Direct Participation
Programs Limited Principal
Qualification Examination
(Test Series 39)

Study Outline

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STUDY OUTLINE

DIRECT PARTICIPATION PROGRAMS
LIMITED PRINCIPAL QUALIFICATION EXAMINATION
(SERIES 39)

The FINRA Direct Participation Programs Limited Principal (Series 39) Qualification Examination (hereinafter called the DPP Principal) is designed to test a candidate's knowledge of the rules and statutory provisions applicable to the management of a broker-dealer which limits its securities business to these products.

This study outline has been prepared to assist FINRA member firms in preparing candidates to sit for the Series 39 exam. It may be used to structure or prepare training materials, develop lecture notes and seminar programs, and as a training aid for candidates themselves. This outline and the exam are divided into three topical sections listed below, along with the percentage of each section’s representation in the overall exam.

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The Series 39 exam is composed of 100 multiple-choice items covering all of the materials in the following outline in accordance with the subject-matter distribution shown above. Candidates will be allowed 135 minutes to complete the exam. A candidate must correctly answer 70 percent of the items to receive a passing grade.

The exam is a closed-book test and candidates will not be permitted to use any reference material during their testing session. White boards/dry erase markers and a basic electronic calculator will be provided by the test center administrator. Severe penalties are imposed on candidates who cheat on securities industry qualification exams.

Exam items are updated regularly to reflect the most current interpretations of the rules and regulations. Items on new rules will be added to the pool of items for this exam within a reasonable period of their effective dates.

At the end of this outline are four sample items written in the various formats used in the actual Series 39 exam. The samples do not mirror the difficulty level of actual test items or the subject matter distribution of the test itself. Their use is merely to familiarize the candidate with the style of multiple-choice items used in the Series 39 exam.

Information about qualifications exams may be found at:
Please Note: Candidates are responsible for keeping abreast of changes made to the applicable rules and regulations, as the exam is updated when new rules are introduced and/or amended.
1.0

STRUCTURE AND REGULATION OF DIRECT PARTICIPATION PROGRAM OFFERINGS

1.1 Direct Participation Program Offering Practices

1.1.1 Types of underwriting commitments

1.1.1.1 Best efforts
   Contingent
   All or none
   Mini-Max

1.1.1.2 Firm commitment

1.1.2 Syndication practices

1.1.2.1 Managed offerings

1.1.2.1.1 Selling group manager

1.1.2.1.2 Soliciting dealer

1.1.2.1.3 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

1.1.2.1.4 Sponsor-managed offerings
   Each dealer enters into agreement directly with program sponsor
   Dealers are paid directly by the program sponsor

1.1.2.2 Role of wholesalers
   Individuals or member firms paid to retain selected dealers or soliciting dealers for the offering
   Interface between issuer and broker-dealers and their sales force
   Dealer Manager or Sponsor may utilize outside or unaffiliated wholesalers
   All wholesaling compensation and expenses are underwriting compensation subject to the 10% limitation

1.1.2.3 Compliance requirements for wholesaling
   Registered individuals acting in wholesaling capacities or functions must be supervised by the firm
Member firms and their registered individuals engaged in wholesaling activities may cause a member to be deemed an underwriter, and subject to underwriter’s liability.

Wholesaling compensation and expenses are items of compensation and must be run through the member firm’s books.

Registration of wholesaler
Member firms must ensure compliance with non-cash compensation guidelines and training and education restrictions.

1.1.2.4 Due diligence
The exercise of reasonable care to determine that the offering disclosures are accurate and complete.

Public offerings--statutory defense available (Section 11(c) or (d))
Private offerings--helps avoid fraud charges
Must be performed by broker-dealers making the offering.

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

1.1.2.5 Finders

1.1.2.5.1 Defined as un-registered introducer

1.1.2.5.2 Prohibited practices
Sales compensation to non-members of a national securities exchange or association registered with the SEC
Referrals by non-members of individual clients to broker-dealers in exchange for compensation

1.1.3 Subscription practices

1.1.3.1 Signature pages of partnership documents
Purchaser representations
Liquidity
Marketability
Suitability

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

1.1.3.3 Sales are conditioned upon acceptance of subscribers

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

1.1.4 Securities Exchange Act of 1934 and SEC Rules Thereunder

1.1.4.1 Handling investor funds

1.1.4.1.1 Rule 15c2-4--Transmission and maintenance of payments received in underwritings
Movement of investor funds between the broker-dealer and escrow agent

