

# **Content Outline for the S101 Regulatory Element**

## **Introduction**

The Securities Industry Continuing Education Program (CE Program), which is required by the rules of several self-regulatory organizations (SRO), is a two-part program composed of a Firm Element and a Regulatory Element. The Firm Element is developed and must be delivered by each firm on an annual basis. The Regulatory Element is developed by industry committees representing a diverse range of broker-dealers, in conjunction with the Securities Industry/Regulatory Council on Continuing Education, industry regulatory agencies and SROs. The CE Program is intended to keep registered securities industry personnel current regarding rules and other issues important to performing their jobs appropriately.

## **The Regulatory Element**

The Regulatory Element requires all registered persons to participate in a prescribed computer-based training session within 120 calendar days of their second registration anniversary date and every three years thereafter. The Regulatory Element is designed to cover significant subject matter that is broadly applicable to all registered persons.

The Regulatory Element focuses on compliance, regulatory, ethical and sales-practice standards. Its content is derived from rules and regulations, as well as standards and practices widely accepted within the industry. Although the specific requirements of certain rules may differ slightly among the various SROs, the program is based on standards and principles applicable to all. In certain instances, particular SRO requirements may be more restrictive than those represented in the Regulatory Element. Additionally, many broker-dealers may have policies and procedures that are more restrictive than industry regulations regarding the types of activities in which their registered employees may engage, the investment products they may represent, and/or specific approvals required for certain functions. Registered persons and their supervisors are responsible for ensuring that their activities are within the scope permitted by their employing broker-dealers and conducted in accordance with the rule requirements of all of the SROs and jurisdictions regulating them.

The S101 Regulatory Element Program (the General Program or S101) is required for Series 7 registered persons and those persons in all other registration categories except principal/supervisor or Series 6 registered. The content for the S101 is organized into four modules, as well as common topics that may be covered in any of the four modules. Topics identified in this outline are covered thoroughly in the modules, and some may be covered in more than one module. The content coverage of each of these modules and the common topics are outlined following this introduction. Unless otherwise specified, the topics are covered at basic levels of knowledge and understanding.

Please note that individuals may see a sample case and the orientation for the Regulatory Element by visiting [www.finra.org/ce/training](http://www.finra.org/ce/training). The sample case and orientation is provided as a resource to those who would like to familiarize themselves with the program format and features. Those required to sit for the Regulatory Element in the near future are encouraged to review the sample case and orientation prior to sitting for their session.

## **Presentation of the Training**

Participants in the S101 are able to choose the order in which to complete the four required modules. In each module of the S101, participants are led through a case that provides a story depicting situations that may be faced by registered persons in the course of their business. Each case contains significant educational content, including optional material called Resources and Glossary Rollovers. Participants must review the story content of each case but may choose whether or not to utilize the optional materials. Participants are encouraged to utilize all of the educational content provided in the S101, including the optional material, as it is designed to aid understanding and enhance the educational experience for the participant.

The format of the cases in the S101 Program is primarily text-based with some media treatments that provide important information, context and education related to the story.

## **Assessment, Proficiency and Timing**

As part of each case, participants are presented a series of questions. These questions, which relate to the story and facts presented in the case, are designed to assess the participants' understanding of the materials presented. The participant must demonstrate his or her understanding of the subject matter by choosing the most appropriate response(s) to questions. If the individual does not demonstrate proficiency with the subject matter, additional content may be provided.

Participants must demonstrate proficiency in each of the four modules of the S101. Participants will be provided a maximum of two cases in each module to demonstrate proficiency. Participants who do not demonstrate proficiency in any one module will not be able to complete the Regulatory Element requirement within that session. In the event a module is not completed, participants may terminate the incomplete session or may continue to review the remaining material for the added educational benefit. In either event, participants will not be able to complete the Regulatory Element requirement in that session and must schedule another session in order to satisfy the requirement.

