

SECTION 1: RULES FOR REGISTERED PERSONS

1a. REGISTRATION OF PERSONNEL

An obligation of FINRA membership is to register "associated persons." FINRA requires that all principals and defined representatives become registered.

Principals are the officers of the firm and managers of other registered persons. The 4 main principal licenses are:

**Series #24
General Principal**

Series #24: The "General Securities Principal" for officers of FINRA member firms and supervisors of Series #7 licensed individuals. In addition, a Series #24 license is needed to approve communications with the public. Also note that the Series #24 does not license an individual to supervise options.

**Series #27
Financial And
Operations Principal**

Series #27: The "Financial and Operations Principal" for the supervisor of the firm's accounting and financial reporting; and the overall supervisors of back office operations.

**Series #4
Registered Options
Principal**

Series #4: The "Registered Options Principal" for the supervisor of options transactions and approval of options communications.

**Series #9/10
Branch Office Manager
Limited Principal**

Series #9/#10: The BOM or Branch Office Manager license, also called the Sales Supervisor license. This is a limited principal license that allows supervision of all branch functions. This license also covers supervision of options and municipal transactions in a branch.

FINRA has other limited principal designations specific to certain types of securities (e.g., an investment companies limited principal), but this information is not important for the exam.

**Definition Of
Registered Rep**

FINRA requires that each representative be registered. A representative is defined as any person who solicits or conducts business in securities for the member. The 2 main representative licenses are the:

**Series #7
General Securities
Representative**

Series #7: The "General Securities Representative" licenses an individual to sell all types of securities.

**Series #6
Investment Companies
Representative**

Series #6: The "Limited Representative - Investment Company and Variable Contracts Products Representative" is a simpler test than the #7, and is used by insurance companies and mutual fund companies to license individuals only to sell their mutual funds and variable annuity products.

FINRA has other limited representative designations specific to certain types of securities (e.g., a direct participation programs representative), but this information is not important for the exam.

In addition, the NASD (now FINRA) has expanded the definition over the years as different scandals unfolded.

**NASDAQ Traders
Must Register**

**Series #7 And
Series #55 OTC Equity
Trader Exams**

In the mid-1990's, when NASDAQ was a phone-based trading system, the Justice Department tapped the phones and discovered, to its shock and horror, that the NASDAQ traders were colluding with each other to artificially widen spreads and threatening (with bodily harm) any traders at other firms that did not comply. The case was settled for \$1 billion (big dollars at the time), but the upshot was that the market was cleaned-up and computerized. Also, the NASD was quite embarrassed that it did not even know who the traders were - since they were not required to be registered! Hence, the NASD (now FINRA) required that all NASDAQ traders be registered and pass both the Series #7 and the Series #55 OTC Equity Trader licensing exams.

**Research Analysts
Must Register**

**Series #7 And
Series #86/87
Research Analyst
Exams**

In the year 2000, another scandal unfolded involving research analysts. Research analysts were discovered to be involved in huge conflicts of interest, especially making recommendations of companies that their employer-member firms were underwriting (this was the heyday of the Internet Bubble). The analysts were either being paid big dollars at the direction of the broker-dealers' underwriting departments to write "favorable" research reports on the companies being underwritten; or they were being threatened with being fired if they did not produce favorable reports. Of course, until this point, there was no registration of research analysts. A big settlement fine was paid by the underwriting firms involved; Information Barriers (IBs) were put in place between research and underwriting; and research analysts now had to register and pass both the Series #7 and the Series #86/87 Research Analyst licensing exams.

**Back Office Supervisors
Must Register**

Series #99 Exam

In late 2008, the Bernie Madoff Ponzi scheme was exposed, where his investors lost about \$20 billion of real invested money and they also "lost" another \$30 million of phantom profits. You probably know that Bernie pleaded guilty and got 150 years in jail. However, you probably didn't know that Bernie was able to keep the scheme going by having a small group of his "back office" personnel create bogus trade confirms and account statements, along with the required computerized accounting systems to support the sham. He kept these people apart from the legitimate Madoff trading operation, and paid them excessively. And, of course, these people were not registered! Now you know the real reason why you are taking this (the Series #99) test! So aside from making his investors miserable, Bernie was able to do the same to you!

