



November 18, 2010

FINRA Issues New Outside Business Activity Rule

New FINRA Rule 3270 (the Rule) will replace NASD Rule 3030, effective December 15, 2010. This change will have a significant impact on the compliance efforts related to outside business activities for member firms of the Financial Industry Regulatory Authority (FINRA). NASD Rule 3030 currently requires a registered person to provide notice whenever he or she is employed by, or accepts any compensation from any person as a result of any outside business activity (other than passive investment), unless he or she has provided prompt written notice to the member firm. The Rule goes beyond that, by prohibiting any registered person from being an employee, independent contractor, sole proprietor, officer, director or partner of another person, or being compensated, or having the reasonable expectation of compensation, from another person as a result of any business activity outside the scope of the relationship with his or her member firm, unless he or she has provided prior written notice to the member firm. Even then, registered persons may not engage in the activity until they receive written permission from the member firm.

Upon receipt of a written notice, firms will have to consider whether the proposed activity will: (1) interfere with or otherwise compromise the registered person's responsibilities to the firm and/or the firm's customers, or (2) be viewed by customers or the public as part of the firm's business. Based on the review, the firm will have to evaluate whether to impose specific conditions or limitations on a registered person's outside business activity up to and including prohibiting the activity. Firms will also have to evaluate the activity to determine whether the activity is truly an outside business activity or whether it should be treated as an outside securities activity subject to the requirements of NASD Rule 3040. Additionally, it should be noted that, with respect to registered persons who are actively engaged in an outside business activity prior to the December 15, 2010 effective date of the Rule, firms will have until June 15, 2011 to review such pre-existing activities, utilizing the standards set forth in the Rule, and document their compliance with such standards.

In addition to having to modify the written procedures of the firm related to this process, the Rule by implication imposes additional obligations for firms to monitor and track outside business activities of their registered representatives. Regulators have inferred that the utilization of a risk based approach to the review and monitoring of registered representative activities would be appropriate. Firms are advised to expand their

historical approach when monitoring to confirm that registered representatives have followed the rule and relevant procedures of the firm related to outside business activities.

Firms that have concerns regarding their registered representatives outside business activities because representatives have previously failed to provide notification, or failed to be responsive to the firm's regulatory obligations, will need to take additional action in the oversight and monitoring of its registered representatives. Additional actions related to the monitoring of outside business activities may include the following: checking the Secretary of State's website to see if the registered representative comes up as an owner or director of an entity; conducting credit checks; requesting and reviewing copies of tax returns, or bank statements and cancelled checks.

You should also note that while the Form U4 does not require the disclosure of outside business activities for not for profit organizations, the revisions brought about by the Rule will require a registered representative to disclose any activity as a director or an officer of a not for profit entity, even if in a non-paid status prior to engaging in the activity.

We hope that this information has been helpful to you. Should you have any additional questions or concerns, please feel free to contact Daniel E. LeGaye or Michael Schaps by e-mail or phone, at 281-367-2454, or consult with your legal counsel or third party consultant.

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