The S101 Program is designed to provide ample time to complete the required materials within the 3½ hour timeframe allotted. Failure to complete the Regulatory Element within 120 days of the prescribed anniversary date will result in a person's registration becoming inactive. This means that he or she may not engage in, or be compensated for, activities requiring a securities registration until he or she satisfies the requirements.

## **Module A: Communications with the Public**

### **A.1 Types of Communications**

#### **A.1.1 Written and Electronic Communications**

- Definitions, use, approval, and retention requirements for written communications, including, but not limited to:
  - ❖ Correspondence
  - ❖ Advertising
  - ❖ Sales literature, such as research reports
  - ❖ Electronic communications including e-mail, websites, text and instant messaging, weblogs (blogs), podcasts, online bulletin boards or other postings, and social networking websites.

#### **A.1.2 Oral and Other Communications**

- Approval and retention requirements for seminars, public speaking engagements, testimonials, and communications in and with the press.
- Telemarketing restrictions, cold calling, various Do-Not-Call lists, Federal regulations applicable to broker-dealers when contacting prospective clients.
  - ❖ Requirements and industry best practices pertaining to the use of scripts.

### **A.2 Content Standards, Review, and Approval Requirements**

- Guidelines for ensuring that all communications are fair and balanced and do not contain misleading, exaggerated or unwarranted statements, or omit material facts.
- Prohibited distribution of confidential material including internal-use-only and broker-dealer-use only materials.
- Prohibited communications, including predictions and projections, guaranteeing performance, and blanket recommendations.
- Requirements for maintaining records of communications distributed to the public and complying with firm policies to support the requirement.
- Use of professional designations

- Required disclosures and restrictions when communicating with the public, such as:
  - ❖ Use of testimonials
  - ❖ Use of copyrighted material and research
  - ❖ Product-specific disclosure documents, such as the Options Disclosure Document (ODD)
  - ❖ Making written investment recommendations.
- Institutional communications:
  - ❖ Content standards of sales material and correspondence
  - ❖ Approval, recordkeeping, and spot-check procedures.

## **Module B: Suitability**

### **B.1 Client Information**

- Requirements for determining suitability of investments before making recommendations.
- Responsibilities for obtaining information including, but not limited to a client's:
  - ❖ Financial data such as net-worth, annual income and tax status.
  - ❖ Life profile information such as employment, marital status, and number of dependents.
  - ❖ Account profile information such as investment objectives, risk tolerance, and time horizon.
- Confirming client information within 30 days of account opening, upon update of account information, or at least every 36 months.

### **B.2 Concepts and Implications Related to Risk**

- Risks, features, and required disclosures for various investment accounts including retirement plans and education savings accounts.
- Disclosure and explanation of risks associated with recommendations.

- Types, potential implications, and examples of risk including, but are not limited to, call risk, concentration risk, credit risk, emerging market risk, interest rate risk, legislative risk, liquidity risk, market risk, purchasing power risk (inflation risk), reinvestment risk, principal risk, currency risk, political risk, sector risk, sovereign risk.
- Characteristics and risks of investment products, including, but not limited to:
  - ❖ Equity securities
  - ❖ Fixed income securities
  - ❖ Municipal securities
  - ❖ Listed and OTC Options
  - ❖ Preferred/Convertible securities
  - ❖ Low-priced securities
  - ❖ American Depository Receipts (ADRs)/American Depository Shares (ADSs)
  - ❖ Cash alternatives
  - ❖ Derivatives; futures and currencies
  - ❖ Alternative investments
  - ❖ Structured products
  - ❖ Hedge funds
  - ❖ Mutual funds
  - ❖ Exchange Traded Funds (ETFs)
  - ❖ Real Estate Investment Trusts (REITs)
  - ❖ Unit Investment Trusts (UITs)
  - ❖ Limited partnerships
  - ❖ Private placements
  - ❖ Variable contracts.