**Persons Who Do
Not Have To Register**

Finally, persons whose duties are solely clerical or who solely handle exempted securities do not have to register. Please note that foreign associates who deal exclusively outside the U.S. do not have to be registered.

**State Blue Sky
Registration Laws**

Also note that aside from Federal registration with FINRA, the state "blue sky" laws require that officers and salespersons be registered in each state where they conduct business. Because Series #99 licensed individuals are not soliciting securities business in a state, they do not fall under the state licensing laws (whereas a Series #7 or Series #6 licensed representative does).

**U-4 Form
Uniform Securities
Application**

To register as either representative or principal, a U-4 (Uniform Securities Application) must be completed and filed with FINRA. Registration continues with the firm unless that person leaves the firm. Any individual may be denied registration if he or she is subject to "statutory disqualification" as specified in the Securities Exchange Act of 1934.

**Reasons For Denying
Registration
Application**

FINRA, under the "statutory disqualification" requirement, will reject the registration application if it finds that the person who wishes to associate with that firm:

has been suspended or expelled from any other Self Regulatory Organization, either domestic or foreign (e.g., if a futures broker is expelled by the NFA - National Futures Association - that individual cannot enter the securities business by registering with FINRA).

is the subject of an SEC order suspending or revoking registration.

by his conduct while associated with a firm has caused that firm's suspension or expulsion.

willfully filed a false or misleading application or has omitted to state material facts in the application.

has been convicted of any securities or "money" related misdemeanor, or any felony, within the past 10 years. Therefore, if you are good for 10 years and 1 day after being convicted, you can become registered again!

has been temporarily or permanently enjoined from engaging in the securities business.

**Wait Period
If Exam Is Failed**

Registration is not effective until the appropriate exam(s) are passed. If an individual fails an exam, 30 days must elapse before a new attempt is permitted. If an individual fails the same exam 3 successive times, a reattempt is not permitted until 180 days elapse. If the individual fails in any additional reattempt, another 180 days must elapse before another attempt is permitted.

**Exam Content
Is Confidential**

Also note that FINRA explicitly states that exam content is confidential. It is prohibited for any person who takes an exam to divulge the content of that exam to anyone else. FINRA can (and will) take disciplinary action against any individual that divulges exam content; any individual that uses such information when taking an exam; and their supervisors.

**Information
On U-4 Form**

Information required on the U-4 Form includes:

Applicant's Name and Address;

Broker-Dealer Name and Address;

Name and Address of "Old" Broker-Dealer if the registrant is transferring from another firm;

5 Year Consecutive Residence History;

10 Year Consecutive Employment History;

Any Other Businesses In Which The Registrant Is Currently Engaged;

Any Other Names By Which The Registrant Is Known;

Disclosure By The Applicant Of Any Arrest, Conviction, Charge, involving investments, fraud, bribery, forgery, etc.;

Disclosure By The Applicant of Any Felony Charge or Conviction; and Any Misdemeanor Charge or Conviction Involving Money, Securities, Theft, Perjury, etc. (Examples of misdemeanors that are not reported include DUIs (but felony DUIs are reported), traffic offenses, assault and battery, and failure to file income tax returns);

Disclosure By The Applicant (If Already Or Previously Registered) Of Any Customer Complaint Settled For More Than \$15,000;

Disclosure By The Applicant Of Any Customer Complaint Alleging A Sales Practice Violation Lodged Against That Individual In An Arbitration or Civil Fraud Proceeding (note that this disclosure, added in 2009, is required before the case is heard, decided, or settled).

Changes - Prompt Amendment

If any of this information changes, the U-4 filing must be amended promptly.

Note that the U-4 questionnaire asks about arrests, convictions, etc., to see if the applicant will be subject to "statutory disqualification." The questionnaire asks about convictions for "any felony," which would include such things as Driving Under the Influence (DUI), possession of a controlled substance, assault, or manslaughter.

