

OMB APPROVAL

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No. SR - 2006 - 082

Amendment No.

Proposed Rule Change by National Association of Securities Dealers

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial ☒	Amendment ☐	Withdrawal ☐	Section 19(b)(2) ☐	Section 19(b)(3)(A) ☒	Section 19(b)(3)(B) ☐
			Rule		
Pilot ☐	Extension of Time Period for Commission Action ☐	Date Expires 	☒ 19b-4(f)(1)	☐ 19b-4(f)(4)	
			☐ 19b-4(f)(2)	☐ 19b-4(f)(5)	
			☐ 19b-4(f)(3)	☐ 19b-4(f)(6)	

Exhibit 2 Sent As Paper Document



Exhibit 3 Sent As Paper Document

**Description**

Provide a brief description of the proposed rule change (limit 250 characters).

Revisions to the Series 22 examination program.

Contact Information

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

First Name Last Name
Title
E-mail
Telephone Fax

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date By
(Name)

(Title)

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

PATRICE GLINIECKI,

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

Form 19b-4 Information

Add Remove View

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

Exhibit 1 - Notice of Proposed Rule Change

Add Remove View

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

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

Add Remove View

Exhibit Sent As Paper Document

☐

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

Exhibit 3 - Form, Report, or Questionnaire

Add Remove View

Exhibit Sent As Paper Document

☒

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

Exhibit 4 - Marked Copies

Add Remove View

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

Exhibit 5 - Proposed Rule Text

Add Remove View

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

Partial Amendment

Add Remove View

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

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ the National Association of Securities Dealers, Inc. (“NASD”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) revisions to the study outline and selection specifications for the Limited Representative – Direct Participation Programs (Series 22) examination program.² The proposed revisions update the material to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a direct participation programs representative. NASD is not proposing any textual changes to the By-Laws, Schedules to the By-Laws, or Rules of NASD.

The revised study outline is attached. The Series 22 selection specifications have been submitted to the Commission under separate cover with a request for confidential treatment pursuant to Rule 24b-2 under the Act.³

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

¹ 15 U.S.C. 78s(b)(1).

² NASD also is proposing corresponding revisions to the Series 22 question bank, but based upon instruction from the Commission staff, NASD is submitting SR-NASD-2006-082 for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(1) thereunder, and is not filing the question bank for Commission review. See Letter to Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, from Belinda Blaine, Associate Director, Division of Market Regulation, SEC, dated July 24, 2000. The question bank is available for Commission review.

³ 17 CFR 240.24b-2.

At its meeting on January 24, 2001, the Board of Directors of NASD Regulation, Inc. authorized the staff to propose modifications to examination programs, including study outlines, examination specifications, and question banks, and to file the proposed modifications with the Commission, without obtaining further or specific authorization from the Board of Directors of NASD Regulation, Inc. The Board of Governors of NASD had an opportunity to review that action at its meeting on January 25, 2001. Further, counsel for The Nasdaq Stock Market, Inc. and NASD Dispute Resolution, Inc. were provided an opportunity to consult with respect to that action. No other action by NASD is necessary for the filing of the proposed rule change.

As further discussed below, NASD is filing the proposed rule change for immediate effectiveness. NASD proposes to implement the revised Series 22 examination program on August 15, 2006. NASD will announce the proposed rule change and the implementation date in a Notice to Members (“NTM”) to be published on the same date as this filing.

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

(a) Purpose

Section 15A(g)(3) of the Act⁴ requires NASD to prescribe standards of training, experience, and competence for persons associated with NASD members. In accordance with that provision, NASD has developed examinations, and administers examinations developed by other self-regulatory organizations, that are designed to establish that

⁴ 15 U.S.C. 78o-3(g)(3).

persons associated with NASD members have attained specified levels of competence and knowledge. NASD periodically reviews the content of the examinations to determine whether revisions are necessary or appropriate in view of changes pertaining to the subject matter covered by the examinations.

Pursuant to NASD Rule 1032(c), an associated person of a member who meets the definition of representative in Rule 1031 may register with NASD as a Limited Representative – Direct Participation Programs if: (1) the individual's activities in the investment banking and securities business are limited solely to the solicitation, purchase, and/or sale of equity interests in or debt of direct participation programs as defined in Rule 1022(e)(2) and (2) the individual passes the Series 22 qualification examination.

A committee of industry representatives, together with NASD staff, recently undertook a review of the Series 22 examination program. As a result of this review, NASD is proposing to make the following revisions to the study outline to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a direct participation programs representative. NASD is proposing to add a section on SEC Form S-1 registration. NASD also is proposing to add a section on NASD Rule 2370 (Borrowing from or Lending to Customers) and a section on like-kind exchanges.

In addition, NASD is proposing to revise the study outline to remove the sections on Section 4(3) (Transactions by a dealer) under the Securities Act of 1933⁵ and SEC Rule 174 (Delivery of prospectus by dealers; exemptions under Section 4(3)).⁶ Further,

⁵ 15 U.S.C. 77d(3).

⁶ 17 CFR 230.174.

NASD is proposing to remove the sections on NASD Rules 1040 (Registration of Assistant Representatives and Proctors) and 1110 (formerly Registration of Government Securities Principals and Representatives), as well as to remove the section on NASD Certificate of Incorporation.

NASD is proposing these changes to the entire content of the Series 22 examination, including the selection specifications and question bank. The number of questions on each section of the Series 22 examination will remain the same. In addition, the number of questions on the examination will remain at 100, and candidates will continue to have 2¼ hours (135 minutes) to complete the exam. Also, each question will continue to count one point, and each candidate must correctly answer 70 percent of the questions to receive a passing grade.

(b) Statutory Basis

NASD believes that the proposed revisions to the Series 22 examination program are consistent with the provisions of Sections 15A(b)(6)⁷ and 15A(g)(3) of the Act,⁸ which authorize NASD to prescribe standards of training, experience, and competence for persons associated with NASD members.

4. Self-Regulatory Organization's Statement on Burden on Competition

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

⁷ 15 U.S.C. 78o-3(b)(6).

⁸ 15 U.S.C. 78o-3(g)(3).

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

Written comments were neither solicited nor received.

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

Not applicable.

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

The proposed rule change is effective upon filing pursuant to Section 19(b)(3)(A)(i) of the Act⁹ and Rule 19b-4(f)(1) thereunder,¹⁰ in that the proposed rule change constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of NASD. NASD proposes to implement the revised Series 22 examination program on August 15, 2006. NASD will announce the implementation date in an NTM to be published on the same date as this filing.

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

Not applicable.

9. **Exhibits**

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

Exhibit 3a. Revised Study Outline for the Series 22 Examination.

Exhibit 3b. Revised Selection Specifications for the Series 22 Examination.

⁹ 15 U.S.C. 78s(b)(3)(A)(i).

¹⁰ 17 CFR 240.19b-4(f)(1).

NASD has requested confidential treatment for the Series 22 revised selection specifications, and thus the specifications are omitted from this filing. The Series 22 revised selection specifications have been filed separately with the Commission pursuant to Rule 24b-2 under the Act.¹¹

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

¹¹ 17 CFR 240.24b-2.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34- ; File No. SR-NASD-2006-082)

Self-Regulatory Organizations: National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Revisions to the Series 22 Examination Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on , the National Association of Securities Dealers, Inc. (“NASD”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD. NASD has designated the proposed rule change as constituting a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of the self-regulatory organization pursuant to Section 19(b)(3)(A)(i) of the Act³ and Rule 19b-4(f)(1) thereunder,⁴ which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(i).

⁴ 17 CFR 240.19b-4(f)(1).

NASD is filing revisions to the study outline and selection specifications for the Limited Representative – Direct Participation Programs (Series 22) examination program.⁵ The proposed revisions update the material to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a direct participation programs representative. NASD is not proposing any textual changes to the By-Laws, Schedules to the By-Laws, or Rules of NASD.

The revised study outline is attached. The Series 22 selection specifications have been submitted to the Commission under separate cover with a request for confidential treatment pursuant to Rule 24b-2 under the Act.⁶

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

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

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

1. Purpose

⁵ NASD also is proposing corresponding revisions to the Series 22 question bank, but based upon instruction from the Commission staff, NASD is submitting SR-NASD-2006-082 for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(1) thereunder, and is not filing the question bank for Commission review. See Letter to Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, from Belinda Blaine, Associate Director, Division of Market Regulation, SEC, dated July 24, 2000. The question bank is available for Commission review.

Section 15A(g)(3) of the Act⁷ requires NASD to prescribe standards of training, experience, and competence for persons associated with NASD members. In accordance with that provision, NASD has developed examinations, and administers examinations developed by other self-regulatory organizations, that are designed to establish that persons associated with NASD members have attained specified levels of competence and knowledge. NASD periodically reviews the content of the examinations to determine whether revisions are necessary or appropriate in view of changes pertaining to the subject matter covered by the examinations.