1.1.4.2 Conditions of the underwriting

1.1.4.2.1 Rule 10b-9--Prohibited representations in connection with certain offerings

1.2 Underwriting Compensation

1.2.1 Types of compensation

1.2.1.1 Cash

1.2.1.2 Non-cash

1.2.1.3 Indeterminate
Carried interest/continuing compensation
Other securities

1.2.2 Limits on sales compensation in public offerings

1.2.2.1 Limited to amount stated in offering document

1.2.2.2 Limit applies to individual and aggregate sales

1.2.2.3 10% of gross dollar amount of securities sold in public offerings; plus up to .3% for reimbursement of bona fide due diligence expenses

1.2.2.4 15% of proceeds for organization and offering expenses

1.2.2.5 Sharing commissions

1.3 Communications with the public

1.3.1 Securities Act of 1933 and SEC Rules Thereunder

1.3.1.1 Section 2--Definitions under the Act
Section 2(8)--Registration statement
Section 2(10)--Prospectus
   Rule 134--Communications not deemed a prospectus

1.3.1.2 Section 5--Prohibitions relating to interstate commerce and the mails
   Rule 135--Notice of certain proposed offerings
   Rule 135A--Generic advertising

1.3.1.3 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

1.3.1.4 Section 10--Information required in prospectus
   SEC Guide 4--Oil and gas
   SEC Guide 5--Real estate

1.3.1.5 Section 11--Civil liabilities on account of false registration statement

1.3.1.6 Section 12--Civil liabilities arising in connection with prospectus and communications

1.3.2 Securities Exchange Act of 1934 and SEC Rules Thereunder

1.3.2.1 Rule 15c2-8--Delivery of prospectus (to customers)
   Preliminary prospectus (red herring)
   Effective prospectus
   Delivery to associated persons
   Delivery to other broker-dealers by managing underwriter

1.3.3 FINRA Conduct Rules

1.3.3.1 Communications with the Public Rules
   FINRA Rule 2210--Communications with the Public
   FINRA Rule 2214--Requirements for the Use of Investment Analysis Tools

1.3.3.2 FINRA Rule 3230--Telemarketing
1.4 Registration of Securities and Exemptions from Registration

1.4.1 Securities Act of 1933 and SEC Rules Thereunder

1.4.1.1 Section 2--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

1.4.1.2 Section 17--Fraudulent interstate transactions

1.4.1.3 Section 23--Unlawful representations

1.4.2 Form of Offering

1.4.2.1 Public programs

1.4.2.1.1 Securities Act of 1933
   Form S-1 registration (general securities)
   Form S-11 registration (real estate programs)
   Form SB-1 registration (small issue registration)
   Regulation A--Conditional small issues exemption

1.4.2.1.2 FINRA Rules
   FINRA Rule 5110--Corporate financing rule-underwriting terms and arrangements
   Definitions
   Filing requirements for public programs
   Underwriting compensation and arrangements

   FINRA Rule 2310--Direct participation programs
   Definitions
   Requirements
   Application
   Suitability
   Disclosure
   Organization and offering expenses
   Valuation for customer accounts
   Participation in rollups

1.4.2.2 Transactions exempt from registration

1.4.2.2.1 Private offerings

1.4.2.2.1.1 Section 4(a)(2)--Transactions by an issuer not involving any public offering
1.4.2.2.1.2 Section 4(6)--Transactions involving offers or sales by an issuer solely to accredited investors
1.4.2.1.3 Regulation D--Rules governing the limited offer and sale of securities without Registration under the Securities Act of 1933

1.4.2.1.3.1 Rule 501--Definitions and terms used in Regulation D
- Accredited investor
- Affiliate
- Aggregate offering price
- Number of purchasers
- Executive officer
- Issuer
- Purchaser representative

1.4.2.1.3.2 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

1.4.2.1.3.3 Rule 503--Filing of notice of sale
- Filing Form D

1.4.2.1.3.4 Rule 504--Exemption for limited offers and sales of securities not exceeding $5,000,000
- Exemption
  - Conditions to be met
    - General conditions
    - Specific conditions
    - Limitation on aggregate offering price

1.4.2.1.3.6 Rule 506--Exemption for limited offers and sales without regard to dollar amount of offering
- Exemption
  - Conditions to be met
    - Limitation on number of purchasers
    - Nature of purchasers

1.4.2.1.3.7 Rule 507--Disqualifying provision relating to exemptions under Rules 504, 505, and 506

1.4.2.1.3.8 Rule 508--Insignificant deviations from a term, condition or requirement of Regulation D

1.4.2.2 Intrastate Offerings

1.4.2.2.1 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
1.4.2.2.2 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

Rule 147A--Exemptions to facilitate intrastate and regional securities offerings

1.4.3 State (Blue Sky) registration and filing requirements

1.4.3.1 Pre-emption of certain state securities regulations by the National Securities Market Improvement Act (NSMIA)

1.4.3.2 State regulation of DPP programs
   - North American Securities Administrators Association (NASAA) Statement of Policy

