

# Notices

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## Research Analysts and Research Reports

### FINRA Provides Guidance on Prohibition Against Offering Favorable Research to Induce Investment Banking Business

#### Executive Summary

FINRA is reminding member firms of the need for heightened supervision over solicitation and research activities in circumstances where an issuer has communicated an expectation of favorable research as a condition of participating in an offering.

Questions concerning this *Notice* should be directed to Philip Shaikun, Associate Vice President, Office of General Counsel, at (202) 728-8451.

#### Background and Discussion

NASD Rule 2711 fosters objectivity in research reports by, among other things, insulating research analysts from pressure to tailor their coverage to the interests of a firm's current or prospective investment banking clients. To that end, NASD Rule 2711(e) prohibits firms from directly or indirectly offering favorable research or a specific rating or price target as consideration or inducement for the receipt of business or compensation. NASD Rule 2711(c)(4) prohibits research analysts from participating in efforts to solicit investment banking business, including participation in "pitches" to prospective investment banking clients and other communications with issuers for the purpose of soliciting investment banking business. FINRA has interpreted that provision to prohibit in pitch materials any information about a firm's research capacity in a manner that suggests, directly or indirectly, that the firm might provide favorable research coverage.<sup>1</sup>

September 2011

#### Notice Type

- ▶ Guidance

#### Suggested Routing

- ▶ Compliance
- ▶ Investment Banking
- ▶ Legal
- ▶ Research
- ▶ Senior Management

#### Key Topics

- ▶ Conflicts of Interest
- ▶ Research

#### Referenced Rules

- ▶ NASD Rule 2711
- ▶ NTM 07-04
- ▶ SEC Regulation AC

It has come to FINRA's attention that certain issuers may be attempting to extract implicit promises of favorable research by suggesting publicly or directly to potential deal participants in advance of an anticipated offering that positive research coverage will be an implicit or explicit condition to selection as an underwriter or selling group member. The suggestions may take the form of hints, insinuations or other subtle references, but are intended to condition the award of investment banking business on the nature of research attendant to the deal. For example, the CEO of an issuer recently stated in an interview that he was dissatisfied with the tone of research coverage of his company by certain firms that previously served as underwriters for the company. As a result, the CEO reportedly intends to require candidates for the company's next offering to demonstrate "a clear understanding of who [the company] is and our trajectory, and why [the company] is a stock that investors should own." He further is quoted as saying, "If I'm confident they can articulate that well, they will have a chance" at being selected as an offering participant.<sup>2</sup>

FINRA views these and similar advance statements as attempts to create an expectation that a firm chosen to participate in a subsequent offering will maintain favorable research on the issuer's stock, irrespective of the stock price or the company's ongoing performance. FINRA views even tacit acquiescence to such overtures to be a violation of NASD Rule 2711(e),<sup>3</sup> and under certain facts and circumstances, potentially a violation of NASD Rule 2711(c)(4).

FINRA understands that such uninvited pronouncements place prospective offering participants in a challenging situation should they seek to compete for a role in the offering. Nonetheless, in circumstances where an issuer makes known, expressly or implicitly, that the selection of an offering participant will be predicated on an expectation of positive research coverage, FINRA will closely scrutinize offering participants' research and other deal-related activities for compliance with, among others, NASD Rule 2711 and SEC Regulation Analyst Certification.

Member firms that choose to compete for or participate in offerings under such circumstances must expressly repudiate to the issuer any expectation with respect to the content of research coverage and document such repudiation. In addition, the firms must implement heightened supervision of their solicitation activities, including pitch meetings and other communications with the issuer, to ensure there is no express or implied acknowledgement or accedence to the research expectation. Finally, members must increase oversight of the preparation and content of their research on the subject company—both before and after deal participants are chosen—including any permissible communications between research and investment banking personnel.

## Endnotes

1. *See Notice to Members 07-04* (January 2007).
2. Serena Ng, *AIG Gets Tough on Analyst Views*, Wall Street Journal, August 26, 2011.
3. While FINRA is concerned with the action of the issuer in such scenarios, FINRA generally does not have jurisdiction over the conduct of non-broker-dealer issuers and their employees and agents.

## Operations Professional Qualification Examination

### Operations Professional Qualification Examination, Examination Fee and Initial Rollout Period

#### Executive Summary

This *Notice* provides member firms with information on the Operations Professional qualification examination, related examination fee and special procedures on the initial rollout of the examination. Candidates for the Operations Professional qualification examination will be able to schedule and take the examination beginning on October 17, 2011. The content outline for the examination is available on FINRA's [website](#).

Questions regarding this *Notice* should be directed to:

- ▶ Joe McDonald, Senior Director, Testing and Continuing Education Department, at (240) 386-5065; or
- ▶ Erika L. Lazar, Counsel, Office of General Counsel, at (202) 728-8013.

#### Background & Discussion

On June 16, 2011, the SEC approved FINRA Rule 1230(b)(6), which establishes a registration category<sup>1</sup> and qualification examination requirement for certain operations personnel (Operations Professionals).<sup>2</sup> The rule requires registration of certain individuals (covered persons) who are engaged in, responsible for or supervising certain member firm operations functions (covered functions) to enhance the regulatory structure surrounding these areas. See [Regulatory Notice 11-33](#) for detailed information on the Operations Professional registration category, including who must register, the qualification examination requirement, exceptions to the qualification examination requirement, implementation and registration procedures and continuing education requirements for Operations Professionals.

#### September 2011

##### Notice Type

- ▶ Guidance

##### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Operations
- ▶ Registration
- ▶ Senior Management

##### Key Topics

- ▶ Operations Professionals
- ▶ Qualification Examinations
- ▶ Registration

##### Referenced Rules & Notices

- ▶ FINRA Rule 1230
- ▶ FINRA Rule 1250
- ▶ NASD Rule 1031
- ▶ NASD Rule 1070
- ▶ NASD Rule 1120
- ▶ Regulatory Notice 11-33

Subject to specified exceptions, FINRA Rule 1230(b)(6)(C) requires any person who must register as an Operations Professional to pass a new Operations Professional qualification examination (Series 99) before the registration may become effective.<sup>3</sup> The Series 99 examination program has been developed to provide reasonable assurance that covered persons understand their professional responsibilities, including key regulatory and control themes, as well as the importance of identifying and escalating red flags that may harm a firm, a customer, the integrity of the marketplace or the public.<sup>4</sup> The Series 99 examination will test applicants on general securities industry knowledge and its associated regulations and rules. The examination fee for the Series 99 examination is \$125.<sup>5</sup>

As detailed in [Regulatory Notice 11-33](#), FINRA Rule 1230(b)(6)(D)(i) sets forth an exception to the Series 99 qualification examination requirement for persons who currently hold certain registrations (each an eligible registration) or have held one during the two years immediately prior to registering as an Operations Professional. The exception also applies to persons who do not hold an eligible registration, but prefer an alternative to taking the Series 99 examination. Such persons may register in an eligible registration category (subject to passing the corresponding qualification examination or obtaining a waiver) and use the registration to qualify for Operations Professional registration.<sup>6</sup>

### Exam Content

The Series 99 examination consists of 100 multiple-choice questions.<sup>7</sup> Candidates will be allowed 150 minutes (two and one-half hours) to complete the examination. Candidates will receive an informational breakdown of their performance on each section of the examination, along with their overall score and pass/fail status at the completion of the testing session.

FINRA has published a [content outline](#) for the Series 99 examination. The content outline provides a comprehensive guide to the areas covered on the examination and is intended to familiarize candidates with the range of subjects covered by the examination. Firms may wish to use the content outline to structure or prepare training material, develop lecture notes and seminar programs, and as a training aide for the candidates. The content outline describes the following three major content areas comprising the examination: (1) Basic Knowledge Associated with the Securities Industry; (2) Basic Knowledge Associated with Broker-Dealer Operations; and (3) Professional Conduct and Ethical Considerations. The allocation of test questions for each major content area is listed in the table below.

#### Number of Questions by Major Content Area

Section	Major Content Area	Number of Questions
1	Basic Knowledge Associated with the Securities Industry	32
2	Basic Knowledge Associated with Broker-Dealer Operations	48
3	Professional Conduct and Ethical Considerations	20
	<b>Total</b>	<b>100</b>

FINRA will update, as needed, the content outline and questions used in the examination to reflect the most current interpretations of the relevant rules and regulations, changes in practices and/or the introduction of new products. Questions on new rules will be added to the pool of questions for this examination within a reasonable time period of the effective dates of those rules. Questions on rescinded rules will be deleted promptly from the pool of questions. Candidates will be asked rules-based questions pertaining only to rules that are effective at the time they take the exam.

The Series 99 examination is administered as a closed-book exam. The proctor will provide erasable note boards, dry erase markers and a basic electronic calculator to candidates. These items must be returned to the proctor at the end of the session.

The Series 99 examination will be administered at test centers operated by Pearson VUE and Prometric professional testing center networks. Appointments to take the examination may be scheduled through either network:

- ▶ **Pearson Professional Centers:** contact Pearson VUE Registration Center at (866) 396-6273 (toll free) or (952) 681-3873 (toll number) or go to [www.pearsonvue.com/finra](http://www.pearsonvue.com/finra).
- ▶ **Prometric Testing Centers:** contact Prometric's National Call Center at (800) 578-6273 (toll free) or go to [www.prometric.com/finra](http://www.prometric.com/finra) for Web-based scheduling.

