing also will be available for inspection and copying at the principal office of FINRA.

All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2007-032 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

Nancy M. Morris

Secretary

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<sup>12</sup> 17 CFR 200.30-3(a)(12).



**Government Securities  
Limited Representative  
Qualification Examination  
(Test Series 72)**

**Study Outline**

## Introduction

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The Government Securities Limited Representative Qualification Examination (Series 72) is used to qualify persons seeking registration with FINRA under FINRA By-Laws Article III, Section 2 and NASD Rule 1032(g). Registered representatives in this limited category of registration are permitted to transact a member's business in government securities, agency securities, and agency-backed mortgage securities. This category, by itself, does not allow a registered representative to transact a member's business in options on government securities. Candidates seeking to conduct transactions in this latter product must also register as registered options representatives.

This study outline has been prepared to assist member firms in preparing candidates to sit for the Series 72 Examination. It may be used to structure or prepare training material and develop lecture notes and seminar programs, as well as a training aid for the candidates themselves. The outline and the test are divided into the six sections, which are listed below along with the number of questions devoted to each section.

Section	Description	Number of Questions
1	Government Securities	22
2	Mortgaged-Backed Securities	25
3	Related Securities and Financial Instruments	9
4	Economic Activity, Government Policy and the Behavior of Interest Rates	13
5	Securities Industry Regulations and Legal Considerations	15
6	Customer Considerations	16
<b>Total</b>		<b>100</b>

The Series 72 Examination is comprised of 100 questions, and 180 minutes of testing time is allowed to complete the examination. A candidate must correctly answer 70 percent of the questions to receive a passing grade. The test is administered as a closed-book exam. Scratch paper and basic electronic calculators will be provided by the proctor. At the completion of the test, candidates will receive an informational breakdown of their performance in each of the above sections, along with their overall score and grade. Topics in this examination may be tested by requiring a candidate to apply the concepts to real-life situations. In some instances, this may require basic level computations.

Examination questions will be updated to reflect the most current interpretations of the rules and regulations. Questions on new rules will be added to the pool of questions for this examination within a reasonable time period after their effective dates. Questions on rescinded rules will be promptly deleted from the pool of questions.

There is a reference list at the end of this study outline that may be used as a source material starting point for course developers in preparing training programs. In addition, nonmember commercial training vendors may offer packaged study courses specifically designed for this registration category. These vendors are often listed in local yellow page directories and advertise in securities industry periodicals.

Copies of this outline may be obtained from the FINRA Web Site at [www.finra.org](http://www.finra.org).

The last chapter of this outline contains sample test questions. These samples do not mirror the difficulty level of actual test questions or the subject-matter distribution of the test itself. Their use is merely to familiarize the candidate with the styles of multiple-choice questions used in the Series 72 Examination.

## **1.0 Government Securities**

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### **1.1 Types and characteristics of Government Securities**

#### **1.1.1 Direct Obligations of the U.S. Treasury**

- 1.1.1.1 Treasury securities -- Benchmark that is the source of credit, marketability and liquidity for other financial markets
  - Full faith and credit of the United States
  - Treasury bills
  - Treasury notes
  - Treasury bonds
  - Separate Trading of Registered Interest and Principal of Securities (STRIPS)
  - Treasury inflation-indexed securities (also referred to as TIPS)

- 1.1.1.2 Non-marketable Treasury instruments
  - United States Savings Bonds (Series EE and I)
  - SLGS (State and Local Government Series)

#### **1.1.2 Agency Securities - As a group, second only to Treasury securities for credit quality**

- 1.1.2.1 General characteristics
  - Provide selected sectors of the economy with funding, capital or liquidity
  - May or may not be a direct obligation of the U.S. Government
  - Marketability and liquidity vary from issue to issue
  - Some issuers may be referred to as Government sponsored entities or GSE

- 1.1.2.2 Agencies with securities having explicit backing (full faith and credit) of the U.S. Government
  - Government National Mortgage Association (GNMA or Ginnie Mae)
  - Private Export Funding Corporation (PEFCO)
  - Small Business Administration (SBA)

- 1.1.2.3 Agencies with securities that do not have explicit backing of the U.S. Government
  - Federal Agricultural Mortgage Corporation (Farmer Mac)
  - Federal Farm Credit Banks (FFCB)
  - Federal Home Loan Banks (FHLB)

Federal Home Loan Mortgage Corporation (FHLMC or Freddie Mac)

Federal National Mortgage Association (FNMA or Fannie Mae) Financing Corporation (FICO)

Resolution Funding Corporation (Refcorp)

Tennessee Valley Authority (TVA)

1.1.2.4 Types of issued Agency securities

Debentures

Discount notes

Global issues

Medium-term notes

Structured notes

Reference notes (benchmark securities)

**1.1.3 Stripped Securities**

Definition

Features

Mechanics of creating and trading

Types

Treasury STRIPS (Separate Trading of Registered Interest and Principal of Securities)

Proprietary instruments (*e.g.*, CATS, TIGRS, TRs [Treasury Receipts])

Agency stripped securities (*e.g.*, Refcorp, FICO)

**1.1.4 Maturity and Denominations of Various Government Securities**

**1.1.5 Call Provisions**

Continuous call provisions

Discrete call provisions

One-time-only calls

**1.1.6 Interest Payment Methods**

Frequency of payment

Fixed

Discount

At maturity

Variable

Floater: indexed to

Treasury bills

CMT (Constant Maturity Treasury)

LIBOR (London Interbank Offered Rate)