Individuals Convicted Of Non-Securities Felonies Can Be Registered

The SEC permits the SRO (e.g., FINRA) to approve these individuals who have such "Other Felony" convictions on a case-by-case basis. Approval is based on the proposed supervision of the person applying for registration, any subsequent disciplinary actions after the event that caused statutory disqualification and the overall merits of the case. The basic question behind the review is this: "Is this person a risk to investors?"

If Omit Information Or Lie On U-4, Then Cannot Be Registered And Can Be Prosecuted

If an individual omits information or lies on the U-4, this will usually be picked up when the background check is performed. At a minimum, this individual will not be allowed to be registered; and in addition, giving false or misleading answers can make that individual subject to civil or criminal penalties.

Principal Verifies Prior 3 Year's Employment History

For a new registration, the principal must sign and date the U-4 Form, and must verify the prior 3 year's employment history. For an amendment to a registration, the principal simply signs and dates the form. Also note that as part of the employment verification, the principal must ascertain the "good character and business reputation" of the applicant.

**Dual
Registration
Permitted If
Disclosed On
U-4 Form**

Concurrent registration with 2 or more different broker-dealers is prohibited in many states, but other states allow this. To be "dual" registered, an individual must disclose the name of each broker-dealer on the U-4 Form. Of course, that person must also obtain approval of his employer to work for the other firm.

**CRD - Record Of
Disciplinary Actions**

Each registered person's U-4 information record is maintained on file at "CRD" - the Central Registration Depository. Any disciplinary action taken against a registered person is part of the U-4 information and is recorded in that person's file.

**FINRA BrokerCheck
Website**

FINRA maintains a website called "BrokerCheck" where the general public can get information on a broker or member firm. The website uses the U-4 and U-5 information to give the registrant's:

**Broker's Employment
History
Broker's Licenses**

10-year employment history, both in and outside the securities industry, taken from the U-4 Form; securities licenses and state registration(s);

**Broker's Complaint
And Disciplinary
Record**

disciplinary record, which includes both complaints and allegations that have not yet been resolved; as well as a record of any disciplinary or settlement actions taken.

Regarding the fact that unresolved customer complaints and allegations are included, FINRA used to exclude this information, but took "heat" for this, so it is now included. They, do, however, include a disclaimer that this information does not automatically indicate wrongdoing!

Specifically excluded from the BrokerCheck record, due to privacy concerns, is the U-4 information on residence history, social security number and physical characteristics, such as a representative's height, weight, hair color and eye color. (This is the information that is used by law enforcement to find a registered person they wish to arrest, and it could be used by a public customer that wishes to stalk or harm a registered representative.)

BrokerCheck includes information on both representatives that are currently working in the securities industry and representatives that have left the business. It allows the public to get a profile of each member firm, with its disciplinary record. This file also includes previously registered member firms that have shut their doors.

If a customer does not have web access, the BrokerCheck information is available from a FINRA toll-free phone number.

**BrokerCheck
Notice To
Customer**

When a customer account is opened, FINRA Rule 2280 requires that the customer be provided with the:

BrokerCheck toll-free number;

BrokerCheck mailing address; and the

FINRA website address.

In addition, the customer must be given notice of an available BrokerCheck brochure. There is no disclosure of a FINRA "800" number required. A logical question is: "Why no disclosure of the BrokerCheck website address?" The answer is the FINRA does not own it! It was grabbed by someone else and, probably, FINRA does not want to pay an extortionate amount of money for it. The only way to get to the real BrokerCheck is through the FINRA website, which is why their web address must be given.

**Continuing
Education
Requirements**

FINRA imposes continuing education requirements ("CE") for all registered persons who deal with customers.

There is a 2 part requirement:

**2nd Anniversary Of
Registration / Every
3 Years Thereafter**

Regulatory Element: Requires that a computerized training session that reviews various regulations and procedures be completed on the registrant's 2nd anniversary of registration and every 3 years thereafter.

**If Regulatory Element
Is Not Completed,
License Is "Inactive"
Without Pay**

If the Regulatory Element is not completed within the required time period (120 days of notice from CRD to the named contact person via the FINRA Contact System), that person's registration is suspended (inactive) until it is completed. During the suspension, this person cannot perform any of the functions of a registered representative and this person cannot be paid (giving him or her a very good incentive to complete the training).