### Initial 60-Day Rollout Period for the Series 99 Examination

Candidates will be able to schedule and take the Series 99 examination beginning on October 17, 2011. During the initial 60-day rollout period (October 17 through December 16, 2011), FINRA will assess the effectiveness of the new examination, in part, by evaluating how candidates perform. FINRA will not immediately release the results for any examination taken during this initial 60-day rollout period. Instead, FINRA will notify candidates who take the examination during this initial rollout period and their firms of test results (including an informational breakdown of their performance on each section of the examination, along with their overall score and pass/fail status) on or shortly after December 16, 2011, at which time the test results will be posted to the Central Registration Depository (CRD®).<sup>8</sup> Candidates who fail the Series 99 examination during the initial 60-day rollout period will be provided an opportunity to retake the examination at no additional cost once the test results are posted.

## Endnotes

1. The Web CRD registration position code for the Operations Professional registration category is "OS."
2. See Securities Exchange Act Release No. 64687 (June 16, 2011), 76 FR 36586 (June 22, 2011) (Order Approving Proposed Rule Change; File No. SR-FINRA-2011-013). In addition, effective October 17, 2011, NASD Rule 1120 (Continuing Education Requirements) has been adopted as FINRA Rule 1250 (Continuing Education Requirements) in the Consolidated FINRA Rulebook with certain changes, including a requirement that Operations Professionals be subject to both Regulatory Element and Firm Element Programs.
3. FINRA notes that NASD Rule 1070 (Qualification Examinations and Waiver of Requirements), as well as other applicable provisions regarding registration and qualification set forth in FINRA's rulebook, such as NASD Rule 1031(c) regarding requirements for examination on lapse of registration, applies to the Operations Professional qualification examination and registration category.
4. See Securities Exchange Act Release No. 65222 (August 30, 2011), 76 FR 55443 (September 7, 2011) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Adopt the Selection Specifications and Study Outline for the Operations Professional ("Series 99") Examination Program; File No. SR-FINRA-2011-041).
5. See Securities Exchange Act Release No. 65221 (August 30, 2011), 76 FR 55441 (September 7, 2011) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Fee for the Operations Professional Examination; File No. SR-FINRA-2011-042).
6. FINRA Rule 1230(b)(6)(D)(ii) provides that the staff may accept as an alternative to the Operations Professional qualification examination requirement any domestic or foreign qualification if it determines that acceptance of the alternative qualification is consistent with the purposes of the rule, the protection of investors and the public interest.
7. To ensure that new exam questions meet acceptable testing standards prior to use, each examination includes 10 additional, unidentified "pre-test" questions that do not contribute towards the candidate's score. The 10 pre-test questions are randomly distributed throughout the examination.
8. As noted above, candidates who take the examination after December 16, 2011, (*i.e.*, subsequent to the initial 60-day rollout period) will receive an informational breakdown of their performance on each section of the examination, along with their overall score and pass/fail status, at the completion of the testing session.

## Indications of Interest

### FINRA Requests Comment on Proposed Amendments to Rule 5210 Regarding Publication of Indications of Interest

Comment Period Expires: October 21, 2011

#### Executive Summary

FINRA requests comment on proposed amendments to FINRA Rule 5210 to require that member firms receive a customer order in a security before displaying a quotation or indication of interest (IOI) in a way that purports to represent that the quotation or IOI originated with a customer. Similarly, a firm could not continue to display a quotation or IOI as representing a customer order once the customer order was executed or cancelled.

The text of the proposed amendments is in Attachment A to this *Notice*.

Questions concerning this *Notice* should be directed to Brant K. Brown, Associate General Counsel, Office of General Counsel, at (202) 728-6927.

#### Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by October 21, 2011.

Member firms and other interested parties can submit their comments using the following methods:

- ▶ Emailing comments to [pubcom@finra.org](mailto:pubcom@finra.org); or
- ▶ Mailing comments in hard copy to:  
Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

### September 2011

#### Notice Type

- ▶ Request for Comment

#### Suggested Routing

- ▶ Compliance
- ▶ Institutional
- ▶ Legal
- ▶ Registered Representatives
- ▶ Senior Management
- ▶ Trading

#### Key Topics

- ▶ Indications of Interest

#### Referenced Rules & Notices

- ▶ FINRA Rule 2010
- ▶ FINRA Rule 2020
- ▶ FINRA Rule 5210
- ▶ NASD Rule 2210
- ▶ NTM 06-50
- ▶ Regulatory Notice 09-28

To help FINRA process and review comments more efficiently, persons should use only one method to comment on the proposal.

**Important Notes:** The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA Web site. Generally, FINRA will post comments on its site one week after the end of the comment period.<sup>1</sup>

Before becoming effective, a proposed rule change must be authorized for filing with the Securities and Exchange Commission (SEC) by the FINRA Board of Governors and then must be filed with the SEC pursuant to Section 19(b) of the Securities Exchange Act of 1934 (SEA).<sup>2</sup>

## Background & Discussion

Indications of interest, or IOIs, are non-firm expressions of trading interest that contain one or more of the following elements: security name, side, size, capacity and/or price. Firms have the ability to communicate or advertise proprietary or customer trading interest in the form of IOIs to the marketplace through their own systems or several service providers that disseminate the information to subscribers and/or the marketplace. For example, some service providers allow firms to publicize trading interest in a particular security relating to firm proprietary interest or interest that the firm represents on an agency basis. A firm may choose to disseminate IOIs to inform other market participants that it seeks to, or represents customer trading interest that seeks to, interact with other order flow in the security.

One attribute that is often associated with an IOI is whether the IOI originated with a customer (what is commonly referred to as a “natural” IOI), rather than with the firm. Although the meaning of the term “natural” may differ across firms and service providers, a “natural” IOI is generally considered to refer either to customer interest a firm represents on an agency basis or to proprietary interest that was established to facilitate a customer order or as part of an execution of a customer order on a riskless principal basis.

In May 2009, FINRA published [Regulatory Notice 09-28](#) reminding firms that, to the extent that they disseminate or use services to communicate indications of interest, IOIs must be truthful, accurate and not misleading.<sup>3</sup> The *Notice* stated that FINRA could view as untruthful, inaccurate or misleading a firm’s representation of firm proprietary interest as a “natural” IOI without making disclosure to its customers of the circumstances in which such representations are made, or that is inconsistent with disclosures made by a firm with respect to the content of its IOIs, or alternatively through the service provider’s system in a manner contrary to the service provider’s guidelines. FINRA also could view as untruthful, inaccurate or misleading a firm’s continuing dissemination of a “natural” IOI to the marketplace when the firm no longer represents any such interest on behalf of a customer. The *Notice* also stated that the communication of untruthful, inaccurate or

misleading information relating to IOIs would be considered conduct inconsistent with high standards of commercial honor and just and equitable principles of trade under FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade) and, depending on the nature and content of the communication, could also violate FINRA Rule 5210 (Publication of Transactions and Quotations), FINRA Rule 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices), NASD Rule 2210 (Communications with the Public) and the anti-fraud provisions of the federal securities laws.

## Request for Comment

Notwithstanding the publication of [Regulatory Notice 09-28](#), FINRA remains concerned that firms are disseminating misleading information regarding IOIs, including not accurately labeling them to reflect their origination. Consequently, FINRA is proposing to amend Rule 5210 in several ways.

First, FINRA is proposing new Supplementary Material to FINRA Rule 5210 that would require that a firm have received a customer order in a security before displaying a quotation or IOI in any way that purports to represent that the quotation or IOI originated with a customer (*e.g.*, by labeling an IOI as “natural”). Thus, firms would not be permitted to label an IOI or quotation in any way that indicates the IOI or quotation represented customer interest until the firm had received a customer order and had recorded the order on its books and records by, for example, creating an order ticket or entering the terms of the order into the firm’s order management system. Importantly, the proposed amendment does not prohibit firms from displaying IOIs or quotations when they have not received a customer order; it merely prohibits the firm from labeling any such IOI or quotation in a way that indicates that the interest arose with a customer. Similarly, a firm could not continue to display such a quotation or IOI as representing a customer order once the customer order was executed or cancelled.

FINRA is also proposing several amendments to Rule 5210 and the existing Supplementary Material to modernize the language in the rule and to align the rule text with the Supplementary Material. Among other things, these amendments would clarify that the prohibitions in Rule 5210 extend to IOIs.

Although FINRA welcomes comments on any aspect of the proposed amendments discussed in this *Notice*, FINRA specifically encourages comments on the following:

- ▶ Should FINRA define the term “indication of interest”? Does the application of the new labeling requirements to both IOIs and quotations adequately cover the situations in which concerns regarding inaccurate labeling arise?
- ▶ Is the approach taken in the proposed amendments appropriate or should FINRA define terms such as “natural” in the rule? Would specific definitions provide firms with clarity or would they create too narrow an application? Would definitions need regular updating to stay current with industry practice?

- ▶ Is the requirement that a firm has received a customer order before labeling an IOI or quotation in a manner that indicates the interest originated with a customer too limiting? Are there instances in which a customer would not want to place an order with a firm, but would want the firm to label an IOI in that manner? Is there an alternative standard that could achieve the same regulatory purpose? If so, what should that standard be?
- ▶ Some buy-side firms have stated that they prefer not to trade with “non-naturals” because “non-naturals” compete with them after the execution. For example, a buy-side firm selling part of a large block to a counterparty may be concerned that the counterparty might create downward pressure on the stock either if it were to sell the position, or if it already sold shares in anticipation of buying from the buy-side firm. Conversely, when trading with a “natural,” the buy-side firm’s selling pressure is potentially offset by the buying interest of the “natural” counterparty. Are these valid concerns by the buy side? Is it too restrictive to assume that “natural” interest can only come from customer orders?