Inverse floater

Indexed notes and bonds

Step ups

- Interest rate floor and/or caps
- 1.1.7 Methods of Quotation**
  - Current yield
  - Day count method
  - Discount basis/Bond equivalent yield
  - Dollar price
  - Money market equivalent yield
  - Option adjusted spread (OAS)
  - Quotation services
  - Quotations vs. firm market
  - Value of a basis point (.0001 or .01%)
  - Yield to call
  - Yield to maturity
  - Yield/spread relationship

- 1.1.8 Methods of Settlement and Delivery**
  - Settlement
    - Regular
    - Cash
    - When issued
    - Delayed
      - Corporate settlement
      - Skip Day
  - Accrued interest
  - Financing positions under delayed settlement
  - Forms of delivery
    - Book entry only
    - Fully registered

## **1.2 The Market for Government Securities**

- 1.2.1 Participants in the Market and the Role of Each**
  - Federal Reserve
  - Primary dealers
  - Government securities dealers
  - Government securities brokers and inter-dealer brokers
  - Investors, retail and institutional

- 1.2.2 Functions of a Trader**
  - Financing the trading position
    - Bank financing
    - Repurchase Agreements (REPOs)
    - Securities borrowing and lending
  - Give quotes
  - Hedging/arbitrage
  - Make markets

Position trading  
Securing collateral for delivery/reverse repos  
Supply information to salespersons

**1.2.3 New Issues**

- 1.2.3.1 U.S. Treasury auction process
  - Treasury announcement
  - Types and mechanics of bids
    - Competitive
    - Non-competitive
    - Treasury direct
  - Basis of awards/prorating of awards
  - Limitations on auction awards
  - Types of auctions
    - Standard
    - Dutch
  - Reopening of existing issues
- 1.2.3.2 Primary market for Agency securities
  - Selling group
    - Discount note program
    - Debenture program
  - Negotiated
    - Reverse inquiry
    - Dealer reallowance
    - Concession
  - Competitive bidding
- 1.2.4 The Secondary Market**
- 1.2.4.1 Kinds of transactions
  - Principal
  - Agent
- 1.2.4.2 When-issued trading
  - Pre-auction trading of Treasury securities
  - Post-auction trading of Treasury securities
  - Forward/reverse roll trading
- 1.2.4.3 Methods of comparing bond prices
  - Bids vs. offers
    - Round lot/odd lot
  - Duration
  - Expression of dollar price/yield
  - Yield to call

Yield to maturity

## **2.0**

### **Mortgage-Backed Securities**

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#### **2.1 Development/Evolution of Mortgage-Backed Securities**

##### **2.1.1 The Underlying Mortgages**

- 2.1.1.1 Definition of mortgage loan
  - Collateralized by real estate
  - Monthly amortization
  
- 2.1.1.2 Traditional mortgage lenders — the institutions that make the loans
  - Commercial banks
  - Mortgage bankers
  - Savings and loan associations
  
- 2.1.1.3 Types of mortgage loans
  - Commercial
  - Project loans
  - Residential
    - Conforming vs. non-conforming
    - Conventional
    - FHA/VA
    - Manufactured housing (mobile homes)
    - Multi-family residential (5 or more units)
    - Single-family residential (1 to 4 units)
    - Whole loan
  
- 2.1.1.4 Characteristics of mortgage loans
  - Adjustable rate (ARM)
    - Caps and floors
      - Periodic
      - Lifetime
    - Convertible vs. nonconvertible
    - Indexed to
      - COFI (Cost of Funds Index)
      - CMT (Constant Maturity Treasury)
      - LIBOR (London Interbank Offered Rate)
    - Initial rates, “teaser rates”
    - Reset parameters
      - Payment reset
      - Interest rate reset
    - Assumable vs. non-assumable
  - Fixed rate
  - Loan size

Maturities

30-year (fully amortized)

20-year (fully amortized)

15-year (fully amortized)

7-year (balloons)

5-year (balloons)

Others (*e.g.*, 10-year, 20-year, interest only and graduated payments)

Underwriting standards (loan-to-value [LTV] ratio and underwriting ratios)

Mortgage amortization

**2.1.2 Securitization of the Mortgages**

2.1.2.1 Purposes

Facilitate issuance of mortgages

Meet legislative intent to provide housing

Provide capital for the mortgage industry and liquidity to the housing market

2.1.2.2 Creating pass-through securities

Pooling process

Originator

Seller

Servicer

Paying agent

**2.2 Mortgage-Backed Securities — Types, Structure and Features**

**2.2.1 Pass-Through Securities or Participation Certificates (PC) in a Securitized Pool of Mortgages**

2.2.1.1 Ginnie Mae Full Modified Pass-Through Mortgage-Backed Certificates (GNMA I and GNMA II)— composed of VA-guaranteed or FHA insured mortgages

30-year

15-year (midgets)

Adjustable rate mortgages (ARMs)

2.2.1.2 Fannie Mae (FNMA) Mortgage Pass-Through Certificates —composed of qualifying FNMA conventional residential mortgages or some FHA insured mortgages

30-year

15-year (dwarfs)

7-year (balloons)

Adjustable rate mortgages (ARMs)

- 2.2.1.3 Freddie Mac (FHLMC) Participation Certificates — composed of qualifying FHLMC conventional residential mortgages (Gold PCs and non-Gold PCs)
  - 30-year
  - 15-year (gnomes)
  - 7-year (balloons)
  - 5-year (balloons)
  - Adjustable rate mortgages (ARMs)

- 2.2.1.4 Private label
  - Underlying mortgages not guaranteed by FNMA, FHLMC or GNMA
  - Structures (senior/subordinate, etc.)
  - Credit rating