Annual Training

Firm Element: Requires that an annual training plan be prepared and implemented by member firms to cover relevant products, regulations, and compliance issues.

**If Called For
Military Duty Then
Registration
Becomes "Inactive"
But Can Be Paid**

If a registered representative is called-up or volunteers for active military duty, FINRA classifies that person as being "inactive" and their CE obligations (both Regulatory and Firm elements) are suspended. The employing broker-dealer must send a letter to CRD (the Central Registration Depository, which keeps all registration and disciplinary information on registered individuals) giving the registered representative's name and CRD number and the

date the firm received notification of the call-up from the representative.

**Upon Return,
Registration Status
Resumes At Same
Point As It Was Left**

Once the representative is discharged from military service, a copy of the discharge notice must be sent to CRD so that the individual can resume active registered status, basically starting from the point where he left off. FINRA has stated that it makes no difference if the individual returns to his or her "old" broker-dealer or if they associate with another broker-dealer upon return to civilian life - FINRA will reactivate that person's registration status.

**Can Return To
Another
Broker-Dealer**

**Can Have Another
Broker At Same
Firm Service
Clients And Share
Commissions**

Also note that the firm can pay the individual while he or she is on military duty, including payments for commissions earned prior to being called-up for military service. While that individual is away in the military, he or she can arrange for another representative at the same firm to service his or her customers and can share commissions with that representative.

**Must Reassociate
Within 90 Days**

Finally, FINRA requires that individual to reassociate with a member firm within 90 days of return to civilian life, otherwise registration with that member is terminated.

**U-5 Form
Termination Of
Registration - File
Within 30 Days**

If a person is terminated, a U-5 form must be filed with FINRA within 30 days of termination. In addition, a copy of the U-5 must be made available to the terminated individual. The person's registration is not reinstated until another firm registers that individual through a new U-4.

**If New Employer
Requests U-5 From
A New Employee -
Must Be Provided
Within 2 Business
Days**

If a person who has left a member firm associates with another member; and the new member requests a copy of that individual's U-5 form from the new employee; the new employee must provide a copy of the U-5 to the new employer within either:

2 business days of the request if the U-5 has been obtained from the ex-employer; or

2 business days of receipt from the ex-employer.

(Note: With the advent of "Web-CRD," a member firm can get the U-5 Form electronically once it is available and does not need to get it from the representative. However, this "old" rule is still on the books and still can be tested.)

**Amend The U-5
Filing Within 30
Days Of Discovery
For Subsequently
Discovered
Information**

If information becomes known about the individual that was not included on the U-5 filing (such as, the member firm discovers 8 months after an individual was terminated, that he or she was doing a little embezzling), the member must amend the U-5 filing within 30 days. This obligation to amend U-5 filings for subsequently

discovered information is an ongoing obligation that has no cut-off date.

**After 2 Years, Must
Requalify By Exam**

After 2 years without being associated with a firm, that person must requalify by taking the appropriate exam(s).

**"Hanging" Licenses
Is Prohibited**

FINRA explicitly prohibits an individual from "hanging" his or her license with a broker-dealer to keep registration current (and therefore not having to retake exams) after leaving the business.

**FINRA Retains
Jurisdiction For 2
Years If Terminated**

Once a person is terminated, if a customer complaint is filed, FINRA retains jurisdiction over that person for 2 years. Also, please note that FINRA does not permit termination of registration via a U-5 if there is any complaint or action being taken against that person. Only **after** the issue is resolved does the U-5 take effect, and the 2 year period starts counting.

**"Reportable
Events"**

FINRA requires that the member firm file a written report if it appears that the firm itself, or an associated person, has gotten into trouble. Note that these reports are required as the event is happening - even if there is no proof or conviction. FINRA assesses the severity of the information in the report in order to decide whether it needs to take further action.