1.4.3.3 Exemption from state registration

1.4.3.4 Broker-dealer state registration

1.4.3.5 Branch office registration

1.4.3.6 Registered representative/principal state registration
2.0

SALES SUPERVISION; GENERAL SUPERVISION OF EMPLOYEES;
REGULATORY FRAMEWORK OF FINRA

2.1 Securities Exchange Act of 1934 and SEC Rules Thereunder

2.1.1 Section 3 Definitions

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Section 3(a)(4) -- Broker
   Rule 3a4-1--Persons 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

2.1.2 Section 10--Regulation of the use of manipulative and deceptive devices

2.1.2.1 Rule 10b-1--Prohibitions with respect to securities exempted from registration

2.1.2.2 Rule 10b-3--Employment of manipulative and deceptive devices by brokers or dealers

2.1.2.3 Rule 10b-5--Employment of manipulative and deceptive devices
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2.1.2.4 Rule 10b-10--Confirmation of transaction
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2.1.3.4 Section 15(c)(1)--Manipulative, deceptive or fraudulent devices or contrivances

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2.1.5 Regulation FD--Disclosure requirements

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Broker
Dealer
Investment banking or securities business
Person associated with a member

2.5.1.2 Article III--Qualifications of members and associated persons

2.5.1.3 Article IV--Membership

2.5.1.4 Article V--Registered representatives and associated persons

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2.5.2 General Provisions

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Rule 0140--Applicability

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2.5.3 Membership, Registration and Qualification Requirements

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FINRA Rule 1122--Filing of misleading information as to membership or registration

2.5.3.2 FINRA Rule 1100 -- Member Application

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Registration requirements
Definition of principals

2.5.3.4 FINRA 1220 -- Registration Categories
Registration requirements
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2.5.3.5 FINRA Rule 1230--Persons exempt from registration

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2.5.4 FINRA Conduct Rules

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2.5.4.4 FINRA Rule 2262--Disclosure of control relationship with issuer

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2.5.4.6 FINRA Rule 2267--Investor education and protection

2.5.4.7 FINRA Rule 2090--Know Your Customer
   FINRA Rule 2111--Suitability

2.5.4.8 FINRA Rule 3240--Borrowing from or lending to customers

2.5.4.9 FINRA Rule 2040--Payments to Unregistered Persons
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2.5.5.2 Rule 9000—Code of procedure

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2.5.5.2.2 Rule 9200—Disciplinary proceedings
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2.6.2 Types of retirement plans

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2.6.7  Distributions from qualified plans - tax effects vary
3.0

COMPLIANCE WITH FINANCIAL RESPONSIBILITY RULES

3.1 Securities Exchange Act of 1934 and SEC Rules Thereunder

3.1.1 Rule 15c3-1--Net capital requirements

3.1.1.1 Minimum net capital requirements

3.1.1.1.1 Broker-dealers engaging in a general securities business

- Aggregate indebtedness to net capital ratio not to exceed 800% during first 12 months of operation; 1500% thereafter
- Minimum net capital of $250,000

3.1.1.1.2 Broker-dealer who do not receive customer funds or securities and do not carry customer accounts--$5,000 minimum net capital requirement

- Introducing broker-dealers
- Broker-dealers participating in underwritings on a "best efforts" or "all or none" basis
- Broker-dealers which promptly forward subscriptions for securities to the issuer, underwriter or distributor
- Broker-dealers effecting occasional transactions for their own investment accounts

3.1.1.2 Aggregate indebtedness

3.1.1.2.1 Definitions

3.1.1.2.2 Exclusions from aggregate indebtedness

3.1.1.3 Net capital

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3.1.1.3.4 Securities haircuts--for proprietary accounts

3.1.1.3.5 Debt-equity requirements

3.1.2 Rule 15c3-3 Customer Protection--reserve and custody of securities

3.1.2.1 Exemptions

3.1.2.1.1 (k)(2) exempt broker-dealers
3.1.2.1.1 (k)(2)(i) broker-dealers
No margin accounts
Promptly transmits all customer funds and securities

3.1.3 Rule 17a-3--Records to Be Made by Brokers and Dealers

3.1.3.1 Proof of money balances of all ledger accounts
Trial balances computed at least once per month
Record of computation of aggregate indebtedness
Record of computation of net capital

3.1.3.2 Questionnaire or application for employment executed by each
"associated person" approved in writing by an authorized representative
of the broker-dealer
Definition of an "associated person"

