



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

**Study Outline**

## 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.

Section	Description	Number of Items
1	Structure and Regulation of Direct Participation Program Offerings	46
2	Sales Supervision; General Supervision of Employees; Regulatory Framework of FINRA	32
3	Compliance with Financial Responsibility Rules	22
<b>Total</b>		<b>100</b>

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:

<http://www.finra.org/industry/qualification-exams>

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 best interest/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
    - 1.1.4.3 Rule 151-1—Regulation Best Interest
    - 1.1.4.4 Rule 17a-14—Form CRS, Form CRS, for Preparation, Filing and Delivery of Form CRS
- 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



- 1.4.2.2.1.3 Regulation D--Rules governing the limited offer and sale of securities without Registration under the Securities Act of 1933
  - 1.4.2.2.1.3.1 Rule 501--Definitions and terms used in Regulation D
    - Accredited investor
    - Affiliate
    - Aggregate offering price
    - Number of purchasers
    - Executive officer
    - Issuer
    - Purchaser representative
  - 1.4.2.2.1.3.2 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
  - 1.4.2.2.1.3.3 Rule 503--Filing of notice of sale
    - Filing Form D
  - 1.4.2.2.1.3.4 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
  - 1.4.2.2.1.3.6 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
      - Nature of purchasers
  - 1.4.2.2.1.3.7 Rule 507--Disqualifying provision relating to exemptions under Rules 504, 505, and 506
  - 1.4.2.2.1.3.8 Rule 508--Insignificant deviations from a term, condition or requirement of Regulation D
- 1.4.2.2.2 Intrastate Offerings
  - 1.4.2.2.2.1 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

- 1.4.2.2.2.2 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**

Section 3(a)(3) -- Member

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  
False, misleading, omitted material information

2.1.2.4 Rule 10b-10--Confirmation of transaction  
Disclosure requirements

##### **2.1.3 Section 15--Registration and regulation of brokers and dealers - Prohibitions and sanctions for fraud**

2.1.3.1 Section 15(a)(1)--Prohibition relating to unregistered broker-dealers

2.1.3.2 Section 15(b)(4)--Sanctions against brokers or dealers

- 2.1.3.3 Section 15(b)(6)--Sanctions for persons associated with brokers or dealers
- 2.1.3.4 Section 15(c)(1)--Manipulative, deceptive or fraudulent devices or contrivances
  - 2.1.3.4.1 Rule 15c1-1--Definitions
  - 2.1.3.4.2 Rule 15c1-2--Fraud and misrepresentation
  - 2.1.3.4.3 Rule 15c1-3--Misrepresentation by brokers and dealers as to registration
  - 2.1.3.4.4 Rule 15c1-5--Disclosure of control
- 2.1.4 Section 17--Accounts and records, reports, examination of exchange members and others**
  - 2.1.4.1 Rule 17f-2--Fingerprinting of securities industry personnel (general requirements)
- 2.1.5 Regulation FD--Disclosure requirements**
  - 2.1.5.1 Rule 100--General rule regarding selective disclosure
  - 2.1.5.2 Rule 101--Definitions
- 2.1.6 Regulation S-P--Privacy of consumer financial information**
- 2.2 Insider Trading**
  - 2.2.1 Insider Trading and Securities Fraud Enforcement Act of 1988**
    - 2.2.1.1 Section 3--Civil penalties of controlling persons for illegal insider trading by controlled persons
    - 2.2.1.2 Section 4--Increases in criminal penalties
    - 2.2.1.3 Section 5--Liability to contemporaneous traders for insider trading
- 2.3 Restrictions on Installment Sales for SEC Registered Public Offerings**
  - 2.3.1 Federal Reserve Board Requirements under Regulation T**
    - 2.3.1.1 Treated as an extension of credit on a non-marginable security  
Not applicable to private offerings
    - 2.3.1.2 SEC Rule 3a12-9--Exemption of certain direct participation programs from the restrictions regarding extending or arranging of credit  
Business development plan

Specified property program

**2.4 Investment Advisers Act of 1940**

**2.4.1 Practices which would require registration**

**2.5 FINRA Rules**

**2.5.1 By-Laws**

2.5.1.1 Article I--Definitions

Branch office

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

2.5.1.5 Article VI--Dues, assessments and other charges

Schedule A (general knowledge of types of income assessed and fees levied)