The comment period expires on October 21, 2011.

## Endnotes

1. FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. See [NTM 03-73](#) (November 2003) (NASD Announces Online Availability of Comments) for more information.
2. See SEA Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the *Federal Register*. Certain limited types of proposed rule changes, however, take effect upon filing with the SEC. See SEA Section 19(b)(3) and SEA Rule 19b-4.
3. The *Notice* also reminded firms that directly disseminate or use services to disseminate IOIs that they must establish, maintain and enforce written supervisory procedures and supervisory systems that are reasonably designed to ensure, among other things, that the information disseminated by or on behalf of the member or its associated persons is truthful, accurate and not misleading. In addition, advertising a firm’s trading activity or interest in contexts other than indications of interest is also subject to FINRA rules and the anti-fraud provisions of the federal securities laws. See [NTM 06-50](#) (September 2006).

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## ATTACHMENT A

Below is the text of the proposed amendments to Rule 5210. Additional language is underlined; deletions are in brackets.

### **5210. Publication of Transaction[s] Reports, [and] Quotations, and Indications of Interest**

No member shall publish or circulate, or cause to be published or circulated; [, any notice, circular, advertisement, newspaper article, investment service, or communication of any kind which purports to]

(a) any report of any securities transaction as a purchase or sale of [any] such security unless [such] the member believes that such transaction was a bona fide purchase or sale of such security; [or which purports to]

(b) any quotation [quote the bid price or asked price] for any security, unless [such] the member believes that such quotation represents a bona fide bid for, or offer of, such security; or

(c) any indication of interest for any security, unless the member believes that such indication of interest represents a bona fide interest in purchasing or selling such security.

• • • Supplementary Material: -----

### **.01 Manipulative and Deceptive Transaction Reports, Quotations, and Indications of Interest.**

(a) It shall be deemed inconsistent with Rules 2010 (Standards of Commercial Honor and Principles of Trade), 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices) and 5210 (Publication of Transactions and Quotations) for a member to publish or circulate or cause to be published or circulated, by any means whatsoever, any report of any securities transaction or of any purchase or sale of any security unless such member knows or has reason to believe that such transaction was a bona fide transaction, purchase, or sale.

(b) [Similarly, i]It shall be deemed inconsistent with Rules 2010, 2020, and 5210 for a member, for itself or for any other person, to publish or circulate or to cause to be published or circulated, by any means whatsoever, any quotation for any security without having reasonable cause to believe that such quotation is a bona fide quotation, is not fictitious, and is not published or circulated or caused to be published or circulated for any fraudulent, deceptive, or manipulative purpose.

[For the purposes of this Rule, the term “quotation” shall include any bid or offer or any formula, such as “bid wanted” or “offer wanted,” designed to induce any person to make or submit any bid or offer.]

(c) It shall be deemed inconsistent with Rules 2010, 2020, and 5210 for a member, for itself or for any other person, to publish or circulate or to cause to be published or circulated, by any means whatsoever, any indication of interest for any security without having reasonable cause to believe that such indication of interest represents a bona fide interest in purchasing or selling the security, is not fictitious, and is not published or circulated or caused to be published or circulated for any fraudulent, deceptive, or manipulative purpose.

(d) With respect to any quotation or indication of interest that purports to represent that the interest the member is displaying originated with a customer, the member must have received a customer order in the security before displaying such quotation or indication of interest. Similarly, the member must withdraw the quotation or indication of interest if the customer order represented by such quotation or indication of interest is executed or cancelled.

## Customer Account Statements

### FINRA Requests Comment on Proposed Amendments to NASD Rule 2340 to Address Values of Unlisted Direct Participation Programs and Real Estate Investment Trusts in Customer Account Statements

Comment Period Expires: November 12, 2011

#### Executive Summary

FINRA is proposing amendments to NASD Rule 2340 (Customer Account Statements) to address how firms report the per share estimated values of unlisted Direct Participation Programs (DPPs) and unlisted Real Estate Investment Trusts (REITs) on customer account statements.<sup>1</sup> The amendments would limit the time period that the offering price may be used as the basis for a per share estimated value to the period provided under Rule 415(a)(5) of the Securities Act of 1933 (Initial Offering Period). The amendments also would require firms to deduct organization and offering expenses from per share estimated values during the Initial Offering Period. The amendments would prohibit a firm from using a per share estimated value, from any source, if it “knows or has reason to know the value is unreliable,” based upon publicly available information or nonpublic information that has come to the firm’s attention. Finally, the amendments would allow a firm to omit a per share estimated value on a customer account statement if the most recent annual report of the DPP or REIT does not contain a value that complies with the disclosure requirements of Rule 2340.<sup>2</sup>

Questions regarding this *Notice* may be directed to:

- ▶ Joseph E. Price, Senior Vice President, Corporate Financing/Advertising Regulation, at (240) 386-4623;
- ▶ Gary L. Goldsholle, Vice President and Associate General Counsel, Office of the General Counsel, at (202) 728-8104; or
- ▶ Paul Mathews, Director, Corporate Financing Department, at (240) 386-4639.

#### September 2011

##### Notice Type

- ▶ Request for Comment

##### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Senior Management

##### Key Topics

- ▶ Customer Account Statements
- ▶ Unlisted Direct Participation Programs (DPPs)
- ▶ Unlisted Real Estate Investment Trusts (REITs)

##### Referenced Rules & Notices

- ▶ FINRA Rule 2231
- ▶ FINRA Rule 2310
- ▶ NASD Rule 2340
- ▶ NASD Rule 5110
- ▶ Regulatory Notice 09-09
- ▶ Rule 415 under the Securities Act of 1933

## Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by November 12, 2011.

Member firms and other interested parties can submit their comments using the following methods:

- ▶ Emailing comments to *pubcom@finra.org*; or
- ▶ Mailing comments in hard copy to:  
Marcia E. Asquith  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

To help FINRA process and review comments more efficiently, persons should use only one method to comment on the proposal.

**Important Notes:** The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA website. Generally, FINRA will post comments on its site one week after the end of the comment period.<sup>3</sup>

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the FINRA Board of Governors, and then must be approved by the SEC, following publication for public comment in the *Federal Register*.<sup>4</sup>

## Background

NASD Rule 2340 generally requires each general securities member firm to send account statements to customers at least quarterly. The account statements must include a description of any securities positions, money balances and account activity since the firm issued the prior account statement. A firm that does not carry customer accounts and does not hold customer funds or securities is not a general securities member firm and is not subject to the provisions of Rule 2340.

NASD Rule 2340(c) contains specific provisions addressing the estimated values of DPPs and REITs on customer account statements.<sup>5</sup> The rule generally requires that a general securities member firm include an estimated value for a DPP or REIT security held in a customer's account. The rule states that the per share estimated value included on a customer account statement may be obtained from the annual report, an independent valuation service or any other source. The rule requires that firms develop a per share estimated value on a

customer account statement from data that is not more than 18 months old.<sup>6</sup> The rule also requires a firm to remove or amend a per share estimated value if the firm can demonstrate that the value was inaccurate as of the date of valuation or is no longer accurate as a result of a material change in operations.

FINRA Rule 2310 (Direct Participation Programs) prohibits a firm from participating in a public offering of a DPP or REIT unless the general partner or sponsor represents that it will include a per share estimated value in each annual report.<sup>7</sup> The current industry practice is to use the value in the issuer's annual report as the per share estimated value on a customer account statement.

*Regulatory Notice 09-09* addressed the use of the offering price, or "par value," as the basis of the per share estimated value required under NASD Rule 2340. The *Notice* discussed the interplay between the use of the offering price from the annual report and the requirement that the per share estimated value on a customer account statement be developed from data that is not more than 18 months old. The *Notice* explained that 18 months after the conclusion of the offering, the per share estimated value must be derived from an appraisal of the issuer's assets and operations, and may not simply be a restatement of the aged offering price.

## Proposed Amendments<sup>8</sup>

### Presenting Per Share Estimated Value, Net of Organization and Offering Expenses

The estimated value of an illiquid security such as a DPP or REIT may be derived from several sources. An appraisal of the issuer's assets and operations will assist investors in understanding the value and relative performance of the DPP and REIT over time. However, in the earlier stages of an offering of a DPP or REIT, as it accumulates assets, the net offering price can be a suitable alternative, particularly since an appraisal would involve recently acquired assets and cash that is yet to be invested during the ramp-up period. Appraisals also may be expensive depending on factors such as the nature and geographic dispersal of assets. In consideration of these concerns, FINRA proposes to permit valuations based on the offering price during the Initial Offering Period when the program is acquiring assets and firms are selling shares at a stable value on a best-efforts basis. However, FINRA proposes to amend the rule to require that all per share estimated values, including those that are based on the offering price, reflect a deduction of all organization and offering expenses (net value).<sup>9</sup>

Under Rule 2310(a)(12), organization and offering expenses consist of expenses incurred in connection with registration and distribution, including all forms of compensation paid to broker-dealers and affiliates in connection with the offering. Rule 2310 generally limits organization and offering expenses to 15 percent of the gross proceeds of an offering.