Pursuant to NASD Rule 1032(c), an associated person of a member who meets the definition of representative in Rule 1031 may register with NASD as a Limited Representative – Direct Participation Programs if: (1) the individual’s activities in the investment banking and securities business are limited solely to the solicitation, purchase, and/or sale of equity interests in or debt of direct participation programs as defined in Rule 1022(e)(2) and (2) the individual passes the Series 22 qualification examination.

A committee of industry representatives, together with NASD staff, recently undertook a review of the Series 22 examination program. As a result of this review, NASD is proposing to make the following revisions to the study outline to reflect changes to the laws, rules and regulations covered by the examination and to better reflect the duties and responsibilities of a direct participation programs representative. NASD is proposing to add a section on SEC Form S-1 registration. NASD also is proposing to add a section on NASD Rule 2370 (Borrowing from or Lending to

⁶ 17 CFR 240.24b-2.

⁷ 15 U.S.C. 78o-3(g)(3).

Customers) and a section on like-kind exchanges.

In addition, NASD is proposing to revise the study outline to remove the sections on Section 4(3) (Transactions by a dealer) under the Securities Act of 1933⁸ and SEC Rule 174 (Delivery of prospectus by dealers; exemptions under Section 4(3)).⁹ Further, NASD is proposing to remove the sections on NASD Rules 1040 (Registration of Assistant Representatives and Proctors) and 1110 (formerly Registration of Government Securities Principals and Representatives), as well as to remove the section on NASD Certificate of Incorporation.

NASD is proposing these changes to the entire content of the Series 22 examination, including the selection specifications and question bank. The number of questions on each section of the Series 22 examination will remain the same. In addition, the number of questions on the examination will remain at 100, and candidates will continue to have 2¼ hours (135 minutes) to complete the exam. Also, each question will continue to count one point, and each candidate must correctly answer 70 percent of the questions to receive a passing grade.

2. Statutory Basis

NASD believes that the proposed revisions to the Series 22 examination program are consistent with the provisions of Sections 15A(b)(6)¹⁰ and 15A(g)(3) of the Act,¹¹ which authorize NASD to prescribe standards of training, experience, and competence

⁸ 15 U.S.C. 77d(3).

⁹ 17 CFR 230.174.

¹⁰ 15 U.S.C. 78o-3(b)(6).

¹¹ 15 U.S.C. 78o-3(g)(3).

for persons associated with NASD members.

B. Self-Regulatory Organization's Statement on Burden on Competition

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

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

Written comments were neither solicited nor received.

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

The proposed rule change has become effective pursuant to Section 19(b)(3)(A)(i) of the Act¹² and Rule 19b-4(f)(1) thereunder,¹³ in that the proposed rule change constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of the self-regulatory organization. NASD proposes to implement the revised Series 22 examination program on August 15, 2006. NASD will announce the implementation date in a Notice to Members to be published on the same date as this filing.

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

¹² 15 U.S.C. 78s(b)(3)(A)(i).

¹³ 17 CFR 240.19b-4(f)(1).

IV. Solicitation of Comments

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

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-NASD-2006-082 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-NASD-2006-082. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for

inspection and copying in the Commission's Public Reference Room. Copies of such filing also will be available for inspection and copying at the principal office of NASD.

All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to the File Number SR-NASD-2006-082 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁴

Nancy M. Morris

Secretary

¹⁴ 17 CFR 200.30-3(a)(12).



**DIRECT PARTICIPATION PROGRAMS
LIMITED REPRESENTATIVE
QUALIFICATION EXAMINATION**

(TEST SERIES 22)

STUDY OUTLINE

STUDY OUTLINE
DIRECT PARTICIPATION PROGRAMS
LIMITED REPRESENTATIVE QUALIFICATION EXAMINATION
(TEST SERIES 22)

The NASD Direct Participation Programs Limited Representative (Series 22) Qualification Examination (hereinafter called the “DPP Exam”) is designed to test a candidate's knowledge of the products, rules and statutory provisions applicable to this category of registration. By passing the DPP Exam, a candidate becomes a Direct Participation Programs Series 22 Registered Representative (hereinafter called the DPP Registered Representative.)

The DPP Registered Representative can participate in the purchase and sale of certain direct participation programs (see Section 1.1-Direct Participation Programs Investment Entities and Section 2.0 - Types of Direct Participation Programs) offered. Section 1.2 lists securities that cannot be sold by the DPP Registered Representative--either because these securities are registered under the Investment Company Act of 1940 or the trades take place on the secondary market.

This study outline has been prepared to assist member firms in preparing candidates to sit for the examination. The outline may also be used by commercial course developers in the preparation of training material, by training directors in the development of lecture notes and seminar programs, and by candidates themselves, both to structure their study and as a final review checklist prior to sitting for the DPP Exam. The DPP Exam and this study outline are composed of six general areas of knowledge, which are listed below with the approximate percentage point value assigned to each area.

	DESCRIPTION	% POINT VALUE
1	Investment Entities for Direct Participation Programs	12
2	Types of Direct Participation Programs	11
3	Offering Practices Applicable to Direct Participation Programs	14
4	Tax Issues Applicable to Direct Participation Programs	20
5	Regulation of Direct Participation Programs	32
6	Factors to Consider in Evaluating Direct Participation Programs	11
TOTAL		100

Structure of the Examination and Grading Procedures

The DPP Exam is composed of 100 multiple-choice questions covering all of the material in the following outline in accordance with the subject matter distribution shown in the Table above. A maximum of 135 minutes is allowed for candidates to complete the DPP Exam. Each multiple-choice question is worth one point. Candidates will be required to correctly answer 70 or more of the 100 questions on the DPP Exam in order to receive a passing grade. At the completion of the DPP Exam, candidates will be provided with their score for the entire DPP Exam, along with their score on each of the six sections.

The DPP Exam is a closed-book test and candidates will not be permitted to use any reference material during their testing session. Scratch paper and basic electronic calculators will be provided to a candidate by the test administrator and must be returned to the administrator at the end of the testing session.

The questions used in the DPP Exam are updated regularly to reflect the current interpretations of the rules and regulations on which they are based. Questions on new rules and regulations are added to the pool of questions and questions on outdated or changed rules and regulations are deleted within a reasonable time after the changes take place. At the end of this outline there are four sample questions written in various formats used in the DPP Exam. The samples do not reflect the difficulty level of the test questions or the subject matter distribution of the test itself. They are intended to familiarize candidates with the various types of multiple-choice question formats used in the DPP Exam.

Reference materials that may be used as a source material starting point for course developers in preparing training programs for the DPP Exam or for candidates as part of a study program are listed below. It is not necessary to obtain all of these reference materials since the topics covered in one may overlap other references. In addition, there are study courses specifically designed for the DPP Exam by vendors that are often listed in local yellow page directories or advertise in securities periodicals.

This study outline is available on the NASD Regulation Web Site at www.nasd.com.

At the end of this outline there are four sample questions written in the various formats used in the DPP Representative Exam. These samples do not reflect the difficulty level of the test questions or the subject matter distribution of the test itself. They are to familiarize candidates with the types of multiple choice question formats in the DPP Representative Exam.

REFERENCE MATERIALS

Blue Sky Practice for Public and Private Direct Participation Offerings

Peter M. Fass and Derek A. Wittner
West Group
610 Opperman Drive
St. Paul, MN 55123
www.westgroup.com

Federal Securities Law Reporter

Volume 1 - Securities Act
Volume 2 - Exchange Act
Commerce Clearing House, Inc.
4025 W. Peterson Avenue
Chicago, IL 60646

Federal Taxation of Partnerships and Partners,

Volumes 1 and 2
W.S. McKee, W.F. Nelson and R.L. Whitmire
Warren, Gorham & Lamont, Inc.
Boston, MA 02111

Guide to Limited Liability Companies,

CCH Incorporated
P.O. Box 5490
Chicago, IL 60680
www.cch.com

Investment Limited Partnerships Handbook

R. J. Haft and P. M. Fass
Clark Boardman Callaghan
155 Pfingsten Road
Deerfield, IL 60015
www.west.thomson.com

Limited Liability Company Handbook

M. A. Sargent and W.D. Schwidetzky
West Group
610 Opperman Drive
St. Paul, MN 55123
www.west.thomson.com

NASD Manual

NASD MediaSource

9513 Key West Avenue
Rockville, MD 20850
www.nasd.com/regulation/manual
Oil and Gas: Federal Income Taxation (2005)

Patrick A. Hennessee, Ph.D., CPA
CCH Incorporated
P.O. Box 5490
Chicago, IL 60680
www.cch.com

2005 Federal Tax Course

Aspen Panel Publishers
1185 Avenue of the Americas
New York, NY 10036
<http://tax.cchgroup.com/Aspen>

Resales of Restricted Securities

J. William Hicks
West Group
620 Opperman Drive
St. Paul, MN 55164
www.westgroup.com

Securities Act Handbook

Aspen Publishers
111 Eighth Avenue
New York, NY 10011
www.aspenpublishers.com

Securities Law Handbook, 2005 ed.