**2.2.2 Structured Mortgage Products — Collateralized Mortgage Obligations (CMOs) and Real Estate Mortgage Investment Conduits (REMICs)**

- Purpose for creation of CMOs and REMICs
- Private label vs. agency
- Investor preference for specified average life
- Yield curve arbitrage
- Trustees handle all legal documentation and processes for the structure
- Ginnie Mae (GNMA) REMIC Pass-Through Securities
- Fannie Mae (FNMA) REMIC Pass-Through Certificates
- Freddie Mac (FHLMC) Multi-Class Mortgage Participation Certificates

**2.2.3 Stripped Mortgage-Backed Securities**

- Interest only (IO)
- Principal only (PO)

**2.3 Characteristics of Mortgage-Backed Securities**

**2.3.1 Characteristics Common to All Mortgage-Backed Securities**

- Backed by real property
- Credit ratings
- Current face/amortized value
- Factor
- Fixed or floating rate securities
- Maturity profile
  - Average life
  - Stated or final maturity
- Original face value
- Payment delay and payment date
- Pool or series number
- Prepayment of principal

Trade in the over-the-counter market (OTC)

## **2.3.2 Unique Characteristics of Specific Mortgage-Backed Securities**

### **2.3.2.1**

CMOs and REMICs

Guarantees (credit quality)

Payment dates

Minimum investments

Classes (“tranches”), such as:

Callable

Companion/support

Floating rate

Interest only (IO)

Inverse floaters

Planned amortization class (PAC)

Principal only (PO)

Residuals

Sequential (plain vanilla)

Targeted amortization class (TAC)

Z-tranches (accretion bonds or accrual bonds)

### **2.3.2.2**

Pass-through securities (the “collateral market”)

Guarantees

Minimum investments

Payment dates/stated delay

Principal repaid monthly

### **2.3.2.3**

Various coupon/maturity terms

Weighted average maturity (WAM)

Weighted average coupon (WAC)

Weighted average loan age (WALA)

## **2.3.3 Impact of Interest Rate Changes on Prepayments**

Effect on average life

Accelerated prepayment of principal

Decelerated prepayment of principal

Effect on value or price

## **2.4 The Mortgage-Backed Securities Market**

### **2.4.1 Participants in the Market**

Dealers — primary, secondary

Federal agencies

Investors — individual, institutional

### **2.4.2 The Distribution Process and Secondary Trading**

- 2.4.2.1 Initial distribution
  - Pass-through securities — the securitization process is the primary market
  - Structured mortgage products (CMOs and REMICs)
  - Offering circular
- 2.4.2.2 The secondary market
  - 2.4.2.2.1 Kinds of transactions
    - Principal
    - Agent
  - 2.4.2.2.2 Functions of a trader
    - Finance the trading position
      - Dollar rolls
      - Bank financing
      - Repos
    - Give quotes
    - Hedging/arbitrage
    - Make markets
    - Position trading
    - Supply information to salespersons
  - 2.4.2.2.3 Form of trading
    - To Be Announced (TBA) trading
      - Direct standard agreement between buyer and seller
      - Contract specifies amount, bond price and delivery date
      - Credit risk/counter party
    - Trading of specified pools
  - 2.4.2.2.4 Mechanics of pricing
    - Bids vs. offers
    - Components of dollar price
    - Credit rating
    - Determination of yield
    - Expression of dollar price /yield
    - Identification of pool number
    - Knowledge of issue size
    - Prepayment speed assumption
    - Quotations vs. firm market
    - Round lot/odd lot
    - Spread relationships
- 2.4.3 **Methods of Comparing Mortgage-Backed Securities**
  - Application of volatility measures
    - FFIEC — Federal Financial Institutions Exam Council

- FLUX — Flow Uncertainty Index
- Cash flow spread vs. forward curve
- Cash flow spread vs. spot curve
- Convexity/negative convexity
- Duration
  - Modified
  - Effective
- Geographic distribution
- Indices, resets, caps and floors for floating-rate tranches
- Measuring prepayments
  - Constant Prepayment Rate (CPR)
  - Public Securities Association (PSA) prepayment model
  - Single Monthly Mortality (SMM)
- Option adjusted spread (OAS)
- Priority of cash flows
- Single prepayment rate vs. vector of prepayment rates
- Spread to Treasury curve based on comparable average life
- Timing of cash flows
  - Lock-out period
  - Window period
- Total return
- Use of WAM, WAC, WALA
- Volatility
- Yield to maturity
- Yield on discounted cash flow
- Yield to average life

## **2.4.4 Methods of Settlement and Delivery**

- 2.4.4.1 Pass-through securities
  - PSA settlement calendar
  - Delivery of specified pool
  - To be announced (TBA) good delivery
  - 48 hour pool notice
    - Allocation procedures
    - Pool substitution cut-off time
  - Forms of delivery
    - Book entry at the Fed
    - Depository Trust Clearing Corp. (DTC)
    - Physical
- 2.4.4.2 REMICs and CMOs
  - Settlement
    - Regular way (T+3)
    - As otherwise specified
    - Blackout period/due bills

Delivery  
Book-entry  
DTC

## **3.0 Related Securities and Financial Instruments**

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### **3.1 Money Market Instruments**

#### **3.1.1 Commercial Paper**

- Issuer placed vs. dealer-placed paper
- Maturities (1 day to 270 days)
- Secondary market trading
- Ratings
  - Moody's Investor Services
  - Standard & Poors Corporation
  - Fitch
- Credit supported commercial paper
  - Letter of credit
  - Surety bond
- Asset-backed commercial paper
- Interest bearing/discount