These expenses have three components: (1) issuer expenses that are reimbursed or paid for with offering proceeds, (2) underwriting compensation, and (3) due diligence expenses.

While any value of an illiquid security is an estimate, netting out the offering expenses is likely to be a closer approximation to the intrinsic value, particularly since the up-front fees and expenses reduce the amount of the investable capital during the ramp-up period when the assets are acquired by the DPP or REIT.<sup>10</sup> Requiring net values on customer account statements during the Initial Offering Period will provide greater transparency to investors about the fees and expenses, which would benefit investors.<sup>11</sup>

### Close of Initial Offering Period and Appraised Values

Rule 415(a)(5) provides that certain types of registered securities, including DPPs and REITs, may be offered and sold if no more than three years have elapsed since the initial effective date of the registration statement. Under Rule 415(a)(6), the Securities and Exchange Commission may make another registration statement for a DPP or REIT effective for a second three-year offering period. If a new registration statement is filed, Rule 415(a)(5) (A) permits securities covered by the prior registration statement to continue to be offered and sold until the earlier of the effective date of the new registration statement or 180 days after the third anniversary of the initial effective date. Under the proposed amendments, the three-year period under Rule 415(a)(5) and any “carryover period” under Rule 415(a)(5) (A) constitute the Initial Offering Period in NASD Rule 2340.

FINRA proposes to limit the period during which a per share estimated value based on the net offering price may be included on an account statement to the Initial Offering Period. Beyond the Initial Offering Period, the volatility in the value of the underlying assets of a DPP or REIT can cause the value to deviate substantially from the initial offering price, rendering the net offering price a poor estimate of the per share estimated value. After the Initial Offering Period, the basis for a per share estimated value included on a customer account statement must be based on an appraisal of a DPP or REIT’s assets, liabilities and operations.

The proposed amendments eliminate the provision in NASD Rule 2340(c)(2) that requires firms to develop a per share estimated value from data that is no more than 18 months old.

Instead, the proposed amendments require the data that serves as the basis for a per share estimated value to be no less current than the data in the most recent annual report. If a per share estimated value is available that is more recent than the value in the annual report, member firms can disclose that value if it meets the requirements of Rule 2340.<sup>12</sup>

## Reliability of Estimated Values

Rule 2340 currently requires a member firm to remove or amend a per share estimated value if the firm can demonstrate that the value was inaccurate as of the date of valuation or is no longer accurate as a result of a material change in operations. The proposed amendments adjust this requirement to prohibit a firm from using a per share estimated value, from any source, if it “knows or has reason to know the value is unreliable,” based upon publicly available information or nonpublic information that has come to the firm’s attention.

The proposed amendments also allow a firm to omit the per share estimated value if the most recent annual report of the DPP or REIT does not contain a value that complies with the disclosure requirements of the rule. In the alternative, a firm could decide to provide a reliable value from a source other than the annual report that meets the rule’s requirements. The amendments would require, however, that if a per share estimated value does not appear in or has been removed from a customer account statement, the firm must disclose the reason the value does not appear or has been removed.

## Endnotes

1. Unlisted DPPs and unlisted REITs do not trade on a national securities exchange. DPPs are defined in FINRA Rule 2310 and offer investors an equity interest in an entity such as a limited partnership that provides flow-through tax consequences and distributes income generated from underlying assets. REITs are defined in Section 856 of the Internal Revenue Code and are pass-through entities that offer investors an equity interest in a pool of real estate assets, including land, buildings, shopping centers, hotels and office properties. The definitions of DPP and REIT in NASD Rule 2340(d)(3) and (4) exclude securities listed on a national securities exchange as well as securities that are in a depository and settle regular way. The definition of DPP also excludes any program registered as a commodity pool.
2. NASD Rule 2340 only applies to customer account statements, as defined by that rule. Rule 2340, and as proposed to be amended, would not apply to annual statements of the fair market value of assets provided by retirement account trustees and custodians under Internal Revenue Service Regulations, including Section 1.408-2(e)(5)(ii)(E).
3. FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. See *NTM 03-73* (November 2003) (NASD Announces Online Availability of Comments) for more information.

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4. See SEA Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the *Federal Register*. Certain limited types of proposed rule changes, however, take effect upon filing with the SEC. See SEA Section 19(b)(3) and SEA Rule 19b-4.
5. NASD Rule 2340 applies to DPPs and REITs regardless of whether they are listed or itemized “above the line” or “below the line.” The term “below the line” means that securities and other assets are reported on the account statement, but are not in the possession of the member. New platforms that provide processing for alternative investments may result in DPPs and REITs being reported more frequently above the line because the securities are in the possession of member firms.
6. NASD Rule 2340(c) also requires that account statements provide: (1) a brief description of the estimated value, its source and the method by which it was developed; and (2) disclosure that the investment program securities are generally illiquid securities and the estimated value may not be realized when investors seek to sell the security. Additional disclosure are required if the account statement does not provide an estimated value.
7. Section 13(a) of the Securities Exchange Act requires annual reports to be distributed to investors.
8. As part of the rulebook consolidation process, FINRA has proposed new FINRA Rule 2231 to replace NASD Rule 2340. See SR-FINRA-2009-028. The amendments discussed herein would be made to NASD Rule 2340 or new FINRA Rule 2231, depending upon the timing of SEC approval.
9. Some REITs have begun to calculate a daily net asset value (NAV). The selling price per share is based on the daily NAV calculation and typically includes a selling commission. Under the proposal, the net estimated value required on customer account statements for such programs would be the NAV and could not include any commissions, nor any other organization or offering expense associated with the offering.
10. If any organization and offering expenses are to be deducted from portfolio assets or income, then under the proposal the net estimated value would have to reflect those deductions that will be taken during the Initial Offering Period, in addition to the deduction for organization and offering expenses paid out of proceeds from the offering.
11. *Regulatory Notice 09-09* reminded firms of their obligation under the suitability rule to determine the amount of dividend distributions that represents a return of investors’ capital and whether that amount is changing. In addition, firms must consider whether there are impairments to the real estate investment program’s assets or other material events that would affect the distributions and whether disclosure regarding dividend distributions needs to be updated to reflect these events.
12. Firms would not be required to immediately update the per share estimated values shown in customer account statements when a new value appears in the annual report. However, firms must use reasonable efforts to address operational or technical requirements associated with updating per share estimated values, to ensure that the updating occurs as promptly as practicable. Firms that require more than one statement cycle to update the per share estimated values are likely to raise a presumption that the firm is not making reasonable efforts.

## Attachment A

Below is the text of the proposed amendments to Rule 2340.

### 2340. Customer Account Statements

#### (a) General

No change.

#### (b) Delivery Versus Payment/Receive Versus Payment (DVP/RVP) Accounts

No change.

#### (c) Unlisted DPP/REIT Securities

(1) A general securities member that holds a direct participation program (DPP) or real estate investment trust (REIT) security in a customer's account must provide a per share estimated value of such security on the account statement as provided below:

(A) The customer account statement must disclose:

(i) the source of the per share estimated value, which may be from the annual report, independent valuation service or any other source, and the manner in which the per share estimated value was calculated, and

(ii) that unlisted DPP or REIT securities are illiquid securities and that the per share estimated value may not be realized when the customer seeks to liquidate the security.

(B) During a period not to exceed the period provided under SEC Rule 415(a)(5) since the initial effective date of the first registration statement under which the DPP or REIT is offered and sold (Initial Offering Period), any per share estimated value based upon the offering price must reflect a deduction of the amount of organization and offering expenses, as defined by FINRA Rule 2310(a)(12).

(C) After the Initial Offering Period, only a per share estimated value calculated based on an appraisal of the assets, liabilities and operations of the DPP or REIT and derived from data no less current than the data in the most recent annual report may be disclosed.

(2) Notwithstanding the requirements in paragraph (1):

(A) A member must refrain from providing a per share estimated value, from any source, if it knows or has reason to know the value is unreliable, based upon publicly available information or nonpublic information that has come to the member's attention; and

(B) A member may refrain from providing a per share estimated value if the most recent annual report of a DPP or REIT does not contain a per share estimated value that complies with the requirements in paragraphs (1)(B) or (1)(C).

**(3)** For any member refraining from providing a per share estimated value as permitted in paragraph (2), the customer account statement must disclose that:

(i) unlisted DPP or REIT securities are illiquid;

(ii) the value of the security is different from its purchase and may be less than the purchase price

(iii) an estimated valuation of the security is unavailable; and

(iv) the reason the value does not appear in, or has been removed from, the account statement.

**(d) Definitions**

No change.

## Qualification Examinations

### FINRA Revises the Series 7, 17, 37 and 38 Examination Programs

Implementation Date: November 7, 2011

#### Executive Summary

FINRA periodically reviews the content of qualification examinations to determine whether revisions are necessary or appropriate in view of changes—including laws, rules and regulations—pertaining to the subject matter covered by the examinations.

Based on these reviews, FINRA has revised the following examination programs:

- ▶ General Securities Representative (Series 7);
- ▶ United Kingdom Securities Representative (Series 17);
- ▶ Canada Securities Representative (Series 37); and
- ▶ Canada Securities Representative (Series 38).<sup>1</sup>

The changes are reflected in the [content outlines](#) on FINRA's website and will appear in examinations starting on November 7, 2011.