### **B.3 Monitor Clients' Information and Accounts**

- Responsibilities for monitoring and periodically confirming information including, but not limited to a client's:
  - ❖ Financial data such as net-worth, annual income and tax status.
  - ❖ Life profile information such as employment, marital status and number of dependents.
  - ❖ Account profile such as investment objectives, risk tolerance, and time horizon.
  - ❖ Changes in circumstances, holdings, and other applicable information.
- Support the firm's requirement to record and confirm changes with the client by promptly recording and reporting changes for client account information.
- Understanding and applying principles of diversification.
- Solicited (recommended) versus unsolicited (not recommended) transactions.
- Sales practices used when servicing senior investors:
  - ❖ Account transactions
  - ❖ Suitability of products
  - ❖ Public appearances (seminars and speaking engagements)
  - ❖ Diminished capacity
  - ❖ Use of professional designations claiming expertise in senior issues.

## **Module C: Handling Customer Accounts, Trade and Settlement Practices**

### **C.1 Account Opening and Client Information**

- Procedures for opening and maintenance of client accounts including required approvals and recordkeeping requirements.
- Customer Identification Program (CIP)
- Clients address issues, such as P.O. boxes and legal and temporary addresses
- Deceased accounts

- Procedures and requirements for account transfers/ACATS
- Option accounts/approvals/agreement/ODD
- Delivery of account documentation including, but not limited to margin disclosure, prospectuses, and insurance contracts.
- Confirmations & statements
- Safeguarding firm and client information
  - ❖ Privacy rules (Regulation SP)
  - ❖ IT security
  - ❖ Document security and destruction
  - ❖ Required initial, annual, and opt-out notifications.
- Securities Investor Protection Corporation (SIPC): Purpose of SIPC, coverage limits and amounts, disclosures to clients.
- Bank sweep programs: Disclosures regarding protection features, methods of determining interest rates, and compensation.
- Federal Deposit Insurance Corporation (FDIC): An agency of the Federal Government established to insure the deposits of account holders at FDIC member institutions.

## **C.2 Anti-Money Laundering**

- Recognizing the three stages of money laundering:
  - ❖ Placement
  - ❖ Layering
  - ❖ Integration.
- Anti-Money Laundering Rules, USA PATRIOT Act, and the Bank Secrecy Act
- Customer Identification Program (CIP)
- Potential indicators (“red flags”) to detect money laundering

- Cash/Equivalents/Deposits & Reporting Requirements
  - ❖ Currency Transaction Reports (CTRs)
  - ❖ Suspicious Activity Reports (SARs)
- Understanding the role of the Office of Foreign Assets Control (OFAC)
  - ❖ Specially Designated Nationals (SDN) List
- Understanding the role of the Financial Crimes Enforcement Network (FinCEN)

### **C.3 Trade Approval / Account Activity**

- Requirements for order entry and price reporting.
- Order ticket requirements, such as recording transactions as solicited or unsolicited.
- Types of orders and required disclosures for penny stocks, options, and short sales.
- Requirements for trade errors and account changes.
- Requirements for conducting third-party transfers or disbursement of funds.
- General requirements for payment and trade settlement
  - ❖ Consequences of nonpayment/nondelivery
- Restrictions, approvals and disclosure requirements when accepting or paying referral fees.

### **C.4 Trading Authorization**

- Orders from someone other than the account owner
  - ❖ Requirements for issuing third-party checks and wire transfers.
  - ❖ Requirements for written authorization of orders.
- Understanding the various types of Powers of Attorney (POA)
  - ❖ Differences between limited and full trading authorization.
  - ❖ Obligations of and limits on fiduciaries, limits on the use of powers of attorney.

- Discretionary Trading/Discretionary Accounts
  - ❖ Required approvals and procedures when using discretion.
- Time & Price Discretion

### **C.5 Client Complaints and Inquiries**

- Identifying client complaints.
- Requirements for investigating and documenting client complaints.
- Broker-dealer and RR reporting requirements.
- Responding to requests for information.
- Information disclosed in disciplinary records and/or Forms U4 and U5.
- Arbitration procedures and awards and required regulatory reporting.
- Mediation and negotiated settlements.

