



> FINRA RULES > 5000. SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES  
> 5100. SECURITIES OFFERINGS, UNDERWRITING AND COMPENSATION

## 5110. Corporate Financing Rule — Underwriting Terms and Arrangements

The Rule

Notices

**This version is valid from Mar 20, 2020 through Jun 29, 2020.**

**Amendments have been announced but are not yet effective. To view other versions open the versions tab on the right.**

### (a) Definitions

For purposes of this Rule, the following terms shall have the meanings stated below. The definitions in Rule 5121 are incorporated herein by reference.

#### (1) Issuer

The issuer of the securities offered to the public, any selling security holders offering securities to the public, any affiliate of the issuer or selling security holder, and the officers or general partners, directors, employees and security holders thereof.

#### (2) Net Offering Proceeds

Offering proceeds less all expenses of issuance and distribution.

#### (3) Offering Proceeds

Public offering price of all securities offered to the public, not including securities subject to any overallotment option, securities to be received by the underwriter and related persons, or securities underlying other securities.

#### (4) Participating Member(s)

Any FINRA member that is participating in a public offering, any associated person of the member, any members of their immediate family, and any affiliate of the member.

#### (5) Participation or Participating in a Public Offering

Participation in the preparation of the offering or other documents, participation in the distribution of the offering on an underwritten, non-underwritten, or any other basis, furnishing of customer and/or broker lists for solicitation, or participation in any advisory or consulting capacity to the issuer related to the offering, but not:

(A) the preparation of an appraisal in a savings and loan conversion or a bank offering or the preparation of a fairness opinion pursuant to SEA Rule 13e-3; or

(B) advisory or consulting services provided to the issuer by an independent financial adviser. For purposes of this provision, an "independent financial adviser" is a member that provides advisory or consulting services to the issuer and is neither engaged in, nor affiliated with any entity that is engaged in, the solicitation or distribution of the offering.

#### (6) Underwriter and Related Persons

Consists of underwriter's counsel, financial consultants and advisors, finders, any participating member, and any other persons related to any participating member.

#### (7) Listed Securities

Securities meeting the listing standards to trade on the national securities exchanges identified in Securities Act Rule 146, markets registered with the SEC under Section 6 of the Exchange Act, and any offshore market that is a "designated offshore securities market" under Rule 902(b) of SEC Regulation S.

#### (8) Derivative Instruments

A derivative instrument is any "eligible OTC derivative instrument" as defined in SEA Rule 3b-13(a)(1), (2) and (3).

#### (9) Fair Price

A derivative instrument or non-convertible or non-exchangeable debt security has been acquired or entered into at a fair price for purposes of paragraphs (b)(6)(A)(iv), (c)(3)(B)(vi) and (vii), and (e)(5) if the underwriters and related persons have priced the debt security or derivative instrument in good faith; on an arm's length, commercially reasonable basis; and in accordance with pricing methods and models and procedures used in the ordinary course of their business for pricing similar transactions. A derivative instrument or other security received for acting as a private placement agent for the issuer, for providing or arranging a loan, credit facility, merger, acquisition or any other service, including underwriting services, is not included within this "fair price" definition.

#### **(10) Required Filing Date**

The required filing date shall be the dates provided in paragraph (b)(4), and for a public offering exempt from filing under paragraph (b)(7), the required filing date for purposes of paragraphs (d) and (g) shall be the date the public offering would have been required to be filed with FINRA but for the exemption.

#### **(11) Company**

A corporation, a partnership, an association, a joint stock company, a trust, a fund, or any organized group of persons whether incorporated or not; or any receiver, trustee in bankruptcy or similar official or any liquidating agent for any of the foregoing, in his capacity as such.

#### **(12) Effective Date**

The date on which an issue of securities first becomes legally eligible for distribution to the public.

#### **(13) Immediate Family**

The parents, mother-in-law, father-in-law, spouse, brother or sister, brother-in-law or sister-in-law, son-in-law or daughter-in-law, and children of an employee or associated person of a member, except any person other than the spouse and children who does not live in the same household as, have a business relationship with, provide material support to, or receive material support from, the employee or associated person of a member. In addition, the immediate family includes any other person who either lives in the same household as, provides material support to, or receives material support from, an employee or associated person of a member.

#### **(14) Person**

Any natural person, partnership, corporation, association, or other legal entity.

### **(b) Requirements for Public Offerings**

#### **(1) General**

No member or person associated with a member shall participate in any manner in any public offering of securities subject to this Rule, Rule 2310 or Rule 5121 unless documents and information as specified herein relating to the offering have been filed with and reviewed by FINRA.

#### **(2) Means of Filing**

Documents or information required by this Rule to be filed with FINRA shall be considered to be filed only upon receipt by its Corporate Financing Department.

#### **(3) Confidential Treatment**

FINRA shall accord confidential treatment to all documents and information filed pursuant to this Rule and shall utilize such documents and information solely for the purpose of review to determine compliance with the provisions of applicable FINRA rules or for other regulatory