

# NASD NOTICE TO MEMBERS 96-14

## SEC Approves Amendments To Sections 1(a)(v) And 73 Of NASD Uniform Practice Code Relating To The Use Of Standardized Limited Partnership Transfer Forms

### Suggested Routing

- Senior Management
- Advertising
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

### Executive Summary

On January 29, 1996, the Securities and Exchange Commission (SEC) approved amendments to Sections 1(a)(v) and 73 of the NASD<sup>®</sup> Uniform Practice Code (UPC) that requires members to use standardized limited partnership transfer forms when transferring interests in a limited partnership security. The text of amendments and the new limited partnership transfer forms follow this Notice. The use of the forms becomes mandatory **on May 15, 1996**.

Although only NASD members are required to use the standardized forms, the NASD has worked closely with sponsors and industry groups in designing these forms and believes that general partners and transfer agents engaged in the transfer of limited partnership securities will use and honor the forms to establish uniform transfer practices and procedures industry-wide.<sup>1</sup>

### Background

Historically, limited partnership securities were not structured to be freely transferrable in secondary market transactions. However, secondary markets now exist for many limited partnership securities, and are in addition to the large publicly traded partnerships that list on The Nasdaq Stock Market<sup>SM</sup> and the national securities exchanges. Therefore, it is critical to process limited partnership securities transfers more timely and accurately.

The terms and requirements relating to the transfer of limited partnership interests are controlled by the partnership agreement,<sup>2</sup> almost all of which state that assignment or transfer of limited partnership interests requires the consent and approval of the general partner(s). As a result, when transferring limited partnership interests, NASD members are currently confronted with transfer

requirements unique to each partnership that may vary widely on the type and amount of documents necessary for the valid transfer of a partnership interest. Some partnership agreements require information so extensive that the transfer documents sometimes reach 30 to 40 pages. The transfer of the partnership interest may take up to six months, in some cases, to be finalized. However, in most cases, prior to the recognition by the general partner of the actual transfer of the partnership property interest from one holder (transferor/seller) to another (transferee/purchaser), a security interest in the property is created whenever the purchaser gives and seller accepts economic consideration to secure the purchaser's right to have the partnership interests transferred. The security interest creates the right for the purchaser to have the security interest transferred in advance of the date specified in the partnership agreement and entitles the purchaser to legal certainty that his or her ownership rights can be recognized and protected until the actual transfer of the partnership interest is complete.

Transfer delays of the security interest and nonstandardized payment provisions have also caused or contributed to delays or mistakes in the allocation of cash distributions between buyers and sellers. A seller of a limited partnership interest, as a

<sup>1</sup> The NASD has worked closely with transfer agents who specialize in the transfer of partnership securities, and the Investment Partnership Association, a trade organization for the partnership industry, to reach an informal consensus on the general applicability of forms throughout the industry.

<sup>2</sup> The Revised Uniform Limited Partnership Act and the Delaware Revised Uniform Limited Partnership Act expressly provide for the ability to recognize transfers and admit new partners under whatever rules the general partners design.

recordholder of the securities, often receives distributions that rightly should have accrued to the buyer and subsequently disposes of such distributions without knowledge of the claims of purchasers. Under current transfer standards and practices, buyers and sellers of limited partnership securities in the secondary market often cannot protect their rights to such distributions. This leads to disputes over distributions that often must be settled by broker/dealers at their own expense or through arbitration or litigation.<sup>3</sup>

### Description

To provide a uniform way for members that transfer limited partnership interests to receive and recognize information on the valid transfer of the security interest separate and apart from the partnership interest, and to record information of valid transfer on members' books and records, the NASD has amended Section 1(a)(v) of the UPC so that the UPC will apply to over-the-counter secondary market transfers of Direct Participation Programs to the extent provided in individual provisions of the UPC. New Section 73 has also been added to the UPC to require members to use standardized transfer forms that are in Exhibit A to Section 73 when transferring limited partnership securities. Section 73 does not apply to limited partnership securities that are traded on The Nasdaq Stock Market or a registered national securities exchange. Such securities trade and settle on a regular-way basis, like publicly traded common stock, and do not require the use of extensive transfer documents. The forms standardize the format for gathering transfer information by members and registered representatives, reduce the amount of information necessary to perform a valid transfer, and eliminate delays and inefficiencies in the transfer and settlement process.