**Notify FINRA
Promptly But
No Later Than 30
Days After Event**

FINRA requires that it be notified in writing promptly, but no later than 30 calendar days, after the member firm knows or should have known, if the firm itself or any registered employee is:

found to have violated any provision of any securities law;

subject of a written customer complaint alleging theft, misappropriation of funds, or forgery;

named as a defendant or respondent in any legal proceeding alleging violations of the Securities Acts brought by a regulatory authority;

denied registration or is expelled, suspended, or disciplined by any self regulatory organization;

indicted, convicted, or pleads guilty to any criminal offense (except for misdemeanor traffic violations and misdemeanor DUIs);

associated with any broker-dealer, investment company, investment advisor, or insurance company which was suspended, expelled or had its registration denied; or which was convicted of, or pleaded no contest, to any felony or misdemeanor;

a defendant or respondent in any securities or commodities related civil litigation or arbitration settled for an amount exceeding \$15,000 (this limit is raised to \$25,000 if the settlement involved that member firm itself);

subject to statutory disqualification, as listed on page 3 of this section;

the subject of disciplinary actions by their firm involving suspension, termination, withholding of commissions, or imposition of fines in excess of \$2,500.

In addition, the rule requires that each member firm report to FINRA under the same time frame if the member firm has concluded that an associated person, or the firm itself, has violated any securities-, insurance-, commodities-, financial- or investment-related law - either domestic or foreign.

1b. INITIAL PUBLIC OFFERINGS (IPOs)

FINRA Rule 5130 is designed to insure that new issue securities that are "in demand" are not withheld from sale to the public by member firms who intend to "keep" these shares for their own or their employees' benefit, since the price is likely to rise in the aftermarket.

Industry Insiders Prohibited From Buying Common Stock IPOs

The rule prohibits member firms or their associated persons from selling a new common stock issue to any account owned by a "restricted person" or to any account in which a "restricted person" has a beneficial interest.

Persons Restricted From Buying IPOs

The "restricted persons" who are prohibited from buying IPOs of common stock are broadly defined into 3 groups:

FINRA Member Firms, Officers, Employees And Immediate Family

1. Member firms for their own accounts, officers of member firms, associated persons, or any other employee of a member firm are restricted. Also prohibited are "agents" of broker-dealers; and immediate family members of the officers and employees of broker-dealers.

Immediate Family - One Up; One Down; One Over

"Immediate family" is anyone that is 1 step removed from that officer or employee and includes spouses, siblings, parents, and children, as well as in-laws of these individuals and any individual to whom the broker-dealer employee provides material support.

**Fiduciaries And
Finders To FINRA
Member Firms**

2. Fiduciaries to member firms are restricted, such as lawyers, accountants and financial consultants who provide services to member firms. Also note that this prohibition applies to the immediate family of lawyers, accountants, and financial consultants for the underwriter.

Portfolio Managers

3. Portfolio managers who have authority to buy or sell securities for institutional investors are restricted. These individuals are typically investment officers of banks, savings and loans, insurance companies, investment companies, investment advisors or collective investment accounts. Also restricted are the immediate family members of these individuals.

The bottom line is that these "industry insiders" are prohibited from buying common stock IPOs from underwriters (and since you will now be registered, you fall into this category as well!). To insure compliance with the rule, FINRA requires that any purchaser of a common stock IPO:

**Initial Positive
Affirmation**

Sign a letter that he or she is not prohibited and this must be retained by the member firm. This is called a "positive affirmation;" and

**Annual Negative
Affirmation Thereafter**

Annually thereafter, the member firm must recertify that this person is not prohibited. This can be done by sending a "negative affirmation" to the client, which is an annual letter stating that: "We have you on record as not being prohibited from buying IPOs. If anything has changed, let us know."

1c. CONDUCT RULES

The FINRA Conduct Rules govern the relationship between member firms and customers; and associated persons and customers. The overriding theme is that customers must be treated fairly and equitably.

**Cannot Guarantee
Customer Against
Loss**

A registered representative is prohibited from guaranteeing a customer's account against loss. Note that repurchase agreements, where the underlying securities are exempt, are not considered to be a prohibited guarantee against loss. However, if a repurchase agreement uses non-exempt securities (such as common stock) as the underlying collateral, this is a violation.

**Cannot Share In
Gain/Loss Of
Customer Account
Unless "At Risk"**

A registered representative is prohibited from sharing in the gain and loss of a customer account. However, registered representatives are allowed to open joint accounts with customers with written approval of the employer. FINRA requires that, in such accounts, profit and loss be shared in direct proportion to the capital contributed. (This is actually a good customer relations idea, because the customer knows that the representative will enjoy the same gains as the customer (or the same losses), so the customer knows that the registered representative's interests are aligned with those of the customer.