Questions regarding this *Notice* should be directed to:

- ▶ Joe McDonald, Senior Director, Testing and Continuing Education Department, at (240) 386-5065; or
- ▶ Patricia Monterosso, Lead Qualifications Analyst, Testing and Continuing Education Department, at (646) 315-8753.

### September 2011

#### Notice Type

- ▶ Guidance

#### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Operations
- ▶ Registration
- ▶ Training

#### Key Topics

- ▶ Canada Securities Representative (Series 37)
- ▶ Canada Securities Representative (Series 38)
- ▶ General Securities Representative (Series 7)
- ▶ Municipal Securities Representative (Series 52)
- ▶ Qualification Examinations
- ▶ United Kingdom Securities Representative (Series 17)

#### Referenced Rules & Notices

- ▶ Incorporated NYSE Rule 10
- ▶ Incorporated NYSE Rules 345.10, 345.15(2) and 345.15(3)
- ▶ Incorporated NYSE Rule Interpretation 345.15/02
- ▶ Information Notice 3/12/08
- ▶ MSRB Rule G-3
- ▶ NASD Rules 1031(a) and (b)
- ▶ NASD Rule 1032
- ▶ NASD Rules 1041 and 1042
- ▶ NYSE Information Memoranda 91-09 and 96-06
- ▶ SEA Section 15A(g)(3)

## Background & Discussion

Section 15A(g)(3) of the Securities Exchange Act of 1934 authorizes FINRA to prescribe standards of training, experience and competence for persons associated with FINRA member firms. In accordance with that provision, FINRA has developed examinations that are designed to establish that persons associated with FINRA member firms have attained specified levels of competence and knowledge, consistent with applicable registration requirements under FINRA Rules.

NASD Rules and the rules incorporated from NYSE<sup>2</sup> require that a “representative,” as defined in the respective rules,<sup>3</sup> register and qualify as a General Securities Representative,<sup>4</sup> subject to certain exceptions. For those representatives who are not engaged in municipal securities activities, the NASD and NYSE Rules provide that registration and qualification as a United Kingdom Securities Representative or a Canada Securities Representative is equivalent to registration and qualification as a General Securities Representative.<sup>5</sup>

The Series 7 examination qualifies an individual to function as a General Securities Representative. The Series 17 examination qualifies an individual to function as a United Kingdom Securities Representative. Either the Series 37 examination or the Series 38 examination qualifies an individual to function as a Canada Securities Representative. Series 17, 37 and 38 candidates must also satisfy certain foreign prerequisite training and competence requirements.<sup>6</sup>

Committees of industry representatives, together with FINRA staff, recently reviewed the Series 7, 17, 37 and 38 examination programs. As a result of these reviews, FINRA has revised the content outlines to reflect changes to the laws, rules and regulations covered by the examinations. Among other revisions, FINRA has revised the outlines to reflect the adoption of rules in the consolidated FINRA rulebook.

FINRA also has revised the outlines to better reflect the functions and associated tasks performed by General Securities Representatives, United Kingdom Securities Representatives and Canada Securities Representatives, and to better reflect the relationship between the different components of the outlines.

FINRA has divided the content outlines into five major job functions denoted F1 through F5:

- F1: Seeks Business for the Broker-Dealer through Customers and Potential Customers;
- F2: Evaluates Customers' Other Security Holdings, Financial Situation and Needs, Financial Status, Tax Status, and Investment Objectives;
- F3: Opens Accounts, Transfers Assets, and Maintains Appropriate Account Records;
- F4: Provides Customers with Information on Investments and Makes Suitable Recommendations; and
- F5: Obtains and Verifies Customer's Purchase and Sales Instructions, Enters Orders, and Follows Up.

Additionally, each job function includes certain tasks describing activities associated with performing that function. Each of the revised outlines also includes a knowledge section describing the underlying knowledge required to perform the major job functions and associated tasks, and a rule section listing the laws, rules and regulations related to the job functions, associated tasks and knowledge statements. There are cross-references within each section to the other applicable sections.

As described in greater detail below, the number of questions associated with each of the five functions, F1 through F5, differs depending on the examination. FINRA has made other revisions to the examinations, which also are described below.

Lastly, in conjunction with the changes to the content outlines, FINRA has made changes to the weighting of questions on content outline topics and to the question banks for these examinations.

## Series 7

The number of questions associated with each of the five functions performed by a General Securities Representative (Series 7) are as follows:

- F1: 68 questions;
- F2: 27 questions;
- F3: 27 questions;
- F4: 70 questions; and
- F5: 58 questions.

The number of questions on the Series 7 examination remains at 250 multiple-choice questions,<sup>7</sup> and candidates continue to have six hours to complete the examination. Currently, a “scaled score” of 70 percent is required to pass the Series 7 examination,<sup>8</sup> while a scaled score of 72 percent will be required to pass the revised examination.

## Municipal Securities Activities

Pursuant to current Municipal Securities Rulemaking Board (MSRB) Rule G-3, either the Municipal Securities Representative (Series 52) examination or the Series 7 examination qualifies an individual to function as a Municipal Securities Representative. In connection with the periodic review of examination content mentioned above, FINRA has revised the Series 7 examination to reduce the emphasis on municipal securities activities. FINRA notes that the MSRB has filed with the SEC a proposed rule change to amend MSRB Rule G-3 to provide, among other things, that, with regard to municipal securities activities, an individual qualifying as a Municipal Securities Representative by passing the Series 7 may engage only in municipal securities sales to, and purchases from, customers.<sup>9</sup>

### Series 17

The number of questions associated with each of the five functions performed by a United Kingdom Securities Representative (Series 17) are as follows:

- F1: 20 questions;
- F2: 15 questions;
- F3: 25 questions;
- F4: 20 questions; and
- F5: 20 questions.

The number of questions on the Series 17 examination remains at 100 multiple-choice questions. However, candidates will have 150 minutes (2.5 hours) to complete the examination, whereas today they have two hours to complete the examination. Also, currently, a score of 70 percent is required to pass the Series 17 examination, while a score of 72 percent will be required to pass the revised examination.

### Series 37

The number of questions associated with each of the five functions performed by a Canada Securities Representative (Series 37) are as follows:

- F1: 22 questions;
- F2: 12 questions;
- F3: 18 questions;
- F4: 16 questions; and
- F5: 22 questions.

The number of questions on the Series 37 examination remains at 90 multiple-choice questions, and candidates continue to have 150 minutes (2.5 hours) to complete the examination. Currently, a score of 70 percent is required to pass the Series 37 examination. A score of 72 percent will be required to pass the revised examination.

### Series 38

The number of questions associated with each of the five functions performed by a Canada Securities Representative (Series 38) are as follows:

- F1: 7 questions;
- F2: 7 questions;
- F3: 12 questions;
- F4: 10 questions; and
- F5: 9 questions.

The number of questions on the Series 38 examination remains at 45 multiple-choice questions, and candidates continue to have 75 minutes to complete the examination. Currently, a score of 70 percent is required to pass the Series 38 examination. A score of 72 percent will be required to pass the revised examination.

## Content Outlines

The revised Series 7, 17, 37 and 38 content outlines are available on FINRA's [website](#).

## Endontes

1. See Securities Exchange Act Release No. 65358 (September 20, 2011), 76 FR 59751 (September 27, 2011) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change; File No. SR-FINRA-2011-045); Securities Exchange Act Release No. 65376 (September 21, 2011), 76 FR 59759 (September 27, 2011) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change; File No. SR-FINRA-2011-046); Securities Exchange Act Release No. 65374 (September 21, 2011), 76 FR 59761 (September 27, 2011) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change; File No. SR-FINRA-2011-047); and Securities Exchange Act Release No. 65375 (September 21, 2011), 76 FR 59757 (September 27, 2011) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change; File No. SR-FINRA-2011-048). These rule filings were filed with the SEC for immediate effectiveness on September 7, 2011.
2. The current FINRA rulebook consists of (1) FINRA Rules; (2) NASD Rules; and (3) rules incorporated from NYSE (Incorporated NYSE Rules) (together, the NASD Rules and Incorporated NYSE Rules are referred to as the Transitional Rulebook). While the NASD Rules generally apply to all FINRA members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (Dual Members). The FINRA Rules apply to all FINRA members, unless such rules have a more limited application by their terms. For more information about the rulebook consolidation process, see [Information Notice, March 12, 2008](#) (Rulebook Consolidation Process). For convenience, the Incorporated NYSE Rules are referred to as the NYSE Rules.
3. See NASD Rule 1031(b) and NYSE Rule 10.
4. See NASD Rules 1031(a) and 1032(a)(1); NYSE Rules 345.10 and 345.15(2); and NYSE Rule Interpretation 345.15/02.
5. See NASD Rules 1032(a)(2)(B) and (a)(2)(C) and NYSE *Information Memoranda* 91-09 (March 1991) and 96-06 (March 1996).