#### **3.1.2 Bankers Acceptances**

- Creation of bankers acceptances
- Credit risk
- Issued by domestic or foreign bank
- Issued at a discount
- Maturities (180 days or less)
- Secondary market trading

#### **3.1.3 Certificates of Deposit (CDs)**

- Brokered CDs
  - FDIC Insurance
- Methods of calculating interest
- Negotiable/ Jumbo CDs
  - Domestic CDs
  - Eurodollar CDs
  - Yankee CDs
- Secondary market trading
- Settlement
- Various maturities

#### **3.1.4 Repurchase Agreements (Repos) and Reverse Repurchase Agreements**

- Types and Maturities
  - Overnight Repo
  - Open Repo/TFN (til further notice)
  - Term Repo

Collateral

- Types of collateral restrictions
- Maturity of collateral restrictions
- Haircut
- Pricing collateral
  - Short squeeze/“special”
- Rights of substitution
- Tri-party Repo agreement
- Matched/mismatched book
- Mark to market
- PSA agreement
- Settlement

**3.2 Other Instruments Affecting the Government Securities Market**

**3.2.1 Federal Funds**

- Definition
- Fed funds rate
- Market/participants
- Purpose

**3.2.2 Asset-Backed Securities (ABS)**

3.2.2.1 Major types

- Auto loans
- Credit cards
- Home equity loans
- Collateralized debt obligations (CDOs)
- Collateralized loan obligations (CLOs)

3.2.2.2 Impact on the government securities market

**3.2.3 Interest Rate Futures**

3.2.3.1 Types traded on exchanges

- Eurodollar time deposit futures contracts
  - Credit risk
- Euro strips contracts
- Treasury Eurodollar (TED) spread
- Fed funds futures
- Treasury bill futures contracts
- Two-year Treasury note futures contract
- Five-year Treasury note futures contract
- Ten-year Treasury note futures contracts
- Treasury bond futures contracts

- 3.2.3.2 Characteristics
  - Actively traded
  - Agreement between buyer/seller and an established futures exchange or its clearing house
  - Contract specifies that buyer/seller take or make delivery of bonds or cash, at a specified price, at a designated time
  - Mark to market
  - Safety net characteristics, *i.e.*, exchange protection factors and procedures
  - Various expiration dates
- 3.2.3.3 Pricing
  - Basis trading
  - Conversion factor
  - Terms of contract quotation
- 3.2.3.4 Impact on the government securities market
  - Open interest
  - Liquidity
- 3.2.4 Options on Government Securities**
- 3.2.4.1 Types
  - Options on cash instruments
  - Options on futures
- 3.2.4.2 Flexibility of over-the-counter options vs. exchange-traded options
- 3.2.4.3 Definitions and terminology
  - American vs. European style
  - At-the-money (ATM)
  - Call
  - Covered options
  - Expiration date
  - Implied volatility
  - In-the-money (ITM)
  - Intrinsic value
  - Option
  - Out-of-the-money (OTM)
  - Premium
  - Put
  - Strike price
  - Time value

## **4.0 Economic Activity, Government Policy, And The Behavior of Interest Rates**

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### **4.1 Fiscal Policy**

#### **4.1.1 Federal Budgetary Practices and Their Impact on the Money and Capital Markets**

- Federal deficits and surpluses — effects on the economy as a result of changes in fiscal policy
- Taxation and spending — effects of congressional or executive authority to raise/lower federal taxes and/or spending
- Multiplier effect of government taxing and spending
- Lag effects on the economy of government action
- Automatic stabilizers — effects in cushioning economic swings
  - Changes in private savings rates
  - Welfare transfer payments

#### **4.1.2 U.S. Treasury Debt Management Practices**

- Impact of short-term and long-term financing
- Increase/decrease in amounts borrowed
- Impact on the average life of debt
- Regularity of debt issuance

#### **4.1.3 Effects of Fiscal Policy on the Economy**

4.1.3.1 Cyclical expansion

- Effects of tax cuts
- Increased government spending
- Transfer payments

4.1.3.2 Structural contraction

- Effects of tax increases
- Decrease of government spending

### **4.2 Monetary Policy**

#### **4.2.1 Objectives of Federal Reserve Monetary Policy**

- Price stability
- Long-term economic growth in an environment of low inflation (*i.e.*, an inflation rate such that economic plans are not impacted by inflationary expectations)
- Low unemployment rate
- Steady non-inflationary growth
- Humphrey-Hawkins Act

**4.2.2 Major Factors Influencing Federal Reserve Monetary Policy**

- Economic indices
- Inflation signals and pressures
- Rate of capital formation and investment
- Foreign exchange considerations

**4.2.3 Operations of the Federal Reserve**

- Role of the Board of Governors
- Role of the Federal Open Market Committee (FOMC)
- Role of the Open Market Trading Desk

**4.2.4 Operating Tools Used for Implementing Federal Reserve Policy**

- Open market operations
  - Adding and draining reserves (Repos and Reverse Repos)
  - Purchase and sale of securities
- Discount window
- Reserve requirements
  - Federal funds market

**4.3 Behavior of Interest Rates**

**4.3.1 Supply and Demand for Credit Relative to the Business Cycle**

- Definition and characteristics of the business cycle
- Public vs. private borrowing needs

**4.3.2 Definition and Impact of Economic Indicators**

- Business inventories
- Consumer confidence
- Consumer credit
- Consumer Price Index (CPI)
- Gross Domestic Product (GDP)
- Employment Cost Index (ECI)
- Employment data
- Existing home sales
- Housing starts and permits
- Industrial production
- Merchandise trade balance
- National Purchasing Managers Survey (NAPM)
- New home sales
- Producer Price Index (PPI)
- Retail sales
- Weekly jobless claims