### **C.6 Prohibited/Fraudulent Practices**

- Definitions and examples of detecting prohibited and improper activities such as:
  - ❖ Insider trading
  - ❖ Circulation of rumors
  - ❖ Entering false orders
  - ❖ Misappropriation of funds
  - ❖ Forgery
  - ❖ Unauthorized trading
  - ❖ Guarantees to clients
  - ❖ Selling away
  - ❖ Piggybacking/shadowing
  - ❖ Selling dividends

- ❖ Commingling funds
- ❖ Selling to breakpoints
- ❖ Churning
- ❖ Switching
- ❖ Market manipulation
- ❖ Unfair/excessive pricing
- ❖ Front-running
- ❖ Free-riding
- ❖ Parking
- ❖ Trading at the close/marketing the close.

### **C.7 Client Account Registrations**

- Understanding the purpose and characteristics of account types, including:
  - ❖ Individual
  - ❖ Corporate
  - ❖ Joint Accounts
    - Joint Tenants with Right of Survivorship (JTWROS)
    - Tenants in Common (TIC)
    - Community Property (CPWROS)
  - ❖ Transfer on Death (TOD)
  - ❖ Custodial Account (UGMA/UTMA)
  - ❖ Trust Accounts (e.g., Revocable, Irrevocable, etc.)
  - ❖ Charitable and foundation accounts
  - ❖ Retirement accounts

- ❖ Educational funding accounts (e.g., 529 College Savings Plans and Coverdell Education Savings accounts).

## **C.8 Margin and Margin Related Issues**

- Basic distinctions between cash and margin accounts.
- Responsibility for ensuring the clients' understanding of the associated risks when using margin.
- Appropriate use of margin and its associated risks (e.g., margin calls, loss of voting power, liquidation of securities).
- Purpose versus non-purpose loans
- Initial, maintenance, and house margin requirements:
  - ❖ Regulation T requirements
  - ❖ Meeting margin calls, including maintenance liquidations.
- Disclosing terms and costs of margin
- Furnishing the margin disclosure document.
- Day trading requirements

## **C.9 Retirement Plans**

- Characteristics including eligibility, employee coverage, types of contributions, maximum contribution limits, taxation of investments within a plan, distribution options and allowable exceptions, taxation of distributions, minimum distribution requirements, penalties for premature distributions, rollovers, excess contributions.
- Characteristics of various Individual Retirement Accounts (IRAs) including, but not limited to:
  - ❖ Traditional
  - ❖ Rollover
  - ❖ Roth
  - ❖ Spousal
  - ❖ Inherited/Beneficiary.

- Characteristics of various Employer sponsored plans, including, but not limited to:
  - ❖ Defined contribution and defined benefit plans
  - ❖ Profit sharing and money purchase plans
  - ❖ SEP (Simplified Employee Pension) plans
  - ❖ 401(k) plans
  - ❖ 403(b) tax-deferred annuity plans/custodial accounts
  - ❖ SIMPLE IRA/401(k) plans.

## **C.10 Investment Companies**

- General characteristics, and the similarities and differences among open and closed-end investment companies, real estate investment trusts, and exchange-traded funds.

### **C.10.1. Mutual Funds**

- Types of mutual funds, including but not limited to equity funds, fixed-income funds, hybrid funds (balanced), money market funds, sector funds, sector diversified funds, specialty funds.
- Structure, operation, and costs:
  - ❖ Systematic investing/withdrawals
  - ❖ Dollar-cost averaging
  - ❖ Net Asset Value (NAV)
  - ❖ Share classes.
- Sales charges:
  - ❖ Computation and types, such as front end load, level load, contingent deferred sales charge (CDSC), and no load.
  - ❖ Qualification for reduction using breakpoint discounts.
  - ❖ Letters of Intent and Rights of Accumulation.
  - ❖ Expenses and 12b-1 fees.