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6. Series 17 candidates must satisfy certain prerequisite training and competence requirements of the United Kingdom's Financial Services Authority (FSA) and be registered and in good standing with the FSA. Series 37 and Series 38 candidates must satisfy certain prerequisite training and competence requirements of the Canadian regulators and be registered and in good standing with the appropriate Canadian regulator. Series 38 candidates must also complete either: (1) the Options Licensing Course and the Derivatives Fundamental Course; or (2) the Canadian Options Course. Since Series 38 candidates are already subject to a Canadian options prerequisite, the Series 38 examination does not include test questions that assess knowledge of options. More information regarding the prerequisite requirements for the [Series 17](#) and [Series 37 and 38](#) examinations is available on FINRA's website.
7. Consistent with FINRA's practice of including "pre-test" questions on certain qualification examinations, which is designed to ensure that new examination questions meet acceptable testing standards prior to use for scoring purposes, each Series 7 examination includes 10 additional, unidentified pre-test questions that do not contribute towards a candidate's score. Therefore, the examination actually consists of 260 questions, 250 of which are scored. The 10 pre-test questions are randomly distributed throughout the examination.
8. The Series 7 examination questions for a given examination are randomly selected from the Series 7 question bank, which may result in slight variations in the difficulty of the examinations. The use of a scaled score accounts for these slight variations and is intended to maintain comparable passing standards across candidates.
9. See Securities Exchange Act Release No. 65393 (September 26, 2011) (Notice of Filing of Proposed Rule Change; File No. SR-MSRB-2011-17).

# Election Notice

## FINRA Small Firm Advisory Board Election

### Executive Summary

The purpose of this Notice is to inform FINRA Small Firm members<sup>1</sup> of the upcoming Small Firm Advisory Board (SFAB) election. Two seats on the SFAB are up for election: the Midwest and South Region seats.

The SFAB provides guidance to FINRA staff, particularly regarding the potential impact of proposed regulatory initiatives on FINRA's small firms, and meets five times a year primarily in Washington, DC, prior to each FINRA Board of Governors meeting. SFAB members are expected to attend SFAB meetings in person, and may be requested to attend certain regional, district and other FINRA meetings. Potential candidates should ensure that their other commitments will allow for their in-person attendance at all SFAB meetings.

Any eligible candidate wishing to have their name added to the ballot must submit the relevant information via the candidate profile form to the Corporate Secretary of FINRA no later than Friday, October 7, 2011. The candidate profile form is available online at [www.finra.org/Notices/SFABElection/090711](http://www.finra.org/Notices/SFABElection/090711) and as an attachment to this Notice.

On or about Wednesday, October 19, 2011, FINRA will mail the official *Election Notice* and ballots to the executive representatives of small firms in the Midwest and South Regions to elect their regional representatives on the SFAB. Voting will conclude in November 2011 and new members will take office in January 2012.

Questions regarding this *Election Notice* may be directed to:

- ▶ Marcia E. Asquith, Senior Vice President and Corporate Secretary, FINRA, at (202) 728-8949;
- ▶ T. Grant Callery, Executive Vice President and General Counsel (Corporate), FINRA, at (202) 728-8285; or
- ▶ Chip Jones, Senior Vice President, Member Relations, FINRA, at (240) 386-4797.

**September 7, 2011**

### Suggested Routing

- ▶ Executive Representatives
- ▶ Senior Management

## Composition of the FINRA Small Firm Advisory Board

The SFAB comprises 10 members, as follows:

- ▶ five regional members elected by small firms in the five FINRA regions (one from each region); and
- ▶ five at-large members appointed by FINRA.

Additionally, the FINRA Board's Small Firm Governors<sup>2</sup> serve as ex-officio members of the SFAB.

The five regional members represent the following geographic regions:

- ▶ **Midwest Region:** Illinois, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota and Wisconsin (Districts 4 and 8)
- ▶ **New York Region:** New York (the counties of Nassau and Suffolk, and the five boroughs of New York City) (District 10)
- ▶ **North Region:** Connecticut, Delaware, the District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York (except for the counties of Nassau and Suffolk, and the five boroughs of New York City), Pennsylvania, Rhode Island, Vermont, Virginia and West Virginia (Districts 9 and 11)
- ▶ **South Region:** Alabama, Arkansas, Florida, Georgia, Louisiana, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, the Canal Zone, Puerto Rico and the Virgin Islands (Districts 5, 6 and 7)
- ▶ **West Region:** Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, Wyoming and the former U.S. Trust Territories (Districts 1, 2 and 3)

As mentioned above, two seats on the SFAB are up for election: the Midwest and South Region seats.

## Candidate Eligibility

Any senior member of a Small Firm whose primary place of business and whose firm has its main office (as indicated in FINRA records) in the Midwest or South region is eligible to have his or her name placed on the SFAB ballot for that region. Senior members of firms include owners, chief executive officers, presidents, chief compliance officers, chief operating officers, the firm's FINOP or individuals of comparable status. Eligible individuals must complete the attached SFAB candidate profile form<sup>3</sup> and submit it, through their firm's Executive Representative, to FINRA's Corporate Secretary. There may be only one candidate per firm on each ballot.

SFAB candidate profiles for the upcoming election must be received by the Corporate Secretary of FINRA no later than Friday, October 10, 2011.

FINRA's Corporate Secretary will confirm the firm's status as a Small Firm and the candidate's eligibility, and include certified candidates on the relevant region's ballot. Individuals have a continuing obligation to satisfy the firm-size requirement on the date the candidacy is certified by the Corporate Secretary and the date the ballots are mailed. Individuals who fail to meet this requirement will be disqualified from election.

SFAB members must also continue to meet their qualifications for election at all times during their terms of office.

## Voting Eligibility

FINRA small firms are eligible to vote for candidates running for the SFAB seat representing the region corresponding to the district to which they are assigned in the Central Registration Depository. Only those firms eligible to vote for the Midwest or South Region seat will receive ballots. The size of each firm and the location of each firm's main office will be verified on the day the ballots are mailed.

Firms may vote for only one candidate listed on the ballot.

## Terms of SFAB Members

The successful candidate will be the individual who receives the most votes and will be elected to serve a three-year term.

The term of an SFAB member shall terminate immediately upon a determination by the SFAB, by a majority vote of the remaining members, that the member no longer satisfies the eligibility criteria. Additionally, the FINRA Board may remove from the SFAB, a member who is unable or fails to discharge the member's duties or violates SFAB policies.

Once an individual has completed a full three-year elected term on the SFAB, he or she is ineligible to run for reelection to the SFAB for another three years.

## Endnotes

1. A Small Firm is defined as a firm that employs at least one and no more than 150 registered persons. See Article I (ww) of the FINRA By-Laws.
2. A Small Firm Governor is defined as a member of the FINRA Board elected by Small Firm members. In order to be eligible to serve, a Small Firm Governor must be registered with a member that is a Small Firm and must be an Industry Governor. See Article I (xx) of the FINRA By-Laws.
3. The SFAB candidate profile form is also available at [www.finra.org/Notices/SFABElection/090711](http://www.finra.org/Notices/SFABElection/090711).

# Attachment A

## Candidate Nomination and Profile Form—SFAB Election

Please complete all sections and email this document to [CorporateSecretary@finra.org](mailto:CorporateSecretary@finra.org). An electronic version of this form is also available at [www.finra.org/Notices/SFABElection/090711](http://www.finra.org/Notices/SFABElection/090711).

Name: \_\_\_\_\_ CRD#: \_\_\_\_\_

*(As you would like it to appear on official correspondence)*

### Current Registration

Firm Name: \_\_\_\_\_ Firm #: \_\_\_\_\_

FINRA District No.: \_\_\_\_\_ Number of Registered Reps. at Firm: \_\_\_\_\_

Title/Primary Responsibility: \_\_\_\_\_

### Address

Street Address: \_\_\_\_\_ Suite/Floor: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_

Email: \_\_\_\_\_

Phone: \_\_\_\_\_

### SFAB Seat Sought

**Midwest Region**

- ▶ Illinois, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota and Wisconsin (Districts 4 and 8) Eligibility (Check all that apply)

**South Region**

- ▶ Alabama, Arkansas, Florida, Georgia, Louisiana, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, the Canal Zone, Puerto Rico and the Virgin Islands (Districts 5, 6 and 7)

### Eligibility Checklist (must meet all three)

1. Senior member of a small firm;
  - ▶ Senior members include owners, chief executive officers, presidents, chief compliance officers, chief operating officers, the firm's FINOP, or individuals of comparable status.
2. Firm's main office is in the Midwest or South Region
  - ▶ Location of firm's main office: \_\_\_\_\_
3. Your primary place of business is in the same region as the firm's main office.



# Election Notice

## District Elections

### Nomination and Election Process to Fill FINRA District Committee Vacancies

#### Executive Summary

This *Notice* notifies member firms of the upcoming nomination and election process to fill forthcoming vacancies on FINRA District Committees. The election process has been modified by recent By-Law changes to adjust the size of the District Committees, elect new members based on firm size, and replace the District Nominating Committees with direct nomination and election.

All eligible candidates will be placed on the ballot if they submit a candidate nomination and profile form to the FINRA Corporate Secretary by Friday, October 7, 2011. The candidate profile form is available online at [www.finra.org/Notices/DistrictElection/090711](http://www.finra.org/Notices/DistrictElection/090711) and as an attachment to this *Notice*.

The seats open for election are included in Attachment A. A list of the current District Committee members is available at [www.finra.org/districtcommittees](http://www.finra.org/districtcommittees).

**Note:** This *Notice* was distributed electronically to the executive representative of each FINRA member firm and is posted on FINRA's website. Executive representatives should circulate this *Notice* to their firm's branch managers.

Questions concerning this *Election Notice* may be directed to

- ▶ Marcia Asquith, Senior Vice President and Corporate Secretary, at (202) 728-8949 or via email to [CorporateSecretary@finra.org](mailto:CorporateSecretary@finra.org).
- ▶ Chip Jones, Senior Vice President, Member Relations, at (240) 386-4797 or via email to [chip.jones@finra.org](mailto:chip.jones@finra.org).