H.S. Bloomenthal
Clark Boardman Callaghan
610 Opperman Drive
St. Paul, MN 55164
www.west.thomson.com

Tax Advantaged Securities Handbook

R. J. Haft and Peter M. Fass
West Group
610 Opperman Drive
St. Paul, MN 55164
www.westgroup.com

1.0

INVESTMENT ENTITIES FOR DIRECT PARTICIPATION PROGRAMS

1.1 Investment Entities

1.1.1 Limited Partnerships (LP)

1.1.1.1 Limited liability

1.1.1.2 Consequences of the pass through tax provision

1.1.1.3 Filing of limited partnership organizational documents in the states--usually called the Certificate of Limited Partnership

1.1.1.3.1 Contains name, address, purpose, date of formation and names of general partner(s) and in some states the names, addresses, and amount of capital contribution of the general and limited partners

1.1.1.3.2 Required to create a limited partnership

1.1.1.3.3 Required for amendments to information contained in Section 1.1.1.3.1 above

1.1.1.4 Agreement of Limited Partnership--the contract between the general partner(s) and limited partners to conduct the business of the limited partnership

1.1.1.4.1 Lists the date of formation, name, place of business, purpose and date of termination

1.1.1.4.2 Specifies the types of partners, each individual partner, the capital contribution of each partner and the provisions in the event a partner defaults on a capital contribution

Types of partners--general, limited, original limited, special limited

Name, address, capital contribution and percent interest in limited partnership are usually listed on separate exhibit

Capital contributions can be made at one time, staged over a defined period or are subject to being called under specified circumstances

Default of partner's obligation to contribute can lead to dilution of interest or dismissal from limited partnership

1.1.1.4.3 Allocates operating income and loss, capital gain and loss, operating cash distributions and capital cash distributions among the partners

Disproportionate allocation of income, loss, gain and cash distribution among the partners

Preferred cash distribution
Cumulative cash distribution

Subordinated distribution

- 1.1.1.4.4 General partner(s)--rights and obligations
 - 1.1.1.4.4.1 Exclusive power and authority to manage the partnership
 - 1.1.1.4.4.2 Usual duties
 - Execute all agreements, contracts and certificates to operate partnership
 - Borrow funds
 - Purchase liability and casualty insurance
 - Employ agents, attorneys, accountants and contractors
 - Pay all expenses
 - Act as tax matters partner
 - Sell or dispose of partnership assets
 - Act as attorney-in-fact for limited partners
 - 1.1.1.4.4.3 Usual limitations on powers of general partner(s) without approval of limited partners
 - Admission of new general partner(s)
 - Substitution of existing general partner(s)
 - Change the purpose of the partnership
 - Sale of all or substantially all the assets of the partnership
 - Refinancing in certain situations
 - 1.1.1.4.4.4 Compensation of general partner(s)
 - Only as specified in partnership agreement
 - Affiliate can be compensated but only at competitive rates
 - 1.1.1.4.4.5 General partner liability
 - 1.1.1.4.4.6 General partner indemnification
 - 1.1.1.4.4.7 Right to compete with partnership
 - 1.1.1.4.4.8 Fiduciary responsibility to limited partners
 - 1.1.1.4.5 Limited partners' rights
 - Amend partnership agreement
 - Vote to lift restrictions on power of general partner(s) (see Section 1.1.1.4.4.3)
 - Receive periodic reports
 - Inspect and copy books and records
 - Vote to continue partnership upon death, bankruptcy or incompetency of sole remaining general partner
 - Remove general partner(s) if provided in partnership agreement
 - 1.1.1.4.6 Limited partners' obligations
 - Pay capital contribution
 - Potential liability for unpaid capital contributions and distributions received, in event of default
 - 1.1.1.4.7 Transfer of interest in limited partnership

- 1.1.1.4.7.1 General partner(s)
 - Need approval of limited partners
 - Opinion of counsel that partnership will not be terminated or taxed as corporation
 - Bankruptcy, death or incompetence
- 1.1.1.4.7.2 Limited Partners
 - Opinion of counsel that partnership will not be terminated or taxed as a corporation
 - General partner(s) approval
 - Restrictions usually on transfer to non-family
 - General partner(s) right of first refusal
- 1.1.1.4.8 Dissolution and liquidation of a limited partnership
- 1.1.1.4.8.1 Events causing dissolution
 - Withdrawal of last general partner
 - Vote of partners
 - Sale of all the assets of the partnership
 - Approval of general partner(s) and required number of limited partners
 - Expiration of term of partnership
- 1.1.1.4.8.2 Liquidation
 - Payment of expenses and liabilities of partnership
 - Distribution to partners in accord with terms of partnership agreement
 - Filing of termination certificates
- 1.1.2 Limited Liability Companies (LLC)**
- 1.1.2.1 Advantages
 - Receive same pass through tax advantages as a limited partnership
 - Have limited liability attributes of corporations
 - Allows disproportionate allocation of income, loss, gain and cash distribution
- 1.1.2.2 Organization filings of LLC--usually called the Articles of Organization
- 1.1.2.2.1 Contains name, address, date of formation and termination and names of members (a minimum of two required) and may contain other provisions from operating agreement
- 1.1.2.2.2 Required to create LLC
- 1.1.2.2.3 Required for amendments to information contained in Section 1.1.2.2.1
- 1.1.2.3 Operating Agreement of LLC--the contract among the members to conduct the business of the LLC
- 1.1.2.3.1 Lists date of formation, name, place of business, purpose and date of termination

- 1.1.2.3.2 Specifies duties of members (may create Managing Member(s)) and their capital contributions
- 1.1.2.3.3 Specifies duties and responsibilities of members
- 1.1.2.3.4 Allocates operating income and loss, capital gain and loss, operating cash distributions and capital cash distributions among members
 - 1.1.2.3.4.1 Disproportional allocations
 - 1.1.2.3.4.2 Preferred cash distributions
 - 1.1.2.3.4.3 Cumulative cash distributions
 - 1.1.2.3.4.4 Subordinated distributions
- 1.1.2.3.5 Rights of members
 - Elect managing members
 - Amend operating agreement
 - Vote on LLC matters as provided in the operating agreement
 - Approve transfers of membership interests unanimously
 - Consent to dissolve the LLC
- 1.1.2.3.6 Rights and powers of managing member(s)
 - Exclusive power to manage the affairs of the LLC
 - Term of office specified in operating agreement
 - Duties similar to general partner(s) in limited partnership
 - Limitation of powers similar to general partner(s) in limited partnership
- 1.1.2.3.7 Liabilities of members including managing member(s) are only for promises of contributions and services to the LLC; not liable for debts and obligations of the LLC
- 1.1.2.3.8 Transfer of member's ownership in the LLC
- 1.1.2.3.9 Indemnification of managing members
- 1.1.2.3.10 Dissolution of the LLC
 - 1.1.2.3.10.1 Events causing dissolution
 - Consent of all members
 - Expiration of term of the LLC
 - 1.1.2.3.10.2 Liquidation
 - Payment of expenses and liabilities of the LLC
 - Distributions to members
 - 1.1.2.3.10.3 Filing of certificate of dissolution

1.1.3

S Corporations

- 1.1.3.1 Requirements for eligibility
 - Limited number of shareholders
 - Must be a domestic, eligible corporation
 - Shareholders must be individuals, certain estates, trusts, or tax exempt organizations
- 1.1.3.2 Election of tax year
- 1.1.3.3 Generally a tax pass-through entity
 - No disproportionate allocation
 - No negative capital account
- 1.1.3.4 Termination of S Corporation election
 - Revoking the election
 - Ceasing to qualify as an S corporation
 - Violating the passive investment income restrictions
 - Restrictions against re-establishing S Corporation

1.1.4 General Partnerships

- 1.1.4.1 Liabilities of general partners
- 1.1.4.2 Partnership subject to technical dissolution by reason of death or legal disability of a partner even though the partnership may be continue
- 1.1.4.3 Passive interests are treated as securities

1.1.5 Joint ventures

- 1.1.5.1 Liabilities of venturers
- 1.1.5.2 Co-venturers join together for a specific project
- 1.1.5.3 Joint venture is terminated upon completion of project
- 1.1.5.4 In some jurisdictions, a corporation may not be a partner, but may take a position as a joint venturer
- 1.1.5.5 Passive interests are treated as securities

1.1.6 Grantor trusts

- 1.1.6.1 Generally used for equipment leasing programs
- 1.1.6.2 May provide pass-through tax benefits