2.5.1.6 Article VII--Board of governors

2.5.1.7 Article IX--Committees

2.5.1.8 Article XII--Disciplinary proceedings

2.5.1.9 Article XIII--Powers of board to impose sanctions

2.5.1.10 Article XV--Limitation of powers

Section 2--Use of name of the corporation by members

**2.5.2 General Provisions**

2.5.2.1 FINRA Rule 0110--Adoption of rules

Rule 0140--Applicability

2.5.2.2 FINRA Rule 0160--Definitions in FINRA By-Laws

**2.5.3 Membership, Registration and Qualification Requirements**

2.5.3.1 FINRA Rule 1210 – Registration Requirements

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

2.5.3.2 FINRA Rule 1100 – Member Application

2.5.3.3 FINRA Rule 1220 –Registration Categories

Registration requirements

Definition of principals

2.5.3.4 FINRA 1220 –Registration Categories

Registration requirements  
Definition of representative

2.5.3.5 FINRA Rule 1230--Persons exempt from registration

2.5.3.6 FINRA Rule 1210--Qualification examinations and waiver of requirements

2.5.3.7 FINRA Rule 1210--Confidentiality of examinations

2.5.3.8 FINRA Rule 1240--Continuing Education Requirements  
1240 (a) Regulatory Element  
1240 (b) Firm Element

## **2.5.4 FINRA Conduct Rules**

2.5.4.1 FINRA Rule 2010--Standards of commercial honor and principles of trade

2.5.4.2 FINRA Rule 2020--Use of manipulative, deceptive or other fraudulent devices

2.5.4.3 FINRA Rule 2232--Customer Confirmations

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

2.5.4.5 FINRA Rule 2269--Disclosure of participation or interest in primary or secondary distribution

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  
Transactions with non-members  
Transactions with foreign non-members  
Non-member broker or dealer

2.5.4.10 FINRA Rule 2122--Charges for services performed

2.5.4.11 FINRA Rule 2121--Fair prices and commissions

2.5.4.12 FINRA Rule 5130 -- Restrictions on the 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

- 2.5.4.13 FINRA Rule 3110--Supervision
  - Supervisory System
  - Written Procedures
  - Inspection Requirements
  - Transaction Review and Reporting
  - Branch Office and OSJ Definitions
- 2.5.4.14 FINRA Rule 3270--Outside business activities of registered persons
- 2.5.4.15 FINRA Rule 3280--Private securities transactions of an associated person
  - Applicability to all associated persons of member
  - Prompt written notice to employer member
  - Transactions for compensation
  - Transactions not for compensation
  - Definitions
    - Private securities transaction
    - Selling compensation
- 2.5.4.16 FINRA 3210 - Accounts At Other Broker-Dealers and Financial Institutions
  - Determine adverse interest
  - Obligations of executing member
    - Notice to employer member
    - Transactions effected for personnel of other members
  - 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 trust

- 2.5.4.17 FINRA Rule 3220--Influencing or rewarding employees of others
- 2.5.4.18 FINRA Rule 2060--Use of information obtained in a fiduciary capacity

## **2.5.5 FINRA Rules**

- 2.5.5.1 Rule 8000--Investigations and sanctions
  - 2.5.5.1.1 Rule 8100--General provisions
    - Rule 8110--Availability of manual to customers
    - Rule 8120--Definitions

- 2.5.5.1.2 Rule 8200--Investigations
  - Rule 8210--Provision of information and testimony and inspection and copying of books
- 2.5.5.1.3 Rule 8300--Sanctions
  - Rule 8310--Sanctions for violation of the rules
  - Rule 8311--Effect of a suspension, revocation, cancellation or bar
  - Rule 8313--Release of disciplinary complaints, decisions and other information
  - Rule 8320--Payment of fines, other monetary sanctions, or costs; Summary action for failure to pay
  - Rule 8330--Costs of proceedings
- 2.5.5.2 Rule 9000--Code of procedure
  - 2.5.5.2.1 Rule 9100--Application and purpose
    - Rule 9110--Application
    - Rule 9120--Definitions
    - Rule 9130--Service; filing of papers
    - Rule 9140--Proceedings
    - FINRA Rule 9160--Recusal or disqualification
  - 2.5.5.2.2 Rule 9200--Disciplinary proceedings
    - Rule 9210--Complaint and answer
    - Rule 9220--Request for hearing; extensions of time, postponements, adjournments
    - Rule 9230--Appointment of hearing panel, extended hearing panel
    - Rule 9240--Pre-hearing conference and submission
    - Rule 9250--Discovery
    - Rule 9260--Hearing and decision
    - Rule 9270--Settlement procedure
    - Rule 9280--Contemptuous conduct
  - 2.5.5.2.3 Rule 9300--Review of disciplinary proceeding by National Adjudicatory Council and FINRA Board; Application for SEC Review
    - Rule 9310--Appeal to or review by National Adjudicatory Council
    - Rule 9320—Transmission of records; extensions of time, postponements, adjournments
    - Rule 9340--Proceedings
    - Rule 9350--Discretionary review by FINRA Board
    - Rule 9360--Effectiveness of sanctions
    - Rule 9370--Application to SEC for review
  - 2.5.5.2.4 Rule 9500—Other proceedings
    - Rule 9520 - Eligibility proceedings
  - 2.5.5.2.5 Rule 9600—Procedures for exemptions
    - Rule 9610 -- Application
    - Rule 9620 -- Decision
    - Rule 9630 -- Appeal