- Activities, services and requirements:
  - ❖ Statutory and Summary Prospectus delivery requirements
  - ❖ Availability of statement of additional information (SAI)
  - ❖ Exchange privileges/conversions/redemptions
  - ❖ Rights of Reinstatement
  - ❖ Exchanging shares of a mutual fund for a comparable number of shares to a fund within the same fund family.
  - ❖ Switching of existing mutual fund shares for another share class or fund outside of the fund family.
  - ❖ Inappropriate sales activities (e.g., late trading, market timing, selling to breakpoints, selling dividends).
  - ❖ Tax consequences from trading activities by the Investment Company and the investor.
- Types of distributions:
  - ❖ Net investment income
  - ❖ Capital gains
  - ❖ Return of capital.

### **C.10.2 Real Estate Investment Trusts (REITs)**

- ❖ Definition, characteristics, and operation
- ❖ Investment considerations (e.g., risks and benefits) including suitability.

### **C.10.3 Exchange-Traded Funds (ETFs)**

- ❖ Characteristics, including how they are structured, traded and priced.
- ❖ Investment considerations (i.e., risks and benefits) and suitability.

## C.11 Variable Annuities & Variable Life Contracts

- Characteristics of variable annuities and comparison to fixed annuities.
- Types of variable products such as bonus, deferred, and immediate variable annuities.
- Sales charges, surrender charges, fees and related expenses (e.g., mortality and expense charges, administrative fees and underlying fund expense charges).
- Insurance company ratings (stability of the issuer)
- Valuation of a variable annuity contract
- Separate account
  - ❖ Subaccount investments
- Tax treatment of individual, tax-deferred variable annuities
- Free-look provisions
- Optional enhanced death benefit
- Living benefit riders:
  - ❖ Guaranteed Minimum Income Benefit (GMIB)
  - ❖ Guaranteed Minimum Withdrawal Benefit (GMWB)
  - ❖ Guaranteed Minimum Accumulation Benefit (GMAB).
- Required disclosures, costs and features of bonus annuities.
- Supervisory review requirements for sales of deferred variable annuities:
  - ❖ Suitability and disclosure obligations for recommended transactions.
  - ❖ Review and approval requirements, including the timing of principal approval.
- Suitability and required disclosures and approval for IRS 1035 Exchanges.
- Prospectus delivery requirements for variable annuities and variable life contracts.
- Characteristics of variable universal and variable life insurance (fixed and flexible premium types).

## **C.12 Other Product Related Issues**

- Tax consequences for various types of products and accounts.
- Understanding the use of cost basis information.
- Dividends and ex-dividends
- Reorganization events (e.g., mergers and acquisitions, odd-lot tender, stock splits, etc.)
- Requirements for disclosing pricing and/or fees relating to commissions, mark-ups and mark-downs, and account service fees.
- Managed accounts
- On-line trading
- Investment Adviser activities by RRs.

## **Module D: New and Secondary Offering and Corporate Finance**

### **D.1 SEC Registration and Prospectus Requirements**

- Registration requirements
- Preliminary prospectus (red herring)
- Limits on advertising and other written materials
- Prospectus delivery requirements
- Prohibition of sales before effective date
- Restrictions before, during, and after a distribution
- Rule 144/Restricted securities

### **D.2 Research & Investment Banking**

- Policies and procedures to provide separation between investment banking and the sales, trading, and research areas of a broker-dealer (Information Barriers).
- Restricted interaction and communication between research and investment banking personnel (e.g., pitch books, roadshows, and conferences).

- Broker-dealer restricted and watch lists
- Proprietary and employee trading accounts (both in and away from the broker-dealer)
- Research/Research reports review and approval for use
- Prohibitions on dissemination or use of material nonpublic information (insider trading).