1.2 Securities Products That Cannot be Sold by a Direct Participation Programs Representative

1.2.1 Real estate investment trusts (REITs)

1.2.2 Master limited partnerships

Roll-ups

Exchange listed real estate limited partnerships

1.2.3 Public limited partnership units in the secondary market

1.2.4 Municipal securities

1.2.5 Corporate securities (domestic and foreign)

Stocks

Bonds

Rights and warrants

1.2.6 Options

1.2.7 Mortgage-backed instruments

Collateralized mortgage obligations (CMOs)

Real estate mortgage investment conduits (REMICs)

1.2.8 Mutual funds (closed-end and open-end investment company shares)

1.2.9 Variable annuities

1.2.10 U.S. government and agency securities

2.0

TYPES OF DIRECT PARTICIPATION PROGRAMS

2.1 Real Estate Programs

2.1.1 Affordable housing

2.1.1.1

Advantages

- Tax credits
- Passive losses
- Predictable tax benefits
- Long term, highly leveraged mortgage financing

2.1.1.2

Risks

- Changes in Government policy and practice
- Subsidized rent greater than market rent
- Historic lack of appreciation potential
- Cash distributions limited by Government regulations
- Loss of rental and other subsidies
- Highly leveraged financing

2.1.2

Development properties (new construction)

2.1.2.1

Advantages

- Higher appreciation potential
- Maintenance and replacement costs lower in early years
- Leverage
- Tax deferred cash flow
- Passive losses
- Long term take-out mortgage financing

2.1.2.2

Risks

- Market acceptability of new development
- Pace of renting to tenants (rate of absorption)
- Development costs in excess of forecast
- Cost and availability of long-term mortgage financing
- Competition - overbuilding-effect on rents
- Governmental restrictions: zoning and building codes
- Changing Governmental regulations: rent control and environmental

2.1.3

Existing properties

2.1.3.1

Advantages

- Greater predictability of net operating income
- Higher reliability of operating cost forecasts
- Physical condition subject to inspection
- Known tenant composition
- Tax deferred cash flow
- Passive losses
- Financing often available from seller

2.1.3.2

Risks

- Higher maintenance and replacement costs
- Unpredictable major maintenance and rehabilitation costs
- Restrictions in existing leases
- Additional competitive properties
- Changing Governmental regulations: rent control and environmental issues

2.1.4 Land Development

2.1.4.1

Advantages

- Potential for higher appreciation
- Seller financing-purchase money mortgage note
- Usually low leverage

2.1.4.2

Risks

- No cash flow
- Carrying costs (taxes, and debt service) with no revenue
- Government restrictions: zoning and environmental
- Lack of appreciation in excess of acquisition and carrying costs of land
- Institutional financing often difficult to obtain
- Higher potential for loss

2.1.5 Sale-Leaseback

2.1.5.1

Advantages

- Predictable taxable income, loss and cash flow
- Risk decreases as net worth of lessee increases
- Mortgage financing more readily available

2.1.5.2

Risks

- Term of lease
- Cash flow and appreciation restricted by lease
- Appreciation often more dependent on financial market conditions than performance of property
- Re-rental after termination of initial lease
- Cost of acquisition greater than market value of property

2.1.6 Mortgage partnerships

2.1.6.1

Advantages

- First lien
- Predictable income
- Interest spread

2.1.6.2

Risks

- Junior liens
- Leverage
- Collection

2.1.7 Condominium securities

2.1.7.1

Rental Pools

2.2 Oil and Gas Programs

2.2.1 Types of programs

- 2.2.1.1 Exploratory
 - High deductibility of investment
 - Return potential determined after drilling stage
 - Higher risk of "dry holes"
- 2.2.1.2 Development
 - High deductibility of investment
 - Return potential less than returns on successful exploratory program
 - Lease costs tend to be higher
 - Lower dry-hole risk versus exploratory
- 2.2.1.3 Income
 - Few front-end tax benefits
 - Capitalized acquisition costs
 - Cash flow program with reinvestment feature
 - Factors to consider in evaluating an income program
 - Amount of oil and gas reserves still in the ground
 - Estimated future net revenues from reserves and calculated present value
 - Present value less various risk factors to obtain "fair market value" of property
 - Liquidity on present value
 - Inflation hedge
 - Possible future enhanced recovery techniques
- 2.2.1.4 Combination investment (drilling and income)
 - Diversification may reduce amount of risk
 - Potential to achieve tax deferral and cash flow
- 2.2.1.5 Completion
 - Intangible expenses and deductions
 - Depreciable tangible expenses
 - Receive a smaller percentage of revenue from wells

2.2.1 Analyzing sharing arrangements of oil and gas programs (methods of allocating costs and revenues)

- 2.2.2.1 Overriding royalty interest
 - Does not share program costs
 - Shares in revenues through cost free interest in production revenues
 - Payable under an oil and gas lease out of total production of well or deposit
- 2.2.2.2 Working interest
 - Interest in production revenues
 - Lessor does share program costs
- 2.2.2.3 Reversionary working interest
 - Does share program costs

Shares in revenues after investors recover their costs
If the lessee's share of the oil extracted; the balance belongs to the
land owner as his royalty interest plus owner's of overriding interest

2.2.2.4 Net operating profits interest
Limited to private deals

2.2.2.5 Disproportional sharing arrangement
Sponsor pays a lower percentage of all costs in return for a higher
percentage of program revenues
Sponsor may share in costs of dry holes
Normally investors pay deductible costs and sponsor pays non-
deductible costs

2.3 Equipment Leasing Programs

2.3.1 Structure of programs

2.3.1.1 Financial (or full payout) lease--no residual value
2.3.1.2 Operating lease-- residual value

2.3.2 Advantages

2.3.2.1 Depreciation
2.3.2.2 Interest deductions on borrowed funds
2.3.2.3 Predictable income

2.3.3 Risks

2.3.3.1 Investor tax basis limited by at-risk rules
2.3.3.2 Investment interest limitations on use of tax losses
2.3.3.3 Alternative minimum tax may limit deductibility of losses
2.3.3.4 Uncertain residual value
2.3.3.5 Potential phantom income upon sale of equipment
2.3.3.6 Cost allocations
2.3.3.7 Competition impacts re-leasing and sale

2.4 Miscellaneous Programs

2.4.1 Agricultural

2.4.1.1 Available deductions
Write-offs on start-up programs
Row crops
Depreciable property, i.e. perennial plants, property improvements, etc.

2.4.1.2 Profits achieved by
Sales of agricultural products
Appreciation of land value

2.4.1.3 Risks include
Natural elements

Disease
Market conditions

2.4.2 Livestock

2.4.2.1 Holding period requirement

2.4.2.2 Capitalized costs

2.4.2.3 Capital gains

2.4.2.4 Deductible maintenance costs

2.4.3 Entertainment

2.4.3.1 Structure of entertainment programs
Advertising service partnership
Production service company

2.4.3.2 Movie syndications
Income forecast method of depreciation
Accounting standards

2.4.4 Research and development/venture capital

2.4.4.1 Deductibility of royalty income

2.4.5 Debt-based (non-equity) direct participation programs

2.4.5.1 Portfolio income

2.4.5.2 Characteristics of debt vs. equity

2.4.5.3 Tax treatment

2.4.5.4 Eligibility of retirement accounts

2.4.6 Commodity Pools

2.4.6.1 Typically structured as limited partnerships, limited liability companies or business trusts

2.4.6.2 Commodity Pools are regulated both under the securities laws and the Commodity Futures Trading Commission Act

2.4.6.3 Commodity Pools typically invest in commodity futures contracts traded on regulated futures exchanges

2.4.7 Like-Kind Exchanges

2.4.7.1 Section 1031 of the Internal Revenue Code

2.4.7.2 Tenants-in-common structure

2.4.7.3

Applicability of private placement exemption rules
and anti-fraud rules

3.0

OFFERING PRACTICES APPLICABLE TO DIRECT PARTICIPATION PROGRAMS

3.1 Types of Underwriting Commitments

3.1.1 Best efforts

- Contingent
- All or none
- Mini-Max

3.1.2 Firm commitment

3.2 Syndication Practices

3.2.1 Managed offerings

3.2.1.1 Selling group manager

3.2.1.2 Soliciting dealer

3.2.1.3 Dealer manager functions

- Performs due diligence
- Solicits and allocates retail participation by other broker-dealers
- Maintains books and records
- May assist issuer in planning and preparation of offering
- May coordinate investor relations after the offering
- Enters into dealer/manager agreement with the program sponsor
- May be an affiliate of the sponsor

3.2.1.4 Sponsor-managed offerings

- Each dealer enters into agreement directly with program sponsor
- Dealers are paid directly by the program sponsor

3.2.2 Role of wholesalers

- Individuals or firms paid to retain selected dealers for the offering
- Interface between issuer and broker-dealers and their sales force
- Usually compensated on the basis of sales of program interests