**4.3.3 Yield Curve Analysis**

- Expectations of Fed policy moves and investor positioning on the curve

Impact of economic and financial conditions on shape of the yield curve

**4.3.4 Technical Analysis — Definitions**

- Breakouts
- Moving averages
- Overbought
- Oversold
- Resistance levels
- Support levels

**4.4 Effects of International Factors on the U.S. Treasury Market**

**4.4.1 Currency Valuation**

- Appreciation
- Depreciation
- Exchange rate of U.S. dollar vs. other currencies

**4.4.2 Balance of Payments**

- Current account surpluses/deficits
- Impact of foreign monetary and fiscal policy on U.S. rates
- Trade surpluses/deficits

## **5.0**

### **Securities Industry Regulations and Legal Considerations**

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#### **5.1 Applicable Federal Laws and SEC Rules Thereunder**

##### **5.1.1 Securities Act of 1933**

Purpose

Section 3 — Government securities exempted from registration

Section 17 — Fraudulent interstate transactions

##### **5.1.2 Securities Exchange Act of 1934**

###### **5.1.2.1 Section 3 — Certain definitions under the Act**

Section 3(a) (4) — Broker

Section 3(a) (5) — Dealer

Section 3(a)(10) — Security

Section 3(a)(12) — Exempted security

Section 3(a)(41) — Mortgage related security

Section 3(a)(42) — Government securities

Section 3(a)(43) — Government securities broker

Section 3(a)(44) — Government securities dealer

Section 3(a)(45) — Person associated with a government securities broker or dealer

###### **5.1.2.2 Section 9 — Prohibitions against manipulation of security prices**

Section 9(a)(1) — Misleading appearance of active trading

Section 9(a)(2) — Inducing purchase or sale by others

Section 9(a)(3) — Dissemination of information as to rise or fall of security prices

Section 9(a)(4) — Making false or misleading statements

Section 9(a)(5) — Dissemination of information for consideration

Section 9(a)(6) — Pegging, fixing, or stabilizing prices

Section 9(e) — Liability for unlawful acts or transactions

###### **5.1.2.3 Section 10 — Regulation use of manipulative and deceptive devices**

Rule 10b-3 — Employment of manipulative and deceptive devices (by brokers or dealers)

Rule 10b-16 — Disclosure of credit terms in margin transactions

###### **5.1.2.4 Section 15(c)(2) — Fraudulent acts or practices and fictitious quotations**

Rule 15c1-2 — Fraud and misrepresentation

Rule 15c1-3 — Misrepresentation by brokers and dealers as to registration

Rule 15c2-1 — Hypothecation of customers' securities

- 5.1.2.5 Section 15C — Government securities brokers and dealers
  - Antifraud provisions applicable to issuers as well as to government securities brokers and dealers
  - Amendments of 1986 (the Government Securities Act of 1986)
    - Registration of government securities brokers and dealers with the SEC
    - Regulators
      - Treasury Department
      - Securities and Exchange Commission
      - Federal Reserve Bank of New York
      - NASD
  - Amendments of 1993 — Registration/qualification of government securities dealer personnel (only qualified to sell securities issued by the U.S. Government and its agencies; not qualified to sell private label CMOs and REMICs)
- 5.1.2.6 SEC Regulation S-P — Privacy of consumer financial information
  - Treatment of nonpublic personal information about consumers by financial institutions
- 5.1.3 Insider Trading Regulations**
  - 5.1.3.1 Insider Trading and Securities Fraud Enforcement Act of 1988
    - Section 3 — Civil penalties of controlling persons for illegal insider trading by controlled persons
    - Section 4 — Increases in criminal penalties
    - Section 5 — Liability to contemporaneous traders for insider trading
  - 5.1.3.2 Securities Exchange Act of 1934 and SEC Rules Thereunder
    - Rule 10b-5 — Employment of manipulative and deceptive devices
      - Insider trading
      - Material information
      - Non-public information
      - Insiders and tippees
      - The Chinese Wall doctrine
    - Rule 10b5-1 — Trading “on the basis of” material nonpublic information in insider trading
    - Rule 10b5-2 — Duties of trust or confidence in misappropriation insider trading cases
- 5.1.4 Customer Confirmations**
  - SEC Rule 10b-10—Confirmations
  - NASD Rule 2230—Confirmations
- 5.1.5 Books and Records**

- 5.1.5.1 Securities Exchange Act of 1934 and SEC Rules Thereunder
  - Rule 17a-3 — Records to be made by certain exchange members, brokers, and dealers
  - Rule 17a-4—Records to be preserved by certain exchange members, brokers and dealers
  - Rule 17a-8 — Recordkeeping and reporting of currency and foreign transactions
  - 17f-1 — Missing, lost, counterfeit or stolen securities reporting
- 5.1.5.2 NASD Rule 3110 — Books and records
  - Record of written complaints
  - “Complaint” defined
  - Requirements using predispute arbitration agreements with customer accounts
  - Negotiable instruments drawn from a customer’s account
  - Holding of customer mail
- 5.2 Treasury Department Regulations Governing the Issuance, Sale and Settlement of Government Securities (31 CFR)**
  - 5.2.1 Descriptions of Securities (Part 356.5 — all securities with the same CUSIP number are considered the same security)**
  - 5.2.2 Bidding, Certifications and Payment (Subpart B)**
    - Noncompetitive and competitive bidding (Section 356.12)
    - Net long position (Section 356.13)
    - Submitting bids for customers (Section 356.14)
    - Certifications (Section 356.15)
    - Required notification to the Fed (Section 356.24d)
  - 5.2.3 Large Position Reporting Requirement (Section 420)**
- 5.3 NASD Rules**
  - 5.3.1 By-Laws**
    - Article III — Qualifications of members and associated persons
      - Section 4 — Definition of disqualification
    - Article V — Registered representatives and associated persons
      - Section 4 — Retention of jurisdiction
    - Article VII — Powers and authority of the Board of Governors
      - Section 2 — Authority to cancel or suspend for failure to submit required information
    - Article XII — Disciplinary proceedings
    - Article XIII — Powers of Board to impose sanctions
  - 5.3.2 Membership and Registration Rules**

