



FINRA Establishes Qualification Rules for Investment Banking Professionals

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FINRA Establishes Qualification Rules for Investment Banking Professionals

FINRA has adopted a new category for investment banking professionals – Limited Representative-Investment Banking (“Series 79”). The new Rule 1032(i) will become effective 90 days after FINRA announces development of a qualification examination for this category.

Responding to concerns that current FINRA licensing qualification requirements represent a barrier for highly qualified professionals to become associated with securities firms to perform investment banking services, FINRA has created a special limited license category. This means that qualified professionals who choose to focus on investment banking transactions will no longer be required to take a Series 7 examination. The Series 7 examination covers a broad range of industry activities in which investment bankers seldom, if ever, become engaged *e.g.*, retail customer solicitation and sales, trading, etc. To become Series 79 qualified, a candidate will be required to pass an examination focusing on the job functions she or he is likely to perform.

Definition: Investment Banking. The functions covered by the new rule include:

(A) Public/Private Offerings. Advising on or facilitating debt or equity securities offerings through a private placement or public offering. Such services would include but not be limited to origination, underwriting, marketing, structuring, syndication, pricing, allocation and stabilization activities for such offerings. This definition includes those working on equity and debt capital markets and syndicate desks.

(B) Issuer Transactions. Advising on or facilitating mergers and acquisitions, tender offers, financial restructurings, asset sales, divestitures or other corporate reorganizations or business combination transactions. The scope of such covered activities includes but is not limited to rendering fairness, solvency and similar opinions. The Series 79 registration will not be available to persons whose investment banking work is limited to public (municipal) finance offerings.

(C) Exempt Activities. Associated persons would not be required to become Series 79 registered if their activities are limited to areas covered by other Limited Representative categories:

- Direct Participation Programs. Advising on or facilitating the placement of direct participation program securities.¹ Persons engaged exclusively in this activity must be qualified by Series 22 examination.
- Private Securities Offerings. Persons effecting sales of private placements.² Those persons must be qualified by Series 82 examination.

¹ See FINRA Rule 1022(e)(2) for full definition.

² See FINRA Rule 1022(h)(1).

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- Equity Trader. Persons effecting retail or institutional sales and trading activities must be qualified by Series 7 and Series 55 or Series 62 examination.³

(D) Six Month Grace Period - New Employee Training. Associated persons participating in a firm's new employee training program will not be required to become Series 79 qualified for up to six months from the time they first engage in investment banking activities. Firms must evidence the details of their training programs and identify trainees whose activities would require Series 79 registration. Trainees have up to two years from hire date to get registered. Thus, trainees involved in other firm activities could qualify to engage in investment banking activities during the final six months of a two year training program.

(E) Effectiveness. FINRA is developing a qualification examination designed to "provide a more targeted assessment of competency of investment banking personnel to perform their unique job functions."⁴ The SEC must approve the new exam and corresponding fees for the Series 79 category. The new rule will become effective 90 days after that process is completed. Thus, the rule will probably not become effective until late Fall 2009 or early in 2010.

(F) General Principal Requirements. To serve as a General Principal for investment banking activities an individual must obtain the Series 79 registration. The individual will be required to qualify by taking the Series 79 examination or opting – into registration under "grandfathering" provisions, (*see* Transition and Grandfathering). Individuals wishing to participate in broader securities-related activities than those covered by the new rule will be required to take other appropriate examinations, *e.g.*, Series 7 or Series 62.

(G) Transition and Grandfathering. It appears that, FINRA's ultimate goal is to establish a specific additional qualification requirement for all investment banking staff members. Following a transition time of six months after the new rule is implemented, all investment banking professionals will be required to successfully complete the Series 79 examination.⁵ Currently, investment bankers need only pass the Series 7 exam to be fully qualified. General principals supervising investment banking activities are currently required to satisfy Series 7 and 24 requirements.

³ See FINRA Rules 1032(f) and 1031.

⁴ See SEC Rel. No. 34-59484 (April 13, 2009), Federal Register at 10317 (April 21, 2009).

⁵ To allow firms time to establish training programs, FINRA will allow Series 79 candidates who are in the process of qualifying in the new category when it becomes effective to take either the Series 7 or the new Series 79 exam when the exam is available. This accommodation will be in place for six months after the implementation date.

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Once the new Rule has been effective for six months, any individual holding a Series 7 registration that wishes to engage in the covered investment banking activities would be required to pass the Series 79 exam.