**September 7, 2011**

#### Suggested Routing

- ▶ Branch Managers
- ▶ Executive Representatives
- ▶ Senior Management

## Background

The FINRA District Committees serve an important role in the self-regulatory process by, among other things:

- ▶ alerting FINRA to industry trends that could present regulatory concerns;
- ▶ consulting with FINRA on proposed policies and rule changes; and
- ▶ serving on disciplinary panels in accordance with FINRA rules.

Committee members must have the experience, ability and commitment to fulfill these responsibilities, including:

- ▶ understanding the issues facing the securities industry and possessing the ability to apply knowledge and expertise to these issues to develop solutions;
- ▶ educating firms in their district on the responsibilities of FINRA;
- ▶ attending regularly and participating in a collegial manner in District Committee meetings; and
- ▶ remaining objective and unbiased, regardless of the interest of their firm, in the performance of District Committee matters.

Committee members also must adhere to the following prohibitions and restrictions:

- ▶ being sensitive to conflicts, such as those that can arise from firm-related work and service on industry committees, or as an expert witness, hearing panelist or arbitrator, and refraining from participating in a particular matter when a conflict exists;
- ▶ refraining from using membership on the District Committee for commercial purposes, for qualifying as an expert or suggesting special access to FINRA; and
- ▶ keeping sensitive, non-public or proprietary information confidential.

## Changes to District Committee Composition

On May 4, 2011, the SEC approved amendments to FINRA Regulation's By-Laws to, among other things, adjust the size and composition of District Committees to align more closely with the industry representation on the FINRA Board of Governors and replace District Nominating Committees with a process of direct nomination and election based on firm size.<sup>1</sup>

## Vacancies

In this election, the District Committees for Districts 1, 2, 3, 4, 5, 6, 7, 8, 9 and 11 each have three seats to fill: one representing small firms, one representing mid-size firms and one representing large firms.<sup>2</sup>

District 10 has five seats to fill: two representing small firms, one representing mid-size firms, and two representing large firms. Firm size categories are:

- ▶ **Small firm**—a firm that employs at least one and no more than 150 registered persons.<sup>3</sup>
- ▶ **Mid-size firm**—a firm that employs at least 151 and no more than 499 registered persons;<sup>4</sup> and
- ▶ **Large firm**—a firm that employs 500 or more registered persons.<sup>5</sup>

## Terms of District Committee Members

The term for District Committee members is three years. There is no limit on the number of terms that may be served by a member of a District Committee, except that a District Committee member may not serve two full terms consecutively. Terms of District Committee members will terminate if they do not remain eligible for the seat for which they were elected. Terms of the individuals elected during this election will begin on January 1, 2012.

## Nomination Process and Eligibility

All candidates who submit their names and meet the qualifications set forth in Article VIII, Section 8.2 of the FINRA Regulation By-Laws (see below) will be included on their district's ballot. FINRA encourages current and former committee members to assist FINRA by soliciting candidates for committee service.

Individuals who seek a seat on the District Committee within their district must complete a candidate nomination and profile form and submit it to FINRA via email to [CorporateSecretary@finra.org](mailto:CorporateSecretary@finra.org) by October 7, 2011.

The candidate nomination and profile form is available online at [www.finra.org/notices/DistrictElection/090711](http://www.finra.org/notices/DistrictElection/090711) and as an attachment to this *Notice*.

Article VIII, Section 8.2 of the FINRA Regulation By-Laws requires for eligibility that District Committee members:

1. be associated with a FINRA member firm eligible to vote in the district for District Committee elections and registered in the capacity of a branch manager or principal or denoted as a corporate officer of the FINRA member;
2. work primarily from such FINRA member firm's principal office or a branch office that is located within the district where the member would serve on a District Committee; and
3. represent and be directly elected by the applicable classification of FINRA members based on the size of the firm with which he or she is associated: small, mid-size or large.

The names of all qualified individuals will be included on the ballot for the appropriate seat. Ballots will be mailed on or around October 19, 2011.

Additional information on District Committee election procedures may be found in [Article VIII of FINRA Regulation's By-Laws](#).

## Firm Contact Information

Firms are reminded to accurately maintain their executive representative's name and email address, as well as their firm's main postal address in the FINRA Contact System. This will ensure that important mailings, such as election information, are properly directed. A firm's failure to keep this information accurate may jeopardize the firm's ability to participate in elections.<sup>6</sup>

To update an executive representative name, mailing address and email address, firms may access the FINRA Contact System, via the Firm Gateway, at <https://firms.finra.org/fcs>. For assistance updating FCS, contact FINRA's Call Center at (301) 590-6500 or the Office of Corporate Secretary at (202) 728-8949.

## Endnotes

1. See Securities Exchange Act Release No. 64363 (April 28, 2011), 76 FR 25397.
2. The By-Law change adjusts the composition of the District Committees over a three-year transition period to align more closely with the industry representation by firm size on the Board of Governors. All District Committees except District 10 (New York) are adjusted from nine to seven members and District 10 is adjusted from 12 to 14 members. All currently serving District Committee members will serve out their original terms. Vacancies since the last election will not be filled because they entail partial terms that were not elected based on firm size.
3. See Article I (jj) of the FINRA Regulation By-Laws.
4. See Article I (aa) of the FINRA Regulation By-Laws.
5. See Article I (y) of the FINRA Regulation By-Laws.
6. Under NASD Rule 1160, firms must 1) update their contact information promptly, but in any event not later than 30 days following any change in such information, as well as 2) review and, if necessary, update the information within 17 business days after the end of each calendar year. Additionally, firms must comply with any FINRA request for such information promptly, but in any event not later than 15 days following the request, or such longer period agreed to by FINRA staff. See NASD Rule 1160 and [Regulatory Notice 07-42](#) (September 2007).

## Attachment A District Committee Positions to Be Elected

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### District 1

*Northern California (the counties of Monterey, San Benito, Fresno and Inyo, and the remainder of the state north or west of such counties), northern Nevada (the counties of Esmeralda and Nye), and the remainder of the state north or west of such counties) and Hawaii*

#### **District Committee for District 1**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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### District 2

*Southern California (that part of the state south or east of the counties of Monterey, San Benito, Fresno and Inyo), southern Nevada (that part of the state south or east of the counties of Esmeralda and Nye) and the former U.S. Trust Territories*

#### **District Committee for District 2**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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### District 3

*Arizona, Colorado, New Mexico, Utah and Wyoming  
Alaska, Idaho, Montana, Oregon and Washington*

#### **District Committee for District 3**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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### District 4

*Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota and South Dakota*

#### **District Committee for District 4**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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### District 5

*Alabama, Arkansas, Louisiana, Mississippi, Oklahoma and Tennessee*

#### **District Committee for District 5**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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## District 6

*Texas*

### **District Committee for District 6**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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## District 7

*Georgia, North Carolina and South Carolina  
Florida, Puerto Rico, Panama and the Virgin Islands*

### **District Committee for District 7**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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## District 8

*Illinois, Indiana, Kentucky, Michigan, Ohio and Wisconsin*

### **District Committee for District 8**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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## District 9

*New Jersey and New York (except for the counties of Nassau and Suffolk, and the five boroughs of New York City), Delaware, the District of Columbia, Maryland, Pennsylvania, Virginia and West Virginia*

### **District Committee for District 9**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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## District 10

*New York (the counties of Nassau and Suffolk, and the five boroughs of New York City)*

### **District Committee for District 10**

Committee members to be elected to terms expiring December 31, 2014: Two small firm representatives, one mid-size firm representative and two large firm representatives.

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## District 11

*Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island and Vermont*

### **District Committee for District 11**

Committee members to be elected to terms expiring December 31, 2014: One small firm representative, one mid-size firm representative and one large firm representative.

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## Attachment B Candidate Profile Form — District Committee Election

Please complete all sections and email this document to [CorporateSecretary@finra.org](mailto:CorporateSecretary@finra.org). An electronic version of this form is also available at [www.finra.org/Notices/DistrictElection/090711](http://www.finra.org/Notices/DistrictElection/090711).

Name: \_\_\_\_\_ Date: \_\_\_\_\_

*(As you would like it to appear on official correspondence)*

### Current Registration

Title/Primary Responsibility: \_\_\_\_\_

Firm CRD#: \_\_\_\_\_ Individual CRD#: \_\_\_\_\_

FINRA District No.: \_\_\_\_\_ Number of Registered Reps. at Firm: \_\_\_\_\_

### Address

Street Address: \_\_\_\_\_ Suite/Floor: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_

Email: \_\_\_\_\_

Phone: \_\_\_\_\_

### District Committee Seat Sought

- Small Firm (150 or fewer registered representatives)
- Mid-Size Firm (151 to 499 registered representatives)
- Large Firm (500 or more registered representatives)

### Eligibility (Check all that apply)

- Associated with FINRA member firm eligible to vote in the district for District Committee elections
- Work primarily from FINRA member firm's principal or branch office in the district of the District Committee sought
- Position

### Registered as

- branch manager
- principal

### OR

- Denoted as a corporate officer of the FINRA member firm.



# Trade Reporting Notice

## FINRA Reminds Firms of Their Trade Reporting Obligations Relating to Customer Sales of Low-Value OTC Equity Securities

### Executive Summary

FINRA is issuing this *Notice* to remind firms that sales of low-value OTC equity securities positions from customer accounts (often deemed by the customer and firm to be “worthless”) are subject to FINRA trade reporting rules and must be reported to FINRA for publication purposes.