- Rule 1021(b) — Definition of principals
- Rule 1030 — Registration of representatives
  - Definition of representatives
  - Categories of representative registration
    - General securities representative
    - Limited representative — government securities
- Rule 1041 — Registration requirements for assistant representative-order processing
- Rule 1060 — Persons exempt from registration
- Rule 1080 — Confidentiality of examinations
- Rule 1120 — Continuing education requirements

### **5.3.3**

#### **Conduct Rules**

- 5.3.3.1 Rule 2110 — Standards of commercial honor and principles of trade
- 5.3.3.2 Rule 2120 — Use of manipulative, deceptive or other fraudulent devices
- 5.3.3.3 Rule 2210 — Communications with the public
  - Definitions
    - Advertisement
    - Sales literature
    - Public appearance
    - Independently prepared reprint
  - Approval and recordkeeping
  - Standards applicable to all communications with the public
  - Standards applicable to advertisements and sales literature
  - IM2210-1—Guidelines to ensure that communications with the public are not misleading
  - IM2210-4—Limitation on use NASD's name
  - IM-2210-6—Requirements for the Use of Investment Analysis Tools
  - IM2210-8—Communications with the public about collateralized mortgage obligations (CMOs)
- 5.3.3.4 Rule 2211—Institutional sales material and correspondence
  - Correspondence
  - Institutional sales material
  - Institutional investor
- 5.3.3.5 Rule 2212 — Telemarketing
- 5.3.3.6 Rule 2250 — Disclosure of participation or interest in primary or secondary distribution
- 5.3.3.7 Rule 2270 — Disclosure of financial condition to customers
  - Requirement to furnish most recent report of the firm's financial condition
- 5.3.3.8 Rule 2330 — Customers' securities or funds
  - Improper use
  - General provisions
  - Authorization to lend
  - Prohibition against guarantees
  - Sharing in accounts; extent permissible
- 5.3.3.9 Rule 2340 — Customer account statements

- Requirement to send customers monthly and/or quarterly statements on account activity
- 5.3.3.10 Rule 2370—Borrowing from or lending to customers
- 5.3.3.11 Rule 2420—Dealing with non-members
- 5.3.3.12 Rule 2440 — Fair prices and commissions
  - Yield burning
  - IM-2440-2—Additional mark-up policy for transactions in debt securities, except municipal securities
- 5.3.3.13 Rule 2520 — Margin requirements
  - Government securities marginable
- 5.3.3.14 Rule 2750—Transactions with related persons
- 5.3.3.15 Rule 2790—Restrictions on the purchase and sale of initial equity public offerings
- 5.3.3.16 Rule 3010 — Supervision
  - Supervisory system
  - Written procedures
  - Written approval
  - Taping rule
  - Definitions
    - Office of supervisory jurisdiction
    - Branch office
- 5.3.3.17 Rule 3120 — Use of information obtained in fiduciary capacity
- 5.3.3.18 Rule 3011—Anti-money laundering compliance program

**5.3.4 Responsibilities Relating to Associated Persons, Employees, and Other’s Employees**

- Rule 3030 — Outside business activities of an associated person
- Rule 3040 — Private securities transactions
  - Applicability
  - Written notice
  - Transactions for compensation
  - Transactions not for compensation
  - Definitions
- Rule 3050— Transactions for or by associated persons
- Rule 3060 — Influencing or rewarding employees of others
- Rule 3070 — Reporting requirements
- Rule 3080 — Disclosure to associated persons when signing Form U-4

**5.3.5 Trading**

- Rule 2320 — Best execution and interpositioning
- Rule 3310 — Publication of transactions and quotations
  - IM-3310 — Manipulative and deceptive quotations
- Rule 3320 — Offers at stated prices
  - IM-3320 — Firmness of quotations

**5.3.6 Procedural Rules**

- 5.3.6.1           Complaints, investigations and sanctions
  - Rule 8110 — Availability of Manual to customers
  - Rule 8120 — Definitions
  - Rule 8310 — Sanctions for violation of the rules
  - Rule 8320 — Payment of fines, other monetary sanctions, or costs; summary action for failure to pay
  - Rule 8330 — Costs of proceedings
  
- 5.3.6.2           Code of Procedure
  - Rule 9100 — Application and purpose
  - Rule 9200 — Disciplinary proceedings
  - Rule 9300 — Review of disciplinary proceeding by National Adjudicatory Council and NASD Board; application for Commission review
  - Rule 9500 —Other proceedings
  - Rule 9800—Temporary cease and desist orders
  