### **D.3 Public Offerings**

- Transactions relating to Initial Public Offerings
- Syndicate activities; policies and procedures when allocating new issue securities to the public:
  - ❖ Indications of Interest (IOI)
  - ❖ Restricted persons and accounts
  - ❖ Selling Agreement: Agreement between a selling dealer and primary distributor providing for the sale to clients by the selling dealer of open-end fund securities.
  - ❖ Official Statement/Prospectus: Discloses material information about a new municipal issue.
- Functions of the syndicate/underwriting group:
  - ❖ Managing underwriter (s)
  - ❖ Selling group.
- Requirements and restrictions when obtaining indications of interest.
- Understanding allocation processes:
  - ❖ Distribution of shares among broker-dealers in the selling group.
  - ❖ Distribution of shares among those customers who submitted indications of interest.
- Certain post-effective issues:
  - ❖ Lock-up period
  - ❖ Prohibition on flipping

- ❖ Penalty bids
- ❖ Understanding stabilizing transactions.
- Secondary Offering/Follow-On Offering/Aftermarket: Regulation M, trading in existing or outstanding shares of securities on either a national exchange or OTC market.
- Electronic Municipal Market Access System (EMMA).

#### **D.4 Private Placement Offerings**

- Exemptions from registration
- Regulation D Offering
  - ❖ Accredited investor and non-accredited investor
- Disclosure requirements including, but not limited to Private Offering Memorandum/Subscription Agreement requirements.
- Resale restriction (s).

### **E: Common Topics**

Topics identified in this section of the outline will be integrated into cases presented for each of the four modules noted and outlined above.

#### **E.1 Ethics and Business Conduct**

- Observe high standards of commercial honor, conduct activities in accordance with good business practices, and honor just and equitable principles of trade.
- Restrictions, required approvals, and legal risks associated with private securities transactions.
- Permitted and prohibited outside business activities including issues associated with dual licensing, part-time employment, and conflicts of interest.
- Required notifications and approvals for outside business activities/accounts/investments.
- Rules, regulations and standards governing sharing commissions or compensation.
- Prohibition on compensating unregistered persons and/or non-brokers and/or dealers.

- Restrictions, approval and disclosure requirements for payment of referral fees to nonaffiliated persons.
- Restrictions on loans to or from clients.
- Prohibitions against as well as understanding and recognizing conflicts of interest and potentially illegal situations.
- Restrictions on giving and receiving gifts and gratuities including supervisory or approval requirements.
- Non-cash compensation and sales contests.
- “Prudent Man” Rule.

## **E.2 Registration and Licensing Requirements**

### **E.2.1. Registration and licensing-related issues and requirements for individuals and the broker-dealer**

- Requirements of the self-regulatory organizations (SROs).
- State authority and jurisdiction.
- State registration and licensing requirements for registered persons and broker-dealers.
- Conditions, restrictions and requirements for amending Form U4.
- Restrictions on the activities of RRs.
- Differences between insurance appointments and securities licensing.
- Selling agreements.
- Insurance licensing for variable annuities.
- General requirements and limitations on activities as well as registration and licensing for investment advisers.
- Restrictions on activities of unregistered persons.
- Consequences of violating registration or licensing requirements.
- Understanding Continuing Education requirements including the Regulatory Element and Firm Element.

### **E.2.2. Blue-Sky Laws and Registration of Securities**

- Requirements for securities to be registered or exempt in states in which they are being sold.
- Distinction between exempt/nonexempt securities.
- General exemptions from registration.

### **E.3 Reporting and Other Requirements**

#### **E.3.1 Securities and Exchange Commission (SEC) and SRO Authority and Investigations**

- Understanding the regulatory structure of the securities industry.
- Jurisdiction of the SEC, SROs, and state regulators.
- Obligations to respond to regulatory inquiries.
- Definition and consequences of statutory disqualification.
- Settlement of employer-employee disputes.