3.2.3 Due Diligence

3.2.3.1 The exercise of reasonable care to determine that the offering disclosures are accurate and complete

3.2.3.2 Public offerings--statutory defense available

3.2.3.3 Private offerings--helps avoid fraud charges

3.2.3.4 Should be performed by broker-dealers making the offering

3.2.3.5 Typical activities

- Verify all material statements in the offering documents
- Confirm compliance with registration/exemption rules
- Review financial data
- Investigate management background
- Check issuers track record
- Review any assumptions in offering forecasts or projections
- Evaluate all fees and other distributions of proceeds

3.2.4 Finders

3.2.4.1 Defined as an un-registered introducer

3.2.4.2 Prohibited practices

- Sales compensation to non-members of a national securities exchange association registered with the Securities and Exchange Commission
- Referrals by non-members of individual clients to broker-dealers in exchange for compensation from broker-dealer

3.3 Subscription Practices

3.3.1 Signature pages of partnership documents

3.3.1.1 Purchaser representations

- Liquidity
- Marketability
- Suitability

3.3.2 Responsibility of the DPP registered representatives

- Familiarity with the DPP offering
- Timely delivery of the prospectus
- “Know your customer” rules
 - Understanding of the risks involved
 - Net worth, income and suitability
- Accuracy of investor’s representations

3.3.3 Sales are conditioned upon acceptance of subscribers

3.3.4 Supervision of order by broker-dealer--review of documents

3.4 Underwriting Compensation

3.4.1 Types of compensation

3.4.1.1 Cash

3.4.1.2 Non-cash

3.4.1.3 Indeterminate

- Carried interest /continuing compensation
- Other securities

3.4.2 NASD guidelines on sales compensation in public offerings

- 3.4.2.1 Limited to amount stated in offering document
- 3.4.2.2 Limit applies to total sales
- 3.4.2.3 10% of gross dollar amount of securities sold in public offerings; plus up to .5% for reimbursement of bona fide due diligence expenses
- 3.4.2.4 15% of proceeds for organization and offering expenses
- 3.4.2.5 Sharing commissions

4.0

TAX ISSUES APPLICABLE TO DIRECT PARTICIPATION PROGRAMS

4.1 Federal Tax Treatment of Direct Participation Programs

4.1.1 General characteristics

- 4.1.1.1 Conduit nature of entity
- 4.1.1.2 Required to file informational tax returns (IRS Forms 1065 and 1120S)
- 4.1.1.3 Required to allocate profits, losses, deductions and credits to partners
- 4.1.1.4 Tax elections
- 4.1.1.5 Some choice of accounting method
- 4.1.1.6 Some selection of taxable year (generally calendar year)
- 4.1.1.7 State tax treatment - generally like federal

4.1.2 Depreciation and amortization for tax purposes

- 4.1.2.1 Allows non-cash deduction based on entity's cost of depreciated or amortized asset
- 4.1.2.2 Depreciation requires asset held for production of income or used in trade or business
 - 4.1.2.2.1 Amortization allows straight line write-off of cost of intangible asset
- 4.1.2.3 Cannot depreciate unimproved land or inventory (e.g. lots for sale)
- 4.1.2.4 Types of depreciable properties
 - Personal property, equipment and land improvements
 - Residential rental property
 - Nonresidential real property
- 4.1.2.5 Tax benefits of depreciation
 - Deferral of tax liabilities on partnership income
 - Deductions in excess of income from partnership (passive income)
- 4.1.2.6 Basis of depreciable property-cost
 - Purchased property
 - Constructed property
 - Improvements to property
- 4.1.2.7 Determination of recovery period
 - Depends on property type
 - Possession relinquished
 - Demolition
 - Exhaustion of allowable depreciation

- 4.1.2.8 Methods of depreciation
 - Straight line
 - Accelerated

4.1.3 Depletion--Definition of depletable assets

- 4.1.3.1 Cost method
- 4.1.3.2 Percentage method
- 4.1.3.3 Small producers and royalty owners (less than 1,000 barrels per day)
 - Limited to 50% of taxable income prior to depletion allowance
 - Limited to 65% of partners' taxable income from all sources

4.1.4 Deductibility of expense items

- 4.1.4.1 Expenses deductible in year of occurrence
 - Interest (except construction interest)
 - Intangible drilling and development costs
 - Taxes--state and local
 - Direct payroll taxes incurred by the partnership
 - General operating costs
 - Service fees
 - Annual management fees
- 4.1.4.2 Expenses amortized over specified periods of time
 - Prepaid interest
 - Construction interest
 - Phase-in rules
 - Prepaid fees
 - Project financing fees
 - Loan standby or commitment fees
 - Rent-up fees (for leases over one year)
 - Organization fees
- 4.1.4.3 Non-deductible, capitalized expenses
 - Syndication related costs
 - Securities brokerage compensation
- 4.1.5 Tax Credits**
- 4.1.5.1 Can offset tax on income taxes within limits, but does not offset alternative minimum tax (AMT)
- 4.1.5.2 Rehabilitation credits
 - For certain buildings originally placed in service before 1936
 - For certified historic structures and buildings located in historic Districts
- 4.1.5.3 Low income housing credits
 - Determined in the year project is placed in service
 - Allowed over a specified number of years

- 4.1.6 Potential recapture on sale or other disposition of property**
 - Tax credit
 - Depreciation
- 4.2 Tax Information Provided by Investment Entity to Investors (Schedule K-1)**
 - 4.2.1 Required to be sent to investors annually within a time usually specified in agreement of investment entity**
 - 4.2.2 Required to be filed with Internal Revenue Service with investment entity's tax return**
 - 4.2.3 Lists name, address and federal identifying number of investment entity and investor**
 - 4.2.4 Information required for S Corporations is substantially less than for other investment entities**
 - 4.2.5 Provides analysis of investor's capital account (not provided on S Corporation's K-1)**
 - 4.2.5.1 Investor's capital account is not the same as the investor's tax basis
 - 4.2.5.2 Investor's capital account balance can be negative in all investment entities other than S Corporations
 - 4.2.5.3 Components of the capital account and their impact of its balance
 - Cash contributions increase balance
 - Cash distributions decrease balance
 - Non-cash property contributions increase balance
 - Non-cash property distributions decrease balance
 - Income and gain increase balance
 - Losses decrease balance
 - Other items such as tax exempt interest and non-deductible expenses such as entertainment increase or decrease balance
 - 4.2.6 Furnishes investor's share of income, loss, deductions, investment interest, credits, adjustments and tax preference items, foreign taxes, other items and supplemental information required. For investment entities other than S Corporations self employment information is furnished, if applicable**
- 4.3 Opinions of Tax Counsel for Direct Participation Programs**
 - 4.3.1 Typically refer to tax consequences of each material tax issue in offering**
 - 4.3.1.1 Opinion may be required as exhibit in certain programs.
- 4.4 Federal Tax Qualifications for Limited Partnerships (LP) and Limited Liability Companies (LLC)**
 - 4.4.1 Tax consequences**

4.4.1.1 Newly formed entities can elect partnership LP/LLC tax status under certain circumstances

4.4.2 Maintaining LP and LLC status of the entity

4.4.2.1 Loss of conduit tax status means tax consequences at entity level and at partner/member level

4.4.3 LPs and LLCs organized according to state statutes may automatically qualify for conduit tax status

4.5 Federal Tax Treatment of Limited Partnerships (LP) and Limited Liability Companies (LLC)

4.5.1 Sources of partner/member income, gain, loss and tax adjustments

Taxable income and loss

Capital gain and loss

Investment interest income and interest expense

Gains and losses from sales or exchanges of property used in trade or business and involuntary conversions