The standardized transfer forms in Exhibit A to Section 73 include:

- **Transferor's (Seller's) Application For Transfer and Transferee's (Buyer's) Application For Transfer** that contain the essential information necessary to perform a valid transfer, including customer identification, partnership identification, tax identification, quantity transferred, broker/dealer and registered representative involved, and signature execution.

- **Registration Confirmation Form** that confirms to the buyer/transferee that the transfer has been completed and contains information regarding, among other things, the partnership's NASD symbol, CUSIP number, tax identification number, number of units transferred, and the effective/admission date.

- **Distribution Allocation Agreement** that is to be completed when the transfer documents are completed and sent to the general partner of the limited partnership security being transferred. The agreement contains certain affirmations on which the transferor and transferee agree and acts as a contract between the buyer and seller setting forth their agreement regarding all unpaid distributions. The agreement specifies when the transferee becomes the unitholder of record, when a unitholder of record is entitled to cash distributions and capital distributions, and who is responsible for correcting a distribution made to the wrong party. The agreement requires, among other things, the party who incorrectly receives a distribution to promptly endorse and deliver to the correct party the distribution checks or otherwise pay to the other party the amount of such distribution.

The NASD believes that, over time, as the use of the standardized forms becomes commonplace, they will significantly reduce the time and

effort required by member firms to process limited partnership transfers from its current time of about 180 days to less than 30 days. The use of standardized forms will also permit uniform identification of limited partnership securities between members that should facilitate transfer of customer accounts through the Automatic Customer Account Transfer System (ACATS). In particular, the use of the Distribution Allocation Agreement will help to provide certainty as to the buyer/transferee and seller/transferor regarding distributions not yet announced or received by memorializing the agreement between the buyer and seller as to the method for handling distributions. The Distribution Allocation Agreement will also prevent member broker/dealers representing such buyers and sellers from effecting and settling trades without knowledge of the buyers' and sellers' rights to any distributions.

The use of the forms will become mandatory for NASD members and registered representatives **on May 15, 1996**.

Questions about this Notice may be directed to Carl R. Sperapani, Assistant Director, Corporate Financing Department, at (301) 208-2759; Dorothy Kennedy, Assistant Direc-

<sup>3</sup> These problems are exacerbated by the fact that general partners relying on no-action letters issued by the Division of Market Regulation do not believe they are required under SEC Rule 10b-17 to publicly disclose the payment of regular or special distributions. In response to this issue, the NASD Board of Governors approved, and the staff has filed, a petition with the SEC that requests that the SEC take action to require that partnership distributions be disclosed timely to the market pursuant to SEC Rule 10b-17 (*See*, Correspondence of John E. Pinto, Executive Vice President, NASD, to Jonathan G. Katz, Secretary, SEC, dated February 14, 1996, SEC File No. 4-386.).

tor, Nasdaq Market Operations, at (203) 385-6243; or Robert J. Smith, Attorney, Office of General Counsel at (202) 728-8176.

### Text Of Amendments

(Note: New text is underlined.)

## UNIFORM PRACTICE CODE

### Scope of Uniform Practice Code

#### Sec. 1

(a) All over-the-counter secondary market transactions in securities

between members shall be subject to the provisions of this Code except:

(i) through (iv) No change.

(v) transactions in Direct Participation Program securities as defined in Article III, Section 34 of the Association's Rules of Fair Practice, except as otherwise provided in this Code.

**Sec. 2** through **Sec. 72** No change.

Limited Partnership Securities

#### Sec. 73

Each member who participates in the transfer of limited partnership securities, as defined in Article III, Section 34 of the Association's Rules of Fair Practice, shall use standard transfer forms in the same form as set forth in Exhibit A of this section. This section shall not apply to limited partnership securities which are traded on the Nasdaq Stock Market or a registered national securities exchange.