**Must Share In
Proportion EXCEPT
For Immediate Family
Member Account**

An exception to the "sharing in direct proportion to capital invested" requirement is given to accounts of the immediate family of associated persons. Immediate family for this requirement is defined as parents, children, spouses, in-laws, or any person supported by the member.

**Cannot Lend
To Or Borrow From
A Customer Unless
Immediate Family
Member Or
Lending Institution**

A registered representative cannot borrow money from a customer; nor can he or she lend money to a customer. However, this rule does not apply if the customer is a member of the registered representative's immediate family (such as a husband working at a broker-dealer as a registered representative and his wife having her own individual account at that broker-dealer - the rep can borrow money from the wife or lend money to the wife at will). The prohibition also does not apply if the customer is a lending institution.

**If Firm Approves,
Can Lend To Or
Borrow From
"Significant Others"**

The rule then goes on to permit, but **only** with prior approval of the member firm, lending or borrowing between:

2 representatives at the same member firm;

a representative at a member firm and a customer with whom the representative has a personal relationship (e.g., a representative and her "live-in" boyfriend); and

a representative at a member firm and a customer with whom the representative has a business relationship.

Gift Limit = \$100

Registered representatives are prohibited from giving or accepting gifts valued in excess of \$100 per person per year, where the gift is related to their activities as a broker.

Note that the gift limit does not preclude business entertainment as long as this is not too excessive or too frequent.

Business Entertainment Is Not Subject To The \$100 Gift Limit

For example you can take a customer to dinner and spend \$300 at a high-end restaurant; you cannot give a customer a \$300 gift certificate to his or her favorite high-end restaurant.

Firm Must Have Written Policies Covering Entertainment

FINRA has implemented a rule requiring member firms to create written policies and procedures covering business entertainment. The member firm must train its employees about these procedures; and must audit employee expenses for compliance.

The gift limit also does not apply to gifts based upon a personal relationship rather than a business relationship. For example, if a registered representative is invited to the wedding of a friend who happens to be registered or is a customer, he or she can give a wedding present valued at over \$100.

Record Of Gifts

FINRA requires that member firms keep a record of all gifts and gratuities given or received by associated persons that are related to the firm's business. Thus, all gifts given and received must be reported to the member firm and must be recorded. The firm must have procedures to aggregate the value of gifts to see if the \$100 limit is breached over the course of a year. Records of gifts must be retained by the member firm for 3 years.

Consider the following scenario: A registered representative gives a gift of \$1,000 to a customer. The member firm learns of this, and when the representative is asked what is going on, he replies: "It wasn't a gift - I hired the customer to mow my lawn on weekends and I am paying for work."

Paying For Work Is Permitted

The gift limit does not prohibit an associated person from paying someone to work as long as:

There is a written agreement spelling out the work to be performed and the compensation to be paid.

The agreement is approved in writing by the principal of the firm before it takes effect.

So in this scenario, the representative has violated the rule because he or she did not follow these procedures.

If such an agreement is made, the firm is obligated to keep a separate record of such agreement, with any payments made, for 3 years.

**Outside Work -
Registered Rep.
Must Notify Firm**

FINRA prohibits registered persons from being employed by anyone other than the member firm, unless he or she provides prompt written notice to the member and follows any instructions of the employer.

**Cannot Share In
Commissions With
An Unregistered
Person**

FINRA prohibits registered persons from sharing in, or paying commissions to, another person that is not registered. For example, a registered representative cannot share in commissions with an unregistered sales assistant. On the other hand, a registered representative could share in commissions with a registered sales assistant, as long as the member firm is given written notice of the arrangement and any instructions of the member firm are followed.

**"Selling Away" Is
Prohibited**

**Cannot Do "Private"
Securities Trades**

If a registered representative handles a securities transaction for a customer through another firm, this is a prohibited practice known as "selling away." FINRA prohibits such "private securities transactions." As a general rule, all trades that a registered representative handles must either be executed through the firm or be known to the firm.