- 5.3.6.3           Code of Arbitration Procedure
  - Part I —Interpretive Material, Definitions, Organization and Authority
    - IM-12000 and IM-13000— Failure to act under provisions of code of arbitration procedure for customer/industry disputes
    - Rules 12105 and 13105—Agreement of the parties
  - Part II— General Arbitration Rules
    - Rule 12200—Arbitration under an arbitration agreement or the rules of NASD
    - Rule 12201—Elective arbitration
    - Rule 12202—Claims against inactive members
    - Rules 12204 and 13204—.Class action claims
    - Rule 12205—Shareholder derivative actions
    - Rule 13200—Required arbitration
    - Rule 13201—Statutory employment discrimination claims
    - Rule 13202—Claims involving registered clearing agencies
  - Part VIII —Simplified Arbitration and Default Proceedings
    - Rules 12800 and 13800— Simplified arbitration
    - Rules 12801 and 13801—Default proceedings
  
- 5.3.6.4           Rule 10400 — Mediation rules

## **5.4       Securities Investor Protection Act of 1970**

### **5.4.1       Customer Claims**

- Definition of “separate customer”
- Maximum limit on claims for securities
- Maximum limit on claims for cash

Valuation of claims  
Submission of claims to trustee

**5.4.2 SIPC vs. FDIC coverage**

General securities firms covered/government securities broker/dealers  
not covered

Requirement for government securities broker/dealers to disclose their  
customers are not covered by SIPC — '34 Act, 15C(a)(4)

## **6.0 Customer Considerations**

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### **6.1 Customer Accounts**

#### **6.1.1 Opening Customer Accounts**

- 6.1.1.1 Account documentation
  - NASD Rule 3110 – Books and records
    - Marking of customer order tickets
    - Customer account information
    - Changes in account name or designation
  - Customer name and residence
  - Whether of legal age
  - Reasonable effort to obtain:
    - Tax identification or social security number
    - Occupation of customer and name and address of employer
    - Whether associated person of another NASD member
  - Discretionary account information
    - Name and signature of person(s) authorized to exercise discretion
    - NASD Rule 2510 — Discretionary accounts
  
- 6.1.1.2 Supplementary documentation — definitions
  - Credit agreement
  - Credit terms disclosure
    - Evidence of authority for:
      - Corporate accounts
      - Partnership accounts
      - Trust accounts
      - Fiduciaries/administrators
      - Investment advisor
  - Hypothecation agreement
  - Joint account agreement form
    - Joint tenants with right of survivorship
    - Tenants in common
  - Loan consent agreement
  - Power of attorney
    - Limited authorization
    - Full authorization
    - Discretionary account
    - Joint tenants with rights of survivorship
  - W-9 backup withholding form
  
- 6.1.1.3 Special requirements for accounts of deceased persons

Uniform Transfer-on-Death Security Registration Act

Outstanding orders

    Cancellation

    Freeze on assets in account until necessary documents are obtained from administrator or executor of estate

6.1.1.4

Forms of ownership of securities

    Custodial accounts under the Uniform Transfers/Gifts to Minors Act

    Irrevocability of gift

    Custodian

    Shares registered to beneficiary upon attaining majority

    Individual registration

    Joint tenants with right of survivorship

    Tenants in common

    Trust accounts

6.1.1.5

Retirement and tax advantaged plans

    Qualified vs. non-qualified plans

    Rollovers and transfers

    Employer sponsored retirement plans

        HR10 plans (formerly KEOGH plans)

        401(k) plans

        403(b) plans

    Individual Retirement Accounts

        Traditional IRAs

        Roth IRAs

    ERISA

    Tax advantaged plans

        529 college savings plans

## 6.2 Recommendations to Customers

### 6.2.1 Investment Objectives of Customers

    Principal appreciation/growth

        Amount

        Investment horizon

    Income

        Current needs

        Preservation of capital

        Amount needed in future

            Accumulation period

            Payout period

### 6.2.2 Financial Status of Customers

    Expected changes in financial status

    Income and expenses

    Net worth

Participation in benefit plans

**6.2.3 Investment Constraints**

Ability or willingness to hold investments over relatively long periods  
Approximate age of customer  
Investment temperament and investment experience  
Liquidity and marketability needs  
Risk tolerance

**6.2.4 NASD Rule 2310 — Recommendations to Customers (suitability)**

IM2310-2—Fair dealing with customers  
Recommending speculative low-priced securities  
Excessive trading activity  
Fraudulent activity  
Fictitious accounts  
Discretionary accounts  
Unauthorized transactions  
Misuse of customers' funds or securities  
Recommending purchases beyond customer capability  
IM2310-3—Suitability obligations to institutional customers

**6.3 Risks and Strategies**

**6.3.1 Types of Risk**

Asset concentration  
Call/extension risk  
Credit risk  
Economic and political risk  
Event risk  
Inflation  
Interest rate risk  
Liquidity risk  
Market risk  
Purchasing power risk  
Reinvestment risk

**6.3.2 Investment Strategies**

Arbitrage techniques  
Barbell  
Butterfly  
Dollar cost averaging  
Hedged/unhedged positions  
Laddering of the portfolio  
Market timing  
Purchasing on margin  
Riding/rolling down the curve

Transactions designed to take advantage of yield differentials in the market

## **6.4 Account Transactions**

### **6.4.1 Information For Order Entry**

- Legal requirements (SEC Rule 17a-3)
- Time of entry/execution
- Terms and conditions of the order
- Price of execution
- If cancelled, a notation to that effect
- Whether a discretionary account
- Types of orders
  - Market orders
  - Specified price orders
  - AON vs. partial execution

### **6.4.2 Review Report of Execution against Order Ticket**

- Report execution to client
- Report errors immediately through appropriate firm channels