Questions regarding this *Notice* may be directed to:

- ▶ Legal Section, Market Regulation, at (240) 386-5126; or
- ▶ Office of General Counsel, at (202) 728-8071.

### Background & Discussion

Some firms facilitate the sale of positions held by their customers in low-value OTC equity securities, as defined in FINRA Rule 6420, that they or their customer may deem to be “worthless.” The firm purchases the shares to remove the position from the customer’s account and to enable the customer to claim a capital loss for tax purposes.<sup>1</sup> The purchase price typically is nominal and set solely for purposes of liquidating the position. In some instances, it may not be a per share price, but may be sold, for example, for one penny or one dollar for the entire lot. Hence, these sales sometimes are referred to as “penny for the lot” transactions.

These sales are considered trades (*i.e.*, there is a beneficial change in ownership) and are not expressly excluded from FINRA trade reporting rules.<sup>2</sup> Accordingly, firms must report these sales to FINRA for public dissemination purposes as they would any other trade.

Because many of these sales are effected at a per lot price, the per share price may extend beyond six decimal places. FINRA notes that the OTC Reporting Facility (ORF) can accommodate six decimal places for purposes of reporting a per share price. If the per share price is equal to or less than \$.000001,<sup>3</sup> firms should report a price of \$.000001. Any trade reported at a per share price less than \$.0001 will be publicly disseminated with a price of \$.0000.<sup>4</sup>

September 23, 2011

### Key Topics

- ▶ OTC Equity Security
- ▶ OTC Reporting Facility
- ▶ “Penny for the Lot” Transactions
- ▶ Trade Reporting
- ▶ “Worthless” Securities

### Referenced Rules & Notices

- ▶ FINRA Rule 6420
- ▶ FINRA Rule 6622
- ▶ NASD Rule 2320

Finally, FINRA notes that some firms deem a security “worthless” solely on the basis that it currently has no bid and no longer trades.<sup>5</sup> Firms are reminded that in any transaction with a customer, including those involving securities that a firm may deem to be “worthless,” best execution obligations under NASD Rule 2320 apply, and firms are required to use reasonable diligence to ascertain whether there is a market for the security.

## Endnotes

1. It is FINRA’s understanding that firms may make this accommodation so that their customers can claim a capital loss in the current year rather than wait for a bankruptcy or other event establishing that the security is “wholly worthless” for purposes of the Internal Revenue Code and IRS rules and regulations. Nothing in this *Notice* is intended to impact the analysis of whether a security is “worthless” or whether customer sales of securities deemed to be “worthless” constitute bona fide losses for tax purposes.
2. See FINRA Rule 6622.  
  
These sales do not fall within the exception for “away from the market sales” under FINRA trade reporting rules and must not be reported as such. See [Trade Reporting Frequently Asked Questions](#), Section 601.
3. FINRA notes that the ORF will not accept a trade price of zero. Therefore, if a security is transferred for no consideration, the transfer would not be reportable to FINRA.
4. FINRA publicly disseminates last sale information for transactions in OTC equity securities via the Trade Data Dissemination Service (TDDS). TDDS disseminates price information out to four decimal places.
5. See note 1 herein.

# Trade Reporting Notice

## Trade Reporting Transactions in OTC Equity Securities and Restricted Equity Securities

### Executive Summary

FINRA is issuing this *Notice* to remind firms that over-the-counter (OTC) trades in OTC Equity Securities and trades in Restricted Equity Securities under Securities Act Rule 144A must be reported to FINRA in accordance with FINRA trade reporting rules. If a firm executes a trade in a security for which there is no valid OTC symbol, the firm must obtain a symbol so it can fulfill its trade reporting obligations.

Questions regarding this *Notice* should be directed to:

- ▶ Legal Section, Market Regulation, at (240) 386-5126;
- ▶ FINRA Operations, at (866) 776-0800; or
- ▶ Office of General Counsel, at (202) 728-8071.

### Discussion

All OTC transactions in OTC Equity Securities must be reported to the OTC Reporting Facility (ORF), in accordance with the FINRA Rule 6600 and 7300 Series, unless they fall within an express exception.<sup>1</sup> The term “OTC Equity Security” is defined in FINRA Rule 6420 as any equity security that is not an “NMS stock”;<sup>2</sup> provided, however, that the term OTC Equity Security shall not include any “Restricted Equity Security.” Thus, “OTC Equity Security” is broadly defined and could include non-exchange-listed equity securities of issuers that have recently emerged from bankruptcy, have no visible public market or are closely held, and non-exchange-listed contingent value rights.

“Restricted Equity Security” is defined in Rule 6420 as any equity security that meets the definition of “restricted security” as contained in Securities Act Rule 144(a)(3). Transactions in Restricted Equity Securities effected under Securities Act Rule 144A must be reported to the ORF.<sup>3</sup> Transactions in Restricted Equity Securities that are not effected under Rule 144A are not reportable.

September 23, 2011

### Key Topics

- ▶ Non-NMS Stock
- ▶ OTC Equity Security
- ▶ OTC Reporting Facility
- ▶ OTC Symbol
- ▶ Restricted Equity Security
- ▶ Trade Reporting
- ▶ “When, As and If” Issued

### Referenced Rules & Notices

- ▶ FINRA Rule 2010
- ▶ FINRA Rule 6420
- ▶ FINRA Rule Series 6600
- ▶ FINRA Rule 6622
- ▶ FINRA Rule Series 7300
- ▶ Regulatory Notice 09-05
- ▶ Securities Act Rule 144
- ▶ Securities Act Rule 144A

From time to time, FINRA receives inquiries about whether certain securities are OTC Equity Securities or Restricted Equity Securities. FINRA is reminding firms that they must have policies and procedures and internal controls in place, including, as necessary, consultation with their counsel, to determine whether FINRA trade reporting obligations are triggered, whether a security meets the definition of OTC Equity Security or Restricted Equity Security and whether any exceptions apply.

In instances where a security does not have a valid OTC symbol assigned, a firm must promptly request that FINRA Operations assign a symbol so that the firm can fulfill its trade reporting obligations. Firms should submit the request on the [OTC Equity Symbol Request Form](#) and must provide all requested information, including a CUSIP number for the security.<sup>4</sup> (FINRA does not issue OTC symbols for any equity security that does not have a CUSIP number.<sup>5</sup>) If the security does not have a symbol at the time the trade is executed, the trade should be reported to FINRA immediately upon the issuance of the symbol and be marked late, as applicable. If the trade is not reported on the trade date, it should be reported on an “as/of” basis using the original execution date as the trade date.

The fact that a security does not have a valid symbol at the time of execution of the trade does not relieve a firm of its trade reporting obligations under FINRA rules. As noted above, a firm with a trade reporting obligation must promptly take the necessary steps to have a symbol assigned and report the trade. Failure to do so is a violation of FINRA trade reporting rules. Moreover, a pattern and practice of executing reportable trades without obtaining a symbol and reporting the trade to FINRA may be considered conduct inconsistent with high standards of commercial honor and just and equitable principles of trade in violation of FINRA Rule 2010.

Firms are reminded that the issuance of an OTC symbol does not otherwise represent a review by FINRA of the tradeability of the security or the adequacy of any disclosures. For example, FINRA receives and processes requests for symbols for “when, as and if issued” contracts; however, the processing and issuance of such symbols does not represent a view by FINRA that the transactions are bona fide and/or subject to (or exempt from) any requirements or prohibitions under the federal securities laws. Those questions are matters of interpretation under the federal securities laws and are neither within the scope of FINRA’s responsibilities under the Uniform Practice Code nor will otherwise be addressed by FINRA as part of the symbol issuance process. Consequently, firms may not rely on the issuance of a trading symbol as permitting, excusing or mitigating any conduct that violates the federal securities laws and/or FINRA rules.<sup>6</sup> Firms also are reminded of their responsibility to ensure that they comply with the federal securities laws and FINRA rules when participating in unregistered resales of restricted securities.<sup>7</sup>

## Endnotes

1. As a general matter, certain transactions and transfers are not reported to FINRA at all (*e.g.*, trades executed and reported through an exchange, including a foreign exchange, and transfers made pursuant to an asset purchase agreement that has been approved by a bankruptcy court), while other transactions are reported to FINRA only for regulatory transaction fee assessment purposes under Section 3 of Schedule A to the FINRA By-Laws (*e.g.*, away from the market sales and transfers in connection with certain corporate control transactions). See FINRA Rule 6622(e).
2. “NMS stock” is defined in Rule 600(b) of SEC Regulation NMS as any NMS security other than an option. “NMS security” is defined as “any security or class of securities for which transaction reports are collected, processed, and made available pursuant to an effective transaction reporting plan, or an effective national market system plan for reporting transactions in listed options.”
3. See FINRA Rule 6622(a)(3).
4. See [Trade Reporting FAQ #105.1](#).  
Firms should use the OTC Equity Symbol Request Form to request symbols for Restricted Equity Securities. The form includes a box to indicate that the security is restricted, and the requesting firm must submit a letter of tradeability with the request.
5. See [Trade Reporting FAQ #105.4](#).
6. See, *e.g.*, [Uniform Practice Advisory \(UPC # 023-2007\)](#) August 21, 2007.
7. See [Regulatory Notice 09-05](#) (January 2009).