**Exception To
Prohibition On
Private Securities
Trades**

An exception to this general prohibition is granted if the firm is given prior written notice of the proposed transaction and compensation to be received and the firm specifically approves of the transaction in writing. The firm is then obligated to supervise the transaction as if it were taking place through the member.

**Disputes Handled
Through Binding
Arbitration**

FINRA requires that any disputes between registered representatives and their firms be handled by binding arbitration (with the sole exception of employment discrimination claims, including sexual harassment), which cannot be appealed. Customer disputes may be handled through the arbitration process only if the customer consents. Consent is given when the customer signs a Predispute Arbitration Agreement upon opening the account.

**Mediation Is An
Alternative To
Arbitration**

Because FINRA has a 3-year backlog of arbitration cases, it offers a voluntary alternative to speed things up - mediation. Both parties must agree to mediate the dispute and neither party can be compelled to use mediation. In contrast to arbitration, the decision of the mediator is not binding and either side can pull out and return to arbitration at any time.

Approval Of Correspondence

Regarding correspondence sent by registered representatives to customers relating to the investment banking or securities business of the firm, the basic rule is that all correspondence must be approved in advance by a manager or principal. This applies not only to written correspondence, but also to e-mails and IMs. Correspondence is defined as a communication to fewer than 25 existing or prospective customers within a 30-day time window.

The requirement for manager approval does not really work well in a world of electronic communications, and FINRA includes in the rule a way to deal with this. If the firm implements a communications compliance program that trains representatives regarding what is permitted and what is prohibited in these communications; and the firm audits these communications for compliance; then prior written principal approval is not required. Instead, post-use review and approval is permitted.

Retain Both Business And Personal Communications

Also note that correspondence is a record that must be retained for 3 years (including e-mails and IMs). Furthermore, because associated persons are often given a separate business cell phone by their employer (who can then make sure that all communications are retained and reviewed) and most people use their cell phones for both personal and business communications without distinguishing between them, all such communications by registered persons must be reviewed and retained by the member firm!

Sales Literature

Communications to 25 or more existing or prospective clients are defined as "sales literature." This reaches a defined broader audience. Sales literature also includes speeches about investing and password-protected websites. Sales literature must be approved, in advance of use, by a Series #24 General Principal.

Advertising

Communications seen by the general public are defined as "advertising." This includes TV, radio, newsprint, websites that are not password protected, etc. Advertising must be approved, in advance of use, by a Series #24 General Principal.

Use Of FINRA Name

The FINRA name can be used on advertising and sales literature. If it is used, it must state that the firm (not the individual associated with the firm) is a FINRA member; and if it is used on a member firm's or associated person's website, the FINRA name must be hyperlinked to the FINRA website.

1d. CUSTOMER COMPLAINTS

Written Customer Complaints

A customer complaint is defined as one that is received in writing, and this would also include complaints received by e-mail, as well as IMs. If a registered person receives such a complaint, the associated person cannot attempt to resolve the complaint by him- or herself.

All Complaints Resolved Under Supervision Of Principal

All written complaints must be resolved under the supervision of a manager or principal. The OSJ (Office of Supervisory Jurisdiction) must keep a copy of all complaints received with their resolution status. This record must be retained for 4 years (this is the only record that is retained for this time period).

Keep 4 Years

Escalation Procedures

This means that all complaints received must be "escalated" to the next level for resolution by a manager. If the manager is incapable of resolving the complaint to the customer's satisfaction, the complaint must be "escalated" again to the firm's compliance department for an attempted resolution. The record of all of these escalation procedures must be part of the complaint file.

Thus, the firm's WSPs (Written Supervisory Procedures) must make provision for these so-called escalation procedures. Part of the WSPs is that any complaint received by the firm that is not directed to a specific person must be sent to the firm's compliance department for resolution.

For example, if a customer complaint is directed to the firm's operations department stating that there are erroneous positions on the account statement, this cannot be resolved by someone in operations **UNLESS** the complaint is escalated to compliance and compliance oversees the resolution.