- 2.5.5.3 Rule 12000 and 13000 Series—Code of Arbitration Procedure for Customer/Industry Disputes
  - 2.5.5.3.1 Part I—Interpretive Material, Definitions, Organization and Authority
    - IM-12000 and IM-13000—Failure to Act Under Provisions of Code of Arbitration Procedure for Customer/Industry Disputes
    - 12105 and 13105—Agreement of the Parties
    - 13200—Required Arbitration
  - 2.5.5.3.2 Part II—General Arbitration Rules
    - 12200—Arbitration Under an Arbitration Agreement or the Rules of FINRA
    - 12201—Elective Arbitration
  - Part VIII—Simplified Arbitration and Default Proceedings
    - 12800 and 13800—Simplified Arbitration
    - 12801 and 13801—Default Proceedings
- 2.5.5.3.3 Rule 14000 – Code of Mediation Procedure
  - Rule 14104 – Mediation under the Code
  - Rule 14105 – Effect of mediation on arbitration proceedings
  - Rule 14109 -- Mediation ground rules

## **2.6 Retirement Plans**

### **2.6.1 ERISA (Employee Retirement Income Security Act)**

### **2.6.2 Types of retirement plans**

- 2.6.2.1 IRA
  - Traditional
  - Roth
- 2.6.2.2 Keogh/HR10
- 2.6.2.3 Corporate pension plans
- 2.6.2.4 Corporate deferred payment profit sharing plans
- 2.6.2.5 401(k) plans -- cash or deferred arrangements (CODA's)  
403(b) plans -- for employees of non-profit organizations  
457 plans -- for government employees

### **2.6.3 Suitability**

- 2.6.3.1 Prudent man rules standards
- 2.6.3.2 Self-directed or fiduciary directed

### **2.6.4 Rollover issues - maintaining non-taxed status**

- 2.6.5**                    **Unrelated business taxable income**
- 2.6.5.1                 Debt vs. equity
- 2.6.6**                    **Prohibited transactions**
- 2.6.6.1                 Self-dealing
- 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

###### 3.1.1.3.1 Adjustments to net worth

###### 3.1.1.3.2 Subordinated liabilities

###### 3.1.1.3.3 Assets not readily convertible into cash

###### 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

- 3.1.2.1.1.1 (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
- 3.1.4.6 Preservation of required records on microfilm or optical storage technology
  - Availability of and facilities for viewing such records
  - Efficiency of index and filing system
  - Facilities to provide facsimile enlargements
  - Separate storage of duplicate file
- 3.1.4.7 Applicability of preservation requirements to firms ceasing to transact a securities business
- 3.1.4.8 Outside service bureaus
- 3.1.5 Rule 17a-5--Reports to be Made by Brokers and Dealers (FOCUS Reports)**
- 3.1.5.1 Filing of monthly and quarterly reports
  - Quarterly filings of FOCUS Part IIA--non-clearing, non-carrying broker-dealers
  - Requirement for Direct Participation Programs broker-dealers
  - Filings specifically required by SEC or designated examining authority
- 3.1.5.2 Annual filing of audited financial statements
- 3.1.5.3 Nature and form of reports
- 3.1.5.4 Accountants
- 3.1.5.5 Audit objectives
- 3.1.5.6 Extent and timing of audit procedures
- 3.1.5.7 Accountant's reports
  - Responsibilities of broker-dealers and accountants
- 3.1.5.8 Accountant's report on material inadequacies
- 3.1.5.9 Extensions and exemptions
- 3.1.5.10 Notification of change of fiscal year
- 3.1.5.11 Filing requirements

- 3.1.6 Rule 17a-8--Reporting of currency and foreign transactions and financial recordkeeping**
- 3.1.7 Rule 17a-11--Supplemental current financial and operational reports to be made by brokers and dealers**
  - 3.1.7.1 Requirements for broker-dealer whose net capital is less than the required minimum net capital under Rule 15c3-1
  - 3.1.7.2 Requirements for broker-dealers to send prompt notice after the occurrence of specified events
  - 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 Pre-dispute 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