## **6.5 Tax Consequences of Securities Transactions**

### **6.5.1 Establishing the Cost Basis of Securities**

### **6.5.2 Determining the Holding Periods of Securities**

### **6.5.3 Tax Treatment of Securities Transactions**

- Definition of a capital gain/loss
- Computation of net capital gains/losses

### **6.5.4 Wash Sale Rules**

- Definition of a wash sale
- Applicable time period of 30 days prior to and after a sale
- Definition of “substantially identical” property

### **6.5.5 Tax Treatment of Interest Income on U.S. Government and Agency Obligations**

- Federal taxation
- State taxation
  - Exemption from taxation at state level for direct government obligations and certain agency securities
  - Other agency securities taxable at state level

### **6.5.6 Special Tax Features of Securities**

- Accretion of bond discounts

Accrued interest  
Amortization of bond premiums  
Original issue discount (OID)

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Frank J. Fabozzi and Steven Mann  
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1221 Avenue of the Americas  
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### **The Handbook of Mortgage-Backed Securities**

Frank J. Fabozzi, ed.  
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New York, NY 10020

### **How SIPC Protects You**

Securities Investor Protection Corporation  
805 15<sup>th</sup> Street, N.W., Suite 800  
Washington, DC 20005

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Robert Zipf,  
New York Institute of Finance  
New York, NY

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Sidney Homer and Martin L. Leibowitz  
Bloomberg Press (*on-line service*)  
[www.ordering1.us/bloombergbooks.com](http://www.ordering1.us/bloombergbooks.com)

### **Instruments of the Money Market**

Federal Reserve Bank of Richmond  
701 East Byrd Street  
Richmond, VA 23219

## Sample Question Format

The questions that follow are similar in format and content to questions on the actual examination. They are not intended, however, to parallel either the level of difficulty or the subject coverage of the examination. Their purpose here is to assist candidates and training personnel in preparing for the types of multiple-choice questions that will appear on the examination.

### Answers

1. (D)
2. (A)
3. (D)
4. (C)
5. (B)

1. Which of the following government securities is a direct obligation of the U.S. Treasury?

- (A) FHLB
- (B) FNMA
- (C) SLMA
- (D) STRIPS

2. Each of the following is an Agency security EXCEPT:

- (A) STRIPS
- (B) SLMA
- (C) FNMA
- (D) FHLB

3. The maximum maturity on a domestic bankers acceptance is:

- (A) 30 days
- (B) 90 days
- (C) 120 days
- (D) 180 days

4. Which two of the following are characteristics of Treasury bills?

- I. Issued at par
- II. Usually very liquid
- III. Mature in less than one year
- IV. More secure than Treasury bonds

- (A) I and III
- (B) I and IV
- (C) II and III
- (D) II and IV

5. If the U.S. balance of payments deficits should decrease, what would be the most likely effect on the dollar and on Treasury bonds?

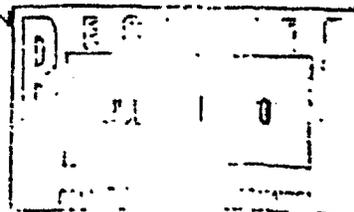
- |     | <u>Dollar</u> | <u>Bond Yields</u> |
|-----|---------------|--------------------|
| (A) | Weaker        | Higher             |
| (B) | Stronger      | Lower              |
| (C) | Weaker        | Lower              |
| (D) | Stronger      | Higher             |

Exhibit 3c  
SR-FINRA-2007-032



DIVISION OF  
MARKET REGULATION

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549



July 24, 2000

Mr. Alden S. Adkins  
Senior Vice President & General Counsel  
NASD Regulation, Inc.  
1735 K Street, N. W.  
Washington, D.C. 20006-1500

Re: Procedure for Filings Relating to Qualification Examinations

Dear Mr. Adkins: <sup>Alina</sup>

I am writing to inform you of a change in the filing requirements for proposed rule changes involving qualification examinations for associated persons. In the past, the Division required the SROs to file question banks for new examinations for Commission approval pursuant to Section 19(b)(2) of the Exchange Act. The Division also required SROs to file questions being added to the question bank for Commission approval.

The Division has decided that it is no longer necessary for SROs to file new exam question banks for Commission approval under Section 19(b)(2). In the future, any new examinations should be filed as non-controversial rule changes for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Exchange Act and Rule 19b-4(f)(6) thereunder. As you know, Rule 19b-4(f)(6) requires the SRO to give notice to the Commission of its intent to file a proposed rule change five days before doing so. During the five days prior to filing, the Division will determine if the proposed rule change is appropriately filed as non-controversial. To assist us in our analysis, please include a complete description of the examination in your rule filing. For example, the proposed rule change should address who will be required to take the exam, what information the exam will cover, the time allotted for each section, the weight assigned to each topic, the effective date of the exam requirement, and any other information that would be helpful to us in determining whether the proposal should become effective on filing. Also, pursuant to Rule 19b-4(f)(6), the rule change should be designated as effecting a change that does not significantly affect the protection of investors or the public interest, does not impose any significant burden on competition and, by its terms, does not become operative for 30 days after the date of the filing.

Alden S. Adkins  
Page 2

Filings to modify an existing examination should be submitted as "constituting a stated policy, practice, or interpretation with respect to the meaning, administration or enforcement of an existing rule..." pursuant to Section 19(b)(3)(A) of the Exchange Act.

Our goal in changing these procedures is to expedite the effectiveness of proposed rule changes involving examination requirements for persons associated with SRO members. Please contact Kathy England, Assistant Director, at 202-942-0154, or Karl Varner, Special Counsel, at 202-942-7125, if you have any questions.

Sincerely,



Belinda Blaine  
Associate Director