

The BrokeAndBroker.com FINRA Rule 3040 / Private Securities Transactions / PST Analysis by Bill Singer

Let's examine FINRA's *PST Rule* and make sure that we understand what's required. Note my commentary after each section:

NASD Rule 3040. Private Securities Transactions of an Associated Person

(a) Applicability

No person associated with a member shall participate in any manner in a private securities transaction except in accordance with the requirements of this Rule.

Bill Singer's Comment: "No" means "no." There is no nuance here at all. Associated persons are prohibited from participating in any PST EXCEPT as permitted under this rule.

(b) Written Notice

Prior to participating in any private securities transaction, an associated person shall provide written notice to the member with which he is associated describing in detail the proposed transaction and the person's proposed role therein and stating whether he has received or may receive selling compensation in connection with the transaction; provided however that, in the case of a series of related transactions in which no selling compensation has been or will be received, an associated person may provide a single written notice.

Bill Singer's Comment: The PST Rule's basic premise is that of prior notice. It is incumbent upon the associated person to provide prior *written* notice to his/her member firm. Two things here tend to trip a lot of folks up:

1. you must submit the notice before you undertake any PST activity -- not after you begin or contemporaneous with your activity; and
2. the notice must be written notice. That's doesn't mean via telephone or pursuant to a conversation in your boss's office. Trust me, this latter lapse is the killer -- yeah, you told your

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firm but now they're denying it and, worse, the Rule doesn't allow you to "tell" anything about the PST other than in written form.

You must also focus on the required content of your written notice:

- A ***detailed*** description of the proposed PST. Detailed does not mean something briefly written on a cocktail napkin. It doesn't mean the rough outline of the transaction. It calls for as much specifics as exist.
- Your proposed role must be set forth. If that role morphs over time, that's okay, but when you submit the prior written notice, you better make sure to accurately characterize what you understand your proposed role to be.

Too many folks get cute is in trying to avoid disclosing that they already received selling compensation --- which is a problem because you were not supposed to be involved in any PST before you submitted a prior written notice to your firm. On top of that dilemma, you must disclose any anticipated selling compensation.

(c) Transactions for Compensation

(1) In the case of a transaction in which an associated person has received or may receive selling compensation, a member which has received notice pursuant to paragraph (b) shall advise the associated person in writing stating whether the member:

(A) approves the person's participation in the proposed transaction; or

(B) disapproves the person's participation in the proposed transaction.

(2) If the member approves a person's participation in a transaction pursuant to paragraph (c)(1), the transaction shall be recorded on the books and records of the member and the member shall supervise the person's participation in the transaction as if the transaction were executed on behalf of the member.

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(3) If the member disapproves a person's participation pursuant to paragraph (c)(1), the person shall not participate in the transaction in any manner, directly or indirectly.

Bill Singer's Comment: PSTs involving your receipt or anticipated receipt of "compensation" not only require that you submit prior written notice but that you also receive prior notice approving or disapproving your proposed participation. If approved, the PST gets put on the firm's books and records, and you are supervised as if the deal were executed at the firm. If not approved, hey, you look pretty sharp and I'm sure you can figure out what that means.

(d) Transactions Not for Compensation

In the case of a transaction or a series of related transactions in which an associated person has not and will not receive any selling compensation, a member which has received notice pursuant to paragraph (b) shall provide the associated person prompt written acknowledgment of said notice and may, at its discretion, require the person to adhere to specified conditions in connection with his participation in the transaction.

Bill Singer's Comment: PSTs not involving your receipt or anticipated receipt of "compensation" not only require that you submit prior written notice but that you also receive prior notice acknowledging your proposed participation. Your firm may impose conditions upon your participation in this type of PST.

(e) Definitions

For purposes of this Rule, the following terms shall have the stated meanings:

(1) "Private securities transaction" shall mean any securities transaction outside the regular course or scope of an associated person's employment with a member, including, though not limited to, new offerings of securities which are not registered with the Commission, provided however that transactions subject to the notification requirements of Rule 3050, transactions among immediate family members (as defined in Rule 2790), for which no associated person receives any selling compensation, and personal transactions in investment company and variable annuity securities, shall be excluded.

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(2) "Selling compensation" shall mean any compensation paid directly or indirectly from whatever source in connection with or as a result of the purchase or sale of a security, including, though not limited to, commissions; finder's fees; securities or rights to acquire securities; rights of participation in profits, tax benefits, or dissolution proceeds, as a general partner or otherwise; or expense reimbursements.

Bill Singer's Comment: The definition of PST is quite broad and literally covers "any" securities transaction outside of your regular course of employment. When in doubt, ask for a lawyer's opinion. Note that "selling compensation" may consist of an indirect consideration in the form of compensation that may be paid from sources other than the proposed deal's principals. The consideration need not be limited to cash but may include profits, tax benefits, or expenses.