Tax credits

Tax preference items

4.5.2 Disposition of property and interests

4.5.2.1 Sale of LP/LLC interest

Capital gain or loss

Ordinary income

4.5.2.2 Tax free exchanges of LP/LLC property (Section 1031)

Requirement for like-kind exchange

No gain or loss

Tax basis is transferred

4.5.2.3 Gifts

Possibility of gift tax liability

Possibility of gain or ordinary income

4.5.2.4 Factors in disposition

Section 754 election--Step up basis upon the death of partner

Phantom income particularly in foreclosure or bankruptcy

4.5.3 Limitation on deduction of LP/LLC losses

4.5.3.1 Tax basis

4.5.3.1.1 Provides upper limit on deductibility of LP /LLC losses

4.5.3.1.2 Unused losses may be held until there is basis

4.5.3.1.3 Used to determine gain or loss on liquidation of LP /LLC or on sale or transfer of an interest

- 4.5.3.1.4 LP/LLC's basis in its assets (inside basis)
- 4.5.3.1.5 Partner's or member's basis is partner's interest in the LP or member's interest in the LLC (outside basis)
- 4.5.3.1.6 Components of basis
 - Cash contribution
 - Non-cash property contribution
 - LP /LLC debt for which the investor is personally liable
 - Non-recourse LP /LLC debt (no limitation for qualified debt in real estate, at-risk limitation for other investments)
- 4.5.3.1.7 Factors resulting in an increase in basis
 - Taxable income and capital gains
 - Cash contributions
 - Non-cash contributions
 - Unused amortized deductions (i.e. organization costs)
 - Increase in LP /LLC debt for which partner/member is liable
 - Increase in non-recourse LP /LLC debt (no limitation for qualified debt in real estate, at-risk limitation for other investments)
- 4.5.3.1.8 Factors resulting in a decrease in basis
 - Taxable loss
 - Cash distribution
 - Non-cash distribution
 - Non-deductible, non-capitalized expenses (i.e. 50% of entertainment expenses)
 - Depletion deduction for oil and gas wells
 - Decrease in LP /LLC debt for which partner/member is liable
 - Decrease in non-recourse LP /LLC debt (no limitation for qualified debt in real estate, at-risk limitation for other investments)
- 4.5.3.2 Investment Interest
 - Limitation on annual deduction
 - Net investment income
- 4.5.3.3 Passive loss limitations
 - Losses from a passive activity
 - For limited partners and non-managing members generally only deductible against income from other passive activities
 - Passive losses carried forward but not backward
- 4.5.3.4 "At Risk" limitations on deduction of losses
 - Limited to partner's/member's capital contribution plus a portion of LP/LLC liabilities for which the partner/member is liable
 - Qualified non-recourse financing in real estate is exempt from "At Risk" limitations
- 4.5.3.5 Alternative minimum tax (AMT)
 - Major limit on potential tax benefits to individuals
 - Direct participation program preference items
 - Certain income tax brackets

- 4.6 Retirement Plans**
- 4.6.1 ERISA (Employee Retirement Income Security Act) requirements**
- 4.6.2 Types of retirement plans**
 - 4.6.2.1 Individual retirement account (IRA)
 - Traditional IRA
 - Roth IRA
 - 4.6.2.2 Keogh Plans/HR-10 Plans
 - 4.6.2.3 Corporate pension plans
 - 4.6.2.4 Corporate deferred payment profit sharing plans
 - 4.6.2.5 401(k) plans--cash or deferred arrangements (CODAs)
 - 4.6.2.6 403(b) plans--for employees of non-profit organizations
 - 4.6.2.7 457 plans--for government employees
- 4.6.3 Suitability**
 - Prudent man rules
 - Self-directed or fiduciary directed
- 4.6.4 Rollover issues - maintaining non-taxed status**
- 4.6.5 Unrelated business taxable income --Debt vs. equity**
- 4.6.6 Distributions from qualified plans -- tax effects vary**
- 4.6.7 Rules against self-dealing**

5.0

REGULATION OF DIRECT PARTICIPATION PROGRAMS

5.1 Federal Regulation of Direct Participation Programs

5.1.1 Securities Act of 1933 and SEC Rules Thereunder - Registration of Securities

- 5.1.1.1 Definitions under the Act
 - Section 2(1) - Security
 - Section 2(2) - Person
 - Section 2(3) - Sale or sell; offer
 - Section 2(4) - Issuer
 - Section 2(11) – Underwriter

5.1.2 Form of Offering

- 5.1.2.1 Public programs
 - 5.1.2.1.1 Securities Act of 1933
 - 5.1.2.1.1.1 Form S-1 registration (general securities)
 - 5.1.2.1.1.2 Form S-11 registration (real estate programs)
 - 5.1.2.1.1.3 Form SB-1 registration (small issue registration)
 - 5.1.2.1.1.4 Regulation A – conditional small issues exemption
 - 5.1.2.2 Transactions exempt from registration
 - 5.1.2.2.1 Private offerings
 - 5.1.2.2.1.1 Section 4(2) -- Transactions by an issuer not involving any public offering
 - 5.1.2.2.1.2 Section 4(6) -- Transactions involving offers or sales by an issuer solely to one or more accredited investors up to the Section 3(b) maximum
 - 5.1.2.2.1.3 Regulation D -- Rules governing the limited offer and sale of securities without registration under the Securities Act of 1933
 - 5.1.2.2.1.3.1 Rule 501 -- Definitions and terms used in Regulation D
 - Accredited investor
 - Affiliate
 - Aggregate offering price
 - Number of purchasers
 - Executive officer
 - Issuer
 - Purchaser representative

- 5.1.2.2.1.3.2
 - Rule 502 -- General conditions to be met
 - Integration—6-month safe harbor rule
 - Information requirements
 - When information must be furnished
 - Type of information to be furnished
 - Limitation on manner of offering
 - Limitations on resale
- 5.1.2.2.1.3.3
 - Rule 503 -- Filing of notice of sale
 - Filing Form D
- 5.1.2.2.1.3.4
 - Rule 504 -- Exemption for limited offers and sales of securities not exceeding \$1,000,000
 - Exemption
 - Conditions to be met
 - Limitation on aggregate offering price
- 5.1.2.2.1.3.5
 - Rule 505 -- Exemption for limited offers and sales of securities not exceeding \$5,000,000
 - Exemption
 - Conditions to be met
 - Limitation on aggregate offering price
 - Limitation on number of purchasers
 - Disqualification
- 5.1.2.2.1.3.6
 - Rule 506 -- Exemption for limited offers and sales without regard to dollar amount of offering
 - Exemption
 - Conditions to be met
 - Limitation of number of purchasers
 - Qualifications of purchasers
- 5.1.2.2.1.3.7
 - Rule 507 -- Disqualifying provision relating to exemptions under Rules 504, 505, and 506
- 5.1.2.2.1.3.8
 - Rule 508 -- Insignificant deviations from a term, condition or requirement of Regulation D
- 5.1.2.2.2
 - Intrastate offerings
 - 5.1.2.2.2.1
 - Securities exempt from registration requirements for intrastate offerings
 - 5.1.2.2.2.1.1
 - Section 3(a)(11) -- Any security which is part of an issue offered and sold only to persons resident within a single state or territory
 - 5.1.2.2.2.1.2
 - Rule 147 -- "Part of an issue", "person resident" and "doing business with"
 - Part of an issue
 - Integration of offerings
 - Nature of the issuer
 - Offerees and purchasers; persons resident

Limitation of resales
Precautions against interstate offers and sales

5.2 Communications With the Public

5.2.1 Securities Act of 1933 and SEC Rules Thereunder

- 5.2.1.1 Section 2 -- Definitions under the Act
 - Section 2(8) -- Registration statement
 - Section 2(10) -- Prospectus
 - Rule 134 -- Communications not deemed a prospectus
- 5.2.1.2 Section 5 -- Prohibitions relating to interstate commerce and the mails
 - Rule 135 -- Notice of certain proposed offerings
 - Rule 135A -- Generic advertising
- 5.2.1.3 Section 6 -- Registration of securities and signing of registration statement
 - Regulation C -- Registration
 - Rule 425 -- Statement required in all prospectuses
 - Rule 425A -- Statement required on all prospectus regarding delivery of prospectuses by dealers
- 5.2.1.4 Section 10 -- Information required in Prospectus
 - SEC Guide 4 - Oil and Gas
 - SEC Guide 5 - Real Estate
- 5.2.1.5 Section 11 -- Civil liabilities on account of false registration statement
- 5.2.1.6 Section 12 -- Civil liabilities arising in connection with prospectus and communications

5.3 Federal Regulation of Broker-Dealers

5.3.1 Securities Exchange Act of 1934 and SEC Rules Thereunder

- 5.3.1.1 Section 3 -- Definitions and Application of Titles
 - Section 3(a)(3) -- Member
 - Section 3(a)(4) -- Broker
 - Rule 3a4-1 -- Associated persons of an issuer deemed not to be brokers
 - Section 3(a)(5) -- Dealer
 - Section 3(a)(8) -- Issuer
 - Section 3(a)(9) -- Person
 - Section 3(a)(10) -- Security
 - Section 3(a)(11) -- Equity security
 - Section 3(a)(12) -- Exempted security
 - Section 3(a)(13) -- Buy and purchase
 - Section 3(a)(14) -- Sale and sell
 - Section 3(a)(18) -- Persons associated with a broker or dealer
 - Section 3(a)(24) -- Participant
 - Section 3(a)(26) -- Self regulatory organization
 - Section 3(a)(35) -- Investment discretion
 - Section 3(a)(37) -- Records