(H) Implications for Unregistered Finders – Broker-Dealer Lite Proposal. A recurring issue in the capital-raising process arises when unregistered persons/firms assist companies to find capital. Unregistered brokers who raise funds for small businesses or engage in merger and acquisition business for a fee are generally referred to as “finders,” “merchant bankers,” “financial public relations advisors,” or simply “business consultants.” Fees are generally based upon a percentage of the amount of securities their clients sell. Perhaps unknowingly, these persons are acting as unlicensed securities brokers whose fee contracts are unenforceable and their activities are illegal. The SEC and the states frequently bring enforcement actions against unlicensed brokers. FINRA encounters many situations where firms and registered representatives (RRs) have facilitated transactions with unlicensed finders. Enforcement actions are frequently brought against unscrupulous or unaware RRs who have engaged in “selling away” transactions. Notwithstanding the legal ramifications, many small businesses rely heavily on unlicensed brokers to raise capital. The strong need for small business capital formation has caused “a large majority of unlicensed [brokers] to violate laws which are overbroad and largely ignored because of the need of the community to act in disregard of those laws.”⁶

Several proposals have been made by respected groups to address this situation. In 2005, an ABA Task Force recommended that the SEC, FINRA and state securities regulators work to establish a simplified system for the registration of private placement broker-dealers.⁷ Along the same lines, the Alliance of Merger and Acquisition Advisors has proposed model rules to federal, state and FINRA regulators to establish a regulatory regimen for merger and acquisition brokers (“M&A Brokers”). Essentially, M&A Brokers would be able to facilitate the transfer of ownership of small businesses where that transfer begins as an asset sale but later changes in to the sale or exchange of stock.⁸ Such M&A Brokers would be exempt from SEC registration if their activities were limited to certain identified actions. M&A Brokers could be engaged in the sale of all or a part of an existing business that was affected through a stock purchase/sale, exchange, merger, or other business involving the transfer or issuance of securities if certain conditions are met. The SEC has hinted on several occasions that it has been working on

⁶ See ABA Task Force Report.

⁷ See **Report and Recommendation of the Task Force on Private Placement Broker-Dealers**, 60 Business Lawyer 959 (May 2005). [**ABA Task Force Report**] at page 2.

⁸ See **Proposed Model State Rules Regulatory “M&A Brokers” and Intermediaries in Small Business Sales** dated March 20, 2008. http://www.amaaonline.com/files/Proposed_Model_State_Rules_for_M&A_Brokers_and_Small_Business_Sales_3-20-08_Final.pdf; and Comment Letter to SEC, from Michael Adikari, Advisory Bond President Alliance of Merger & Acquisitions Advisors to Elizabeth M. Murphy, Secretary, SEC, dated March 30, 2009. <http://sec.gov/comments/sr-finra-2009-006/finra2009006-4.pdf>.

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proposed rulemaking in this area.⁹ While the SEC in approving the new FINRA rule acknowledged that it has been studying these and similar proposals, it asserted in the approving release that the proposals are “not germane to this proposed rule” and are “being considered separately by the Trading and Markets Division.”

Notwithstanding regulatory hesitance to adopt a “B-D Lite” registration or to exempt certain merger and acquisition firms from registration requirements, the new FINRA rule will allow firms to associate with investment banking professionals more easily. If firms have demonstrable training programs, experienced individuals could associate with them and perform investment banking services while they train and attain Series 79 status. Individuals have up to six months to successfully complete the prerequisite examination.

Participants in a firm’s training program have up to two years from associating with a firm to get qualified, so long as their involvement in investment banking activities is less than six months. For example, a person participating in a training program may choose investment banking work after working/training in a firm’s other businesses. This flexibility should aid firms and individuals to identify the “right fit” for a trainee without transgressing regulatory licensing requirements.

Hopefully, the FINRA action represents a strong step by regulators in the path toward workable process supporting capital formation for small businesses. As the ABA Task Force declared in its proposal: “Small businesses create many more new jobs than public companies which have no need for” unlicensed brokers.¹⁰

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⁹ See Joseph W. Bartlett, *ABA Task Force Urges the SEC to Promulgate “Broker Dealer Lite”:* *Registration Requirements for Unregistered Finders: Many Firms Are Currently at Risk in a “Gray Area”*, the *Journal of Private Equity*, Summer 2007. <http://sec.gov/comments/sr-finra-2009-006/finra2009006-4.pdf>.

¹⁰ **ABA Task Force Report** at page 2.

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