3.1.3.3 Fingerprint records required to be maintained pursuant to SEC Rule 17f-2(d)

3.1.4 Rule 17a-4--Records to be Preserved by Certain Exchange Members, Brokers and Dealers

3.1.4.1 Records to be preserved for not less than six years, the first two years in a readily accessible place
Ledgers or other records reflecting in all broker-dealer’s assets and liabilities, income and expense and capital accounts
Ledger accounts or other records itemizing separately required information per Rule 17a-3 as to each account

3.1.4.2 Records to be preserved for not less than three years, the first two years in a readily accessible place
All check books, bank statements, canceled checks and cash reconciliations
All bills receivable or payable
Originals of all communications received and sent
All guarantees of accounts, powers of attorney and other evidence granting discretionary authority and resolutions empowering an agent to act on behalf of a corporation
All written agreements entered into by a broker-dealer relating to his business as such records containing the following information in support of amounts included in Focus Part II-A reports and in audited financial statements required by Rule 17a-5
Detail of all items which are charged or credited in the computation of net capital

3.1.4.3 Customer account records (including subscription documents and questionnaires) for a period of six years after the closing of such account

3.1.4.4 Partnership articles or articles of incorporation of charter, minute books and stock certificate books for the life of the enterprise and of any
successor enterprise

3.1.4.5 The following records with respect to associated persons:
   Employment applications until at least three years after such person has terminated employment
   Fingerprint records pursuant to Rule 17f-2 until at least three years after such person has terminated employment

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   Availability of and facilities for viewing such records
   Efficiency of index and filing system
   Facilities to provide facsimile enlargements
   Separate storage of duplicate file

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3.1.7.1 Requirements for broker-dealer whose net capital is less than the required minimum net capital under Rule 15c3-1

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3.1.7.3 Requirement for broker-dealers who fail to make and keep current the books and records specified in Rule 17a-3

3.1.7.4 Requirement for broker-dealer who discovers or is notified by an accountant, pursuant to Rule 17a-5, that material inadequacies in its accounting system exist

3.1.7.5 Transmittal of required notices and reports

3.2 Securities Investor Protection Act and SIPC Rules Thereunder

3.2.1 Membership requirements of SIPC

3.2.2 Protection of customers

3.2.2.1 Determination of need for protection

3.2.3 SIPC Rules

3.2.3.1 Prohibited acts
   Embezzlement of SIPC assets

3.2.3.2 Advertising by members of SIPC protection

3.3 FINRA Rules

3.3.1 FINRA CONDUCT RULES

3.3.1.1 FINRA Rule 2261 – Disclosure of financial condition

3.3.1.2 FINRA Rule 2150 – Improper use of customers’ securities or funds; prohibition against guarantees and sharing in accounts
   Improper use
   Prohibition against guarantees
   Sharing in accounts; extent permissible

3.3.1.3 FINRA Rule 3310 – Anti-money laundering compliance program
   Bank Secrecy Act
3.3.1.4  FINRA Rule 3120 – Supervisory Control Systems

3.3.1.5  FINRA Rule 3130 – Annual certification of compliance and supervisory processes

3.3.1.6  FINRA 4360 – Fidelity Bonds

3.3.1.7  Books and Records

- FINRA Rule 2268 - Requirements When Using Predispute Arbitration Agreements for Customer Accounts
- FINRA Rule 4511 - General Requirements
- FINRA Rule 4512 - Customer Account Information
- FINRA Rule 4513 - Records of Written Customer Complaints

3.3.1.8  FINRA Rule 1020--Approval of change in exempt status under SEC Rule 15c3-3

- Loss of 15c3-3(k) exemption when member conducts business that will disqualify it from the exemption without the prior written approval of the Association

3.3.1.9  FINRA Rule 4370 – Business Continuity Plan and Emergency Contact Information

3.4  Proprietary Accounts of Broker-Dealers (PAB)

3.4.1  Required computations

- Net capital
- Customer reserve
- Segregation of introducing broker-dealer accounts
- Frequency of calculations

3.4.2  Required written agreements
SAMPLE ITEMS

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

1. Under FINRA rules, which of the following documents must a member firm make available for inspection by its customers?

   (A) the most recent balance sheet **
   (B) the most recent FOCUS Report
   (C) the most recent income statement
   (D) the most recent net capital computation

2. A FINRA member in a public offering of a direct participation program may receive commissions from all of the following except:

   (A) an FINRA member.
   (B) a non-member wholesaling organization. **
   (C) directly from the program sponsor.
   (D) the dealer-manager.

3. Which two of the following types of electronic communications require written approval prior to dissemination?

   I. An email sent to an individual
   II. An email sent to 50 prospective retail customers
   III. Personal communications sent to a chat room
   IV. Communications posted on the firm’s website

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

4. 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