Section 3(a)(39) -- Statutory disqualification

- 5.3.1.2 Section 10 -- Regulation of the use of manipulative and deceptive devices
 - 5.3.1.2.1 Rule 10b-1 -- Prohibitions with respect to securities exempted from registration
 - 5.3.1.2.2 Rule 10b-3 -- Employment of manipulative and deceptive devices by brokers or dealers
 - 5.3.1.2.3 Rule 10b-5 -- Employment of manipulative and deceptive devices
False, misleading, or omitted material information
 - 5.3.1.2.4 Rule 10b-9 -- Prohibited representations in connection with certain offerings
Conditions of the underwriting
 - 5.3.1.2.5 Rule 10b-10 -- Confirmation of transactions
Information disclosure requirements
- 5.3.1.3 Section 15(c) -- Registration and regulation of brokers and dealers-- prohibitions and sanctions for fraud
 - 5.3.1.3.1 Rule 15c1-2 -- Fraud and misrepresentation
 - 5.3.1.3.2 Rule 15c1-3 -- Misrepresentation by brokers and dealers as to registration
 - 5.3.1.3.3 Rule 15c1-5 -- Disclosure of control
 - 5.3.1.3.4 Rule 15c2-4 -- Transmission or maintenance of payments received with underwritings
Handling investor funds
Bank escrow requirements
 - 5.3.1.3.5 Rule 15c2-8 -- Delivery of prospectus (to customers); see also Rule 174 under the 33 Act
Preliminary prospectus (red herring)
Effective prospectus
Delivery to associated persons
Delivery to other broker-dealers by managing underwriter
- 5.3.1.4 Section 17 -- Accounts and records, reports, examinations of exchanges, members and others
 - 5.3.1.4.1 Rule 17a-8 -- Financial recordkeeping and reporting of currency and foreign transactions
 - 5.3.1.4.2 Rule 17f-2 -- Fingerprinting of securities industry personnel (general requirement)
- 5.3.1.5 Regulation FD -- Disclosure requirements

5.3.1.6 Regulation S-P – Privacy of consumer financial information

5.4 Insider Trading

5.4.1 Insider Trading and Securities Fraud Enforcement Act of 1988

5.4.1.1 Section 3 -- Civil penalties of controlling persons for illegal insider trading
by controlled persons

5.4.1.2 Section 4 -- Increases in criminal penalties

5.4.1.3 Section 5 -- Liability to contemporaneous traders of insider trading

5.5 Restrictions on Installment Sales for SEC Registered Public Offerings

5.5.1 Regulation T -- Federal Reserve Board Requirements

5.5.1.1 Treated as an extension of credit on a non-marginable security
Not applicable to private offerings

5.5.2 Rule 3a12-9 -- Exemption of certain direct participation program securities from the restrictions regarding the extending or arranging of credit

5.5.2.1 Business development plan

5.5.2.2 Specified property program

5.6 Investment Advisers Act of 1940

5.6.1 Practices which would require registration

5.7 NASD Rules

5.7.1 By-Laws

5.7.1.1 Article I -- Definitions
Branch office
Broker
Dealer
Investment banking or securities business
Person associated with a member

5.7.1.2 Article III -- Qualifications of members and associated persons

5.7.1.3 Article IV – Membership

5.7.1.4 Article V -- Registered Representatives and Associated Persons

5.7.1.5 Article VI -- Dues, Assessments and other charges

5.7.1.6 Article VII -- Board of Governors

- 5.7.1.7 Article IX -- Committees
- 5.7.1.8 Article XII -- Disciplinary proceedings
- 5.7.1.9 Article XIII -- Powers of the Board to prescribe sanctions
- 5.7.1.10 Article XV -- Limitations of powers
 - Section 2 -- Use of name of NASD by members
- 5.7.2 General Provisions**
 - 5.7.2.1 Rule 0110 -- Adoption and application
 - Rule 0115 – Applicability
 - 5.7.2.2 Rule 1020 -- Definitions
- 5.7.3 Membership, Registration and Qualification Requirements**
 - 5.7.3.1 Rule 1020 – Registration of principals
 - Registration requirements
 - Definition of principal
 - Categories of principal registration
 - General securities principal
 - Limited principals
 - 5.7.3.2 Rule 1030 -- Registration of representatives
 - Registration requirements
 - Definition of representative
 - Categories of representative registration
 - General securities representative
 - Limited representative
 - 5.7.3.3 Rule 1060 -- Persons exempt from registration
 - 5.7.3.4 Rule 1070 -- Qualification examinations and waiver of requirements
 - 5.7.3.5 Rule 1080 -- Confidentiality of examinations
 - 5.7.3.6 Rule 1120 -- Continuing education requirements
 - Firm element
 - Regulatory element
- 5.7.4 Conduct Rules**
 - 5.7.4.1 Rule 2110 - Standards of commercial honor and principles of trade
 - 5.7.4.2 Rule 2120 - Use of manipulative, deceptive, or other fraudulent devices
 - 5.7.4.3 Rule 2210 - Communications with the public
 - Definitions
 - Advertisement
 - Sales literature

- Public appearance
- Independently prepared reprint
- Approval and recordkeeping
- Filing requirements and review procedures
- Content standards
 - Standards applicable to communication with the public
 - Standards applicable to advertisements and sales literature
- IM-2210-1 – Guidelines to ensure that communications with the public are not misleading
- IM-2210-4 – Limitations on use of NASD's name

- 5.7.4.4 Rule 2211 - Institutional sales material and correspondence
 - Definitions
 - Correspondences
 - Institutional sales material
 - Institutional investor
 - Existing retail customer
 - Approval and recordkeeping
 - Spot-check procedures
 - Content standards applicable to institutional sales material and correspondence
- 5.7.4.5 Rule 2212 - Telemarketing
- 5.7.4.6 Rule 2230 - Confirmations
- 5.7.4.7 Rule 2240 - Disclosure of control relationship with issuer
- 5.7.4.8 Rule 2250 - Disclosure of participation or interest in primary or secondary distribution
- 5.7.4.9 Rule 2310 - Recommendations to customers (suitability)
- 5.7.4.10 Rule 2330 - Customers' securities or funds
 - Improper use
 - Prohibition against guarantees
 - Sharing in accounts; extent permissible
- 5.7.4.11 Rule 2370 - Borrowing from or lending to customers
- 5.7.4.12 Rule 2420 - Dealing with non-members
 - Transactions with non-members
 - Transactions with foreign non-members
 - Non-member broker or dealer
 - IM-2420 - Transactions between members and non-members
 - Member
 - Expelled dealer
 - Suspended dealer
 - Broker or dealer whose registration is revoked by the SEC
 - Membership resigned or canceled
- 5.7.4.13 Rule 2430 - Charges for services performed

- 5.7.4.14 Rule 2440 - Fair prices and commissions
- 5.7.4.15 Rule 2710 - Corporate financing rule
 - Definitions
 - Filing requirements-public programs
 - Underwriting compensation and arrangements
- 5.7.4.16 Rule 2790 - Restrictions on purchase and sale of initial equity public offerings
 - General prohibitions
 - Preconditions for sale
 - General exemptions
 - Issuer-directed securities
 - Anti-dilution provisions
 - Stand-by purchasers
 - Undersubscribed offerings
 - Definitions
- 5.7.4.17 Rule 2810 - Direct Participation Programs
 - Definitions
 - Requirements
 - Application
 - Suitability
 - Disclosure
 - Organization and offering expenses
 - Valuation for Customer Accounts
 - Participation in rollups
- 5.7.4.18 Rule 3010 - Supervision
 - Supervisory systems
 - Written procedures
 - Supervisory manual
 - Readily accessible and continuously updated
 - Internal inspections
 - Review of transactions and correspondence
 - Qualifications investigated
 - Applicant's responsibility
 - Definitions
 - Office of supervisory jurisdiction
 - Branch office
- 5.7.4.19 Rule 3011 - Anti-money laundering compliance program
- 5.7.4.20 Rule 3030 - Outside business activities
 - Prompt written notice for all outside business activities including registered investment advisers
- 5.7.4.21 Rule 3040 - Private securities transactions (selling away)
 - Applicability to all associated persons of the member
 - Prompt written notice to the employer member
 - Transactions for compensation
 - Transactions not for compensation
 - Definitions

Private securities transaction
Selling compensation

- 5.7.4.22 Rule 3050 - Transactions for or by associated persons
 - Determine adverse interest
 - Obligations of executing member
 - Obligations of associated persons concerning an account with a member
 - Obligations of associated persons concerning an account with an investment adviser, bank, or other financial institution
 - Exemption for transactions in investment company shares and unit investment trusts
- 5.7.4.23 Rule 3060 - Influencing and rewarding employees of others
- 5.7.4.24 Rule 3070 - Reporting requirements
- 5.7.4.25 Rule 3110 - Books and records
 - Requirements
 - Customer account information
 - Record of written complaints
 - "Complaint" defined
 - Requirements when using predispute arbitration agreements with customers
 - Telemarketing requirements
- 5.7.4.26 Rule 3120 - Use of information obtained in fiduciary capacity
- 5.7.5 Procedural Rules**
 - 5.7.5.1 Rule 8000 -- Investigations and sanctions
 - 5.7.5.1.1 Rule 8100 -- General provisions
 - Availability of NASD Manual to customers
 - 5.7.5.1.2 Rule 8200 -- Investigations
 - Provision of information and testimony and inspection and copying of books
 - Suspension for failure to provide requested information
 - 5.7.5.1.3 Rule 8300 -- Sanctions
 - Sanctions for violation of the Rules
 - IM 8310-1 -- Effect of a suspension, revocation, cancellation or bar
 - IM 8310-2 -- Release of disciplinary information
 - Payment of fines, other monetary sanctions, or costs; summary action for failure to pay
 - Costs of proceedings
 - 5.7.5.2 Rule 9000 -- Code of Procedure
 - 5.7.5.2.1 Rule 9100 -- Application and purpose
 - Application
 - Definitions

Service; filing of papers
Proceedings
Recusal or disqualification

- 5.7.5.2.2 Rule 9200 -- Disciplinary proceedings
 - Complaint and answer
 - Request for hearing; extensions of time, postponements, adjournments
 - Appointment of hearing panel, extended hearing panel
 - Pre-hearing conference and submission
 - Discovery
 - Hearing and decision
 - Settlement procedure
 - Contemptuous conduct
- 5.7.5.2.3 Rule 9300 -- Review of disciplinary proceeding by National Adjudicatory Council and NASD Board; application for Commission review
 - Appeal to or review by National Adjudicatory Council
 - Transmissions of record; extensions of time, postponements, adjournments
 - Proceedings
 - Discretionary review by Board
 - Effectiveness of sanctions
 - Application to Commission for review
- 5.7.5.2.4 Rule 9500 -- Suspension, cancellation, bar, denial of access and eligibility procedures
 - Procedures for summary and non-summary suspension, cancellation, bar, limitation or prohibition
 - Eligibility proceedings
- 5.7.5.2.5 Rule 9600 -- Procedures for exemptions
 - Application
 - Decision
 - Appeal
- 5.7.5.3 Rule 10000 -- Code of Arbitration Procedure
- 5.7.5.3.1 Rule 10100 -- Administrative provisions
 - Failure to act under Code of Arbitration Procedure
 - Matters eligible for submission
- 5.7.5.3.2 Rule 10300 -- Uniform Code of Arbitration
 - Required submission
 - Simplified arbitration
 - Designation of number of arbitrators
 - Composition of panel
 - Initiation of proceedings
 - General provisions governing pre-hearing proceedings
 - Awards
- 5.7.5.3.3 Rule 10400 -- Mediation rules

Scope and authority
Submission of eligible matters
Limitation on liability
Mediation ground rules

5.8 State (Blue Sky) Registration and Filing Requirements

**5.8.1 State Regulation of DPP Programs
North American Securities Administrators Association (NASAA)
Statement of Policy**

5.8.2 Exemptions from state registration

5.8.3 Broker-dealer state registration

5.8.4 Registered representative/principal state registration

6.0

FACTORS TO CONSIDER IN EVALUATING DIRECT PARTICIPATION PROGRAMS

6.1 Evaluation of the Direct Participation Program

6.1.1 Economic soundness of program

6.1.2 Basic objectives of program

6.1.3 Value of assets

Cost to general partner

Cost to program

Third party appraisal of property, if applicable

6.1.4 Nature of Assets

Location

Economics of area

Demographics

Climatic conditions

Physical conditions

6.1.5 Principal Risk factors

Investment risk

Business/credit risk

Interest rate risk

Risk of liquidating investment at inappropriate times

Marketability or redeemability of the investment

Tax impact

Management ability

Market risk

Economic, social and political risk

Exchange rate risk

Lack of investment liquidity

Possible loss of principal

Unpredictability of income and expenses

Capability of general partner

Leverage

Competition

6.1.6 Potential conflicts of interest

Competing property interests held by the sponsor and his affiliates

Commingling program funds

Sponsor receives compensation for services rendered at favorable rates

Purchase or sale of property to partnership by general partner

6.1.7 Sponsor and affiliate interest and compensation

6.1.7.1 Organization and offering period

Acquisition and development fees

Other offering and organization fees paid

- Selling compensation
 - Asset mark-ups
 - Cost reimbursement
- 6.1.7.2 Operational period
 - Asset management fees
 - Property management fees
 - Interest in profits, losses and cash distributions (subordinated or non-subordinated)
- 6.1.7.3 Termination period
 - Disposition fee
 - Cost reimbursement
 - Carried interest in gain, loss and cash distribution (subordinated or non-subordinated)
- 6.1.8 Sponsor's track record**
 - Review data from sponsor's previous programs to determine experience in the type of program being offered
 - Success ratio versus type of program
- 6.1.9 Sources of offering proceeds**
 - Capital contributions
 - Installment or staged payments
 - Letters of credit
 - Loans
 - Assessments (additional capital contributions)
- 6.1.10 Use of offering proceeds**
 - 6.1.10.1 Offering proceeds less offering and organization (front-end load) expenses equals amount available for investment
 - 6.1.10.2 Types of offering and organization expenses
 - Underwriting compensation (sales and wholesaling fees)
 - Due diligence fees
 - Advisory fees (legal, accounting, consulting, investor relations, etc.)
 - Direct costs (printing, mailing, administrative, etc.)
 - 6.1.10.3 Amounts of offering and organization expenses paid to sponsor and affiliates
 - 6.1.10.4 Limits on offering and organization expenses in public programs
 - 6.1.10.5 Indeterminate compensation adjustments on underwriting compensation
 - 6.1.10.6 Use of amount available for investment

- Acquisition of assets
 - Reimbursement of prepayments for loans, options, advisory fees, administrative costs--amounts paid to sponsor and affiliates
 - Acquisition fees (real estate commissions) -- amounts paid to sponsor and affiliates
 - Net cash to acquire assets
- Working capital reserve

6.1.11

Anticipated cash flow

- Payments to investors
- Automatic re-investment plan
- Preferred returns
- Guaranteed returns
- Subordinated returns
- Cumulative returns
- Sharing ratio(s)

6.1.12

Anticipated returns on investments

- Analyze elements of return before and after taxes
- Examine tax factors by year over life of the investment
- Methods of calculating return and present value (time value of money)
 - Internal rate of return
 - Discounted cash flows

6.2

Investor Suitability

6.2.1

Recommendation to Customers (Suitability/Know your customer)

- Financial status
- Tax status
- Tax identification number or social security number
- Investment objectives
- Ability to commit money for long periods (illiquidity)
- Financial ability to lose the amounts invested
- Purchaser representative requirements
- Risk tolerance

6.2.2

Investor's understanding of the direct participation program

- Ability to understand risks of the underlying investment
- Lack of liquidity and marketability

6.2.3

Alternative investment products -- appropriateness for investors, given the investor's investment objectives and risk-taking profile

- Treasury bills
- Money market funds
- Short-term government bond funds
- Intermediate government bond funds
- Long-term government bond funds
- Municipal securities
- Corporate securities
- Real-estate investment trusts
- Aggressive growth funds
- Speculative stocks
- Option trading

SAMPLE QUESTIONS

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

1. In a joint venture, a venturer has liability that is equivalent to the liability of
 - (A) a limited partner
 - (B) a general partner
 - (C) a shareholder in a C corporation
 - (D) a shareholder in an S corporation

2. Which of the following is TRUE of a partner in a general partnership?
 - (A) He cannot participate in management without jeopardizing his status.
 - (B) He has limited liability.
 - (C) He has personal liability for obligations of the partnership.
 - (D) He is not responsible to creditors of the partnership beyond the subscription amount.

3. When calculating the cash flow from a residential property, which two of the following items must be considered?
 - I. The amount of the rent received.
 - II. The amount of cash expenses paid to operate the property.
 - III. The amount of cash expenses less depreciation.
 - IV. The amount of all amortized items.
 - (A) I and II
 - (B) I and IV
 - (C) II and III
 - (D) III and IV

4. Each of the following is true of a public limited partnership offering EXCEPT
 - (A) The offering must be filed with the SEC and NASD.
 - (B) The offering may be advertised in securities industry magazines.
 - (C) The number of accredited investors is limited to 35.
 - (D) The offering may be made in more than one state.

ANSWERS TO SAMPLE QUESTIONS

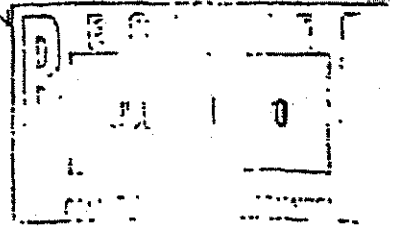
1. (B)
2. (C)
3. (A)
4. (C)

Exhibit 3c
SR-NASD-2006-082



DIVISION OF
MARKET REGULATION

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



July 24, 2000

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

Re: Procedure for Filings Relating to Qualification Examinations

Dear Mr. Adkins: *Alden*

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

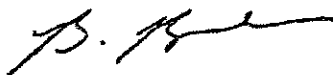
The Division has decided that it is no longer necessary for SROs to file new exam question banks for Commission approval under Section 19(b)(2). In the future, any new examinations should be filed as non-controversial rule changes for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Exchange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

Alden S. Adkins
Page 2

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

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

Sincerely,



Belinda Blaine
Associate Director