The reason is simple - the source of the erroneous positions might be the operations department; or it might be the registered representative servicing the account. Either would have the incentive to make sure that the complaint gets buried and is not reported. By escalating to compliance, the appropriate compliance officer can determine the facts of the complaint and can alter the firm's policies and procedures as needed to "fix" the root cause of the error.

1e. MSRB POLITICAL CONTRIBUTIONS

Rule G-37

This rule was approved by the SEC in mid-1994, and was written in response to some municipal "scandals" that occurred at the time. For example, the firm of Lazard Freres, in New York City, was one of the city's underwriters. (The city sells most of its issues through negotiated underwritings.) Lazard Freres gave a "loan" of \$125,000 to the primary campaign of a candidate for mayor of New York City.

When this was "discovered," the candidate argued that this would in no way result in her favoring Lazard Freres in future underwritings, if she were elected mayor. She lost the election, mainly due to the public's perception that this was a "payoff" - restoring our faith in the political system.

Contributions By Municipal Firms To Elected Officials' Campaigns Is Prohibited

When the news broke, the SEC told the MSRB to "Do something!" Rule G-37 is the result. It prohibits municipal dealers from engaging in municipal securities business with an issuer within 2 years after any contribution is made to an elected official of that issuer by:

The municipal dealer;

A municipal finance professional ("MFP") associated with the dealer; or

A Political Action Committee ("PAC") controlled by the municipal dealer or MFP associated with the dealer.

Associated Persons That Deal With Individual Customers Are Not MFPs

The term "municipal finance professional" refers to any associated person who solicits municipal securities business - however, individuals who solicit business from "natural persons" are excluded. This means that regular registered representatives who deal with individual customers are not MFPs.

Generally, MFPs Deal With Issuers

In essence, an MFP is an associated person who solicits business from municipal issuers, renders financial advisory services to municipal issuers, or who performs research or writes reports on municipal issues. However, most firms apply the rule as a blanket prohibition to all registered personnel.

Rule Only Applies To Negotiated Underwritings And Advisory Services

The term "municipal securities business" only applies to negotiated underwritings (as managing underwriter or syndicate member), financial advisory services, and private placements.

**Does Not Apply To
Competitive Bid
Underwritings**

It does not apply to competitive bid underwritings, since there is no way for a municipal dealer to exert influence (by making political contributions) over the selection of the winning bidder.

The term "contribution" includes any gift, loan, advance, or deposit of any money, for the purpose of:

Influencing the election of any official of an issuer;
Paying or reducing debt incurred in connection
with any election; and

Paying transition or inaugural expenses incurred
by a successful candidate for office.

The rule cannot be circumvented by making payment through someone not on the prohibited list; nor can it be circumvented by making payment to someone affiliated with the candidate (instead of to the candidate directly).

**Contributions Of
Up To \$250 Per
Election Permitted
Only If Donor Is
Eligible To Vote**

Contributions of up to \$250 or less, **per election**, are exempt from the rule, and thus are permitted. This "de minimis" exemption only applies to contributions made by MFPs eligible to vote for such official of the issuer (that is, they are registered to vote in that official's district).

Also note that annual contributions of up to \$250 per political party in a State or political subdivision in which an MFP is entitled to vote are permitted as well. Otherwise, the exemption is not available.

**Political
Contribution That
Exceeds Limit Will
Result In That Member
Firm Being Banned
For 2 Years From
Being That Issuer's
Underwriter**

To summarize, if an MFP makes a contribution:

of any size to an issuer official for whom the MFP is not entitled to vote; or

of more than \$250 to an issuer official for whom the MFP is entitled to vote; then

the firm would be prohibited from engaging in municipal securities business with that issuer for 2 years from the contribution date.

**2 Year Ban Travels
With MFP If He Or
She Moves To
Another Firm**

Also note that this prohibition carries over if the MFP joins another municipal firm.

For example, if an MFP at municipal dealer "A" makes a contribution resulting in a 2 year prohibition; and less than 2 years later, joins municipal dealer "B;" both firms are subject to the prohibition until the end of the 2 year period.

Similarly, if a person not associated with a municipal firm makes a contribution to an issuer official; and within 2 years, that person joins a municipal firm as an MFP; that firm would be subject to a prohibition which would end 2 years from contribution date.