

05-67

## Notice to Members

OCTOBER 2005

GUIDANCE

### **Branch Office Definition**

SEC Approves Uniform Branch Office Definition and Related Interpretive Material; **Effective Date: May 1, 2006**

#### ***Location Used Primarily to Engage in Non-Securities Transactions***

Rule 3010(g)(2)(A)(v) exempts from branch office registration locations where associated persons are primarily engaged in non-securities activities (*e.g.*, insurance sales) and from which an associated person effects no more than 25 securities transactions in a calendar year; provided that advertisements or sales literature, including business cards, identifying such location also set forth the locations from which the associated person or persons are directly supervised. All securities transactions originating from such locations must be entered through, and supervised by, the associated person's designated branch office. Once the 25 securities transaction threshold is exceeded, members will be given a 30-calendar-day window to register such locations as branch offices.

#### ***Locations Other than Primary Residences***

Rule 3010(b)(2)(A)(iii) exempts from branch office registration any location, other than primary residences, provided it is used for securities-related activities less than 30-business days in any calendar year. These would generally include vacation or second homes and other non-primary residences. Such locations are subject to the same criteria imposed upon exempted primary residences (enumerated above).

In the context of this exemption, the term "business day" is defined to exclude any partial day, provided the associated person spends at least four hours of such business day at his or her designated branch office during the time period such office is normally open for business. This is intended to prevent associated persons from regularly conducting business from locations other than their primary residence for the majority of a business day, without such activity being counted towards the 30-business-day limit.

Where the 30-business-day exemption is utilized, members are expected to maintain records adequate to demonstrate compliance with the business day limitations. Once the 30-business day limit has been reached, members will have a 30-calendar-day window to register such locations as branch offices.

#### ***Primary Residences***

Rule 3010(g)(2)(A)(ii) exempts from the definition of branch office any location that is the

associated person's primary residence. Only one associated person, or multiple associated persons who reside at the location and are members of the same immediate family, may conduct business from the location. Each member must maintain a current list of any such locations, which are subject to the following specific safeguards and limitations:

The location may not be held out as an office. The associated person(s) may not meet with customers at the location. Neither customer funds nor securities may be handled at the location. The associated person or persons are assigned to a designated branch office, which is reflected on all business cards, stationery, advertisements and other communications with the public.

All communications with the public must be subject to supervisory provisions pursuant to all applicable NASD rules (including, but not limited to, Rule 3010).

Electronic communications must be transmitted through the member's electronic system.

All orders must be entered through the designated branch office or through an electronic system established by the member that is reviewable at such branch office.

Written procedures relating to the supervision of sales activities conducted at the location must be maintained by the member.

#### **Exemptions from Branch Office Registration**

NASD believes the exceptions from branch office registration are practically based while still containing important safeguards and limitations to protect investors.

Accordingly, as further detailed below, the Uniform Definition excludes from registration as a branch office: (1) a location that operates as a non-sales location/back office; (2) a representative's primary residence provided it is not held out to the public and certain other conditions are satisfied; (3) a location, other than the primary residence, that is used for less than 30 business days annually for securities business, is not held out to the public as an office, and which satisfies certain of the conditions set forth in the primary residence exception; (4) a location of convenience used occasionally and by appointment; (5) a location used primarily for non-securities business and from which less than 25 securities transactions are effected annually; (6) the floor of an exchange; and (7) a temporary location used as part of a business continuity plan.

#### **First Asset Financial Inc. comments:**

Notice to Members 06-12 states:

***As a result of amended NASD Rule 3010, many members may now be required to register existing office locations as branch offices.***

If you are not currently registered as a BRANCH office, you need to be aware of the NEW definition of a branch office.

The initial costs of registering a branch office (as of 12-31-07) is \$175 total (consisting of both NASD fee and Surety Bonding Charges) with renewal costs each year of \$195 (due to a FINRA \$20 "processing fee").

The following could **force you to be registered as a branch office:**

1. Your business card:

You need to be particularly careful of WHAT is placed on your business card, letterhead, etc. Placing your office address on these materials would make you instantly subject to branch office registration in the case of using a residence address! An office primarily used for non-securities activities (e.g. insurance sales) may place the address on the card as long as the address & phone of the FAF OSJ is also on the card. Be very careful. You **CAN** use your office/home telephone number and/or cell phone number on your card as long as your OSJ telephone number & address appears on your card as well, but you **CANNOT** place your address on the card.

2. Number of transactions taking place in your home:

If you use your primary residence from which you effect no more than

3. Number of days your office (insurance or otherwise) is used for securities business.

If you use your office location for securities business **30 days or more a year, you MUST register** your location as a branch office.

Those of you who are relying on the "30 day" exemption, be especially careful to follow the FINRA/NASD ruling:

**Where the 30-business-day exemption is utilized, members are expected to maintain records adequate to demonstrate compliance with the business day limitations. Once the 30-business day limit has been reached, members will have a 30-calendar-day window to register such locations as branch offices.**

**If you rely on the exemption for an office location used primarily for non-securities sales, YOU must keep track of your sales each calendar year. Once the 25 sales in a calendar year limit has**

**been reached for your office, you are required to notify FAF. You have a 30 calendar-day window to notify FAF to register your location as a branch office. If you fail to do so, you will be in violation of FINRA/NASD Rule 3010(g)(2)(B).**

If you wish to know more about this issue and how it affects you, here are excerpts from FINRA/NASD Notice to Members 06-12 and 05-67. You can view the entire NTM at [www.finra.org](http://www.finra.org) and then click on "notices" then on 2005 or 2006 notice (first number of the NTM is the year of the notice) and scroll down to the number.

## **Excerpts from Notice to Member 06-12:**

### **Interpretive Questions**

A "branch office" is generally defined as any location where one or more associated persons of a member regularly conducts the business of effecting any transactions in, or inducing or attempting to induce the purchase or sale of any security, or that is held out as such.

The Uniform Definition excludes from registration as a branch office:

(1) a non-sales location that provides customer service or back office functions; (2) an associated person's primary residence provided it is not held out to the public as a branch office and certain other conditions are satisfied; (3) a location, other than the primary residence, that is used for less than 30 business days in any calendar year for securities business, is not held out to the public as an office, and which satisfies certain of the conditions set forth in the primary residence exemption; (4) a location of convenience used occasionally and by appointment; (5) a location used primarily for non-securities business and from which no more than 25 securities transactions are effected annually; (6) the floor of a registered securities exchange; and (7) a temporary location used as part of a business continuity plan.

The SROs(FINRA/NASD) have received questions from broker-dealers and associated persons requesting clarification of certain exemptions under the Uniform Definition. These questions, and SRO(FINRA/NASD) responses, are as follows:

#### **"Regularly Conducts the Business of Effecting Transactions"**

Q1 The Uniform Definition provides that a "branch office" is "any location where one or more associated persons of a member regularly conducts the business of effecting transactions in, or inducing or attempting to induce the purchase or sale of any security, or is held out as such." What types of activities would this include?

A1 Such activities would include, for example: (1) soliciting new accounts or orders; (2) opening new accounts; (3) accepting or executing orders; or (4) making recommendations with respect to securities transactions. NASD members should keep in mind that certain activities, such as order execution, may also require a location to be registered as an office of supervisory jurisdiction (OSJ) under NASD Rule 3010(g)(1).

## Primary Residences

The Uniform Definition exempts from the definition of “branch office” any location that is an associated person’s primary residence<sup>10</sup>, provided that:

(a) only one associated person, or multiple associated persons who reside at the location and are members of the same immediate family, conduct business from the location; (b) the location is not held out to the public as an office and the associated person does not meet with customers at the location; (c) neither customer funds nor securities are handled at the location; (d) the associated person is assigned to a designated branch office, and such designated branch office is reflected on all business cards, stationery, advertisements, and other communications to the public by the associated person; (e) the associated person’s correspondence and communications with the public are subject to the member’s supervision in accordance with NASD Rule 3010 and NYSE Rules 342 and 472; (f) electronic communications (e.g., email) are transmitted through the member’s electronic system; (g) all orders are entered through the designated branch office or through an electronic system established by the member that is reviewable at the branch office; (h) written supervisory procedures pertaining to supervision of sales activities conducted at the residence are maintained by the member; and (i) a list of the residence locations is maintained by the member.

Q6 One of the conditions that must be satisfied for the “primary residence” exemption from the Uniform Definition to apply is that the associated person be assigned to a designated branch office, and that the address of such designated branch office be reflected on all business cards, stationery, advertisements and other communications to the public. Can an associated person use the unregistered location address in telephone directories, business cards, stationery, advertising or sales literature, so long as such communication also sets forth the address and telephone number of the branch office or OSJ from which the associated person is supervised?

A6 No. The use of the primary residence address in a telephone directory, business card, stationery, advertising or sales literature will be deemed “holding out” the location as a branch office in violation of NASD Rule 3010(g)(2)(A)(ii)(b) and NYSE Rule 342.10(B)(ii), even if such communication also sets forth the address and telephone number of the branch office or OSJ from which the associated person is supervised.

Q7 Can an associated person use an unregistered location (e.g., primary residence) telephone number or mobile telephone number in telephone directories, business cards, stationery, advertisements and other communications with the public by such associated person?

A7 Yes. An associated person can use the telephone number of an unregistered location or a mobile telephone number in telephone directories, business cards, stationery, advertising or other communications with the public, provided (1) the address of the unregistered location is not listed on any such communication; and (2) the communication also includes the telephone number and address of the branch office or OSJ from which the associated person is supervised.

Q8 One of the conditions that must be satisfied for the “primary residence” exemption from the Uniform Definition to apply is that “neither customer funds nor securities are handled at that location.” Are there instances when an associated person may accept funds and/or securities and not violate this condition?

A8 Associated persons may not directly accept funds or securities at their primary residence since this would violate the “primary residence” exemption prohibition against meeting with customers at the residence. Likewise, accepting funds or securities mailed directly to the primary residence address would violate the prohibition against “holding out” the location as a branch office.

However, an associated person working from a primary residence may accept funds or securities at an “office of convenience,”<sup>13</sup> provided the following conditions are met: (1) the funds are made payable to the member or the issuer, as the case may be; (2) the funds are not deposited by the associated person; and (3) the associated person promptly forwards such funds or securities received from the customer to the member or the issuer, as the case may be.

If an associated person subsequently brings funds and/or securities received from a customer to the primary residence location, it will not be considered a violation of the primary residence exemption provided such funds or securities are promptly forwarded to the member or issuer. However, the associated person must not exercise control over the funds or securities. Members are advised to consider the requirements of SEC Rules 15c3-1 (Net Capital Requirements for Brokers and Dealers) and 15c3-3 (Customer Protection – Reserves and Custody of Securities).<sup>14</sup>

Q9 One of the conditions that must be satisfied in order for the “primary residence” exemption to the Uniform Definition to apply is that electronic communications (e.g., email) are transmitted through the member’s electronic systems.<sup>15</sup> Further, such communications must be entered through the designated branch office or through an electronic system established by the member that is reviewable at the branch office.<sup>16</sup> Can an associated person use his or her personal email accounts to communicate with potential or existing customers?

A9 No. All electronic communications must be made through the member’s electronic system, and all orders must be entered through the designated branch office or through an electronic system established by the member that is reviewable at the branch office. In addition, the SEC’s Books and Records Rules (SEC Rules 17a-3 and 17a-4)<sup>17</sup> require members to maintain records of electronic mail communications.

### **Locations Other than Primary Residences**

The Uniform Definition exempts from branch office registration any location, other than primary residences, provided it is used for securities-related activities less than 30-business days in any calendar year.<sup>18</sup> These would generally include vacation or second homes and other non-primary residences. Such locations are subject to most of the criteria (enumerated above) imposed upon exempted primary residences. In the context of this exemption, the term “business day” is defined to exclude any partial day, provided the associated person spends at least four hours of such business day at his or her designated branch office during the time period such office is normally open for business. This is intended to prevent associated persons from regularly conducting business from locations other than their primary residences for the majority of a business day, without such activity being counted towards the 30-business day limit.

Q10 If a member relies on the “30-business days in one calendar year” exemption, what types of records must a member maintain to demonstrate compliance with the “business day” limitation?

A10 A member is expected to demonstrate compliance with the “business day” limitation by maintaining, at a minimum, logs identifying any such locations, “business days” spent at

such locations, and the activities of the associated person conducted from such locations.

Q11 If a member relies on the “30-business days in one calendar year” exemption and the location later exceeds the 30-business day threshold in one calendar year, must the member register the location?

A11 The member’s initial reliance on this exemption must be reasonably determined based on an understanding of the use of such location. Once the 30-business days in a calendar year limit has been reached, members will have a 30 calendar-day window to register such location as a branch office.

### **Offices of Convenience**

The Uniform Definition exempts from branch office registration “offices of convenience.”<sup>19</sup> An office of convenience is defined as a location where an associated person occasionally and exclusively by appointment meets with customers, provided such location is not held out to the public as an office. Where such office of convenience is located on bank premises, signage necessary to comply with applicable federal and state laws, rules and regulations and applicable rules and regulations of the NYSE, other self-regulatory organizations, and securities and banking regulators may be displayed and will not be deemed “holding out” for purposes of this section. NYSE Rule 342(D) prescribes that only signage required by the Interagency Statement (Statement on Retail Sales of Nondeposit Investment Products required under Banking Regulations) may be displayed at such locations. Such limited signage is allowed to prevent confusion on the part of customers who might otherwise believe that only traditional, insured bank-related investments are being offered at the location.

Q12 If an associated person works from multiple offices, (e.g., “bank circuit riders”), can a member rely on the “office of convenience” exemption to not register such locations?

A12 Yes. A member may rely on this exemption to not register multiple locations that an associated person is assigned to, provided: the associated person meets with customers only occasionally and exclusively by appointment at any such location; and no other activities occur at such location that would require branch office registration. For instance, the location may not be held out to the public, other than, in the case of a location on bank premises, displaying signage necessary to comply with applicable federal and state laws, rules and regulations and applicable rules and regulations of other self-regulatory organizations, and securities and banking regulators. The associated person, however, must be assigned to at least one registered location for supervisory purposes. The exemption is not limited to bank locations. Any broker-dealer can use the exemption so long as the conditions of the exemption are satisfied.

Q13 What is the meaning of “occasionally” for purposes of “offices of convenience” exemption pursuant to NASD Rule 3010(g)(2)(A)(iv) and NYSE Rule 342.10(D)?

A13 An associated person may meet with customers at such location by appointment only; however, an associated person may not establish regular business hours at such location or hold out the location in any way (except for signage permitted at banks as discussed above). If customers or prospective customers know that an associated person can be met with regularly (or on some predetermined schedule such as the first Monday of every month) at a particular location, it would not qualify as an office of convenience. If the associated person meets with walk-in customers at such location, such location would not qualify as an office of convenience. For example, if a member has a location in a hospital, school or similar type location where an associated person(s) offers securities (such as through 403(b) type plans<sup>20</sup>) and the associated person(s) is there on a regular

schedule, such location would not qualify for this exemption.

### **Location Used Primarily to Engage in Non-Securities Transactions**

The Uniform Definition exempts from branch office registration locations where associated persons are primarily engaged in non-securities activities (e.g., insurance sales) and from which an associated person effects no more than 25 securities transactions in a calendar year, provided that advertisements or sales literature, including business cards, identifying such location also set forth the locations from which the associated person or persons are directly supervised.<sup>21</sup>

Q15 If a member relies on the non-securities transaction exemption and the location later exceeds the 25 securities transactions in a calendar year limitation, must the member register the location?

A15 A member's initial reliance on this exemption must be reasonably determined based on the use of such location (i.e., an ongoing determination must be made to determine whether the total number of securities transactions effected from the location exceeds the 25-transaction de minimis standard). Once the 25 securities transactions in a calendar year threshold is exceeded, members will be given a 30 calendar-day window to register such locations as branch offices.

Q16 Are there any transactions that do not count towards the "25 securities transactions in a calendar year" limitation?

A16 Yes. Transactions made pursuant to automatic investment plans wherein a customer provides prior written instructions to purchase a predetermined number of shares on a regular basis would not count towards the 25 transactions in one calendar year limitation, provided there is no new recommendation given by an associated person to the customer with respect to such transactions.

### **Offices That Supervise Other Offices**

NASD Rule 3010(g)(2)(B) and NYSE Rule 342.10 provide that notwithstanding the exclusions provided in 3010(g)(2)(A)(i)-(vii) or 342.10(A)-(G), respectively, any location that is responsible for supervising the activities of persons associated with the member at one or more *non-branch* locations of the member is considered to be a branch office. For example, if an associated person supervises the activities of persons at one or more *non-branch* locations from his primary residence, such primary residence location must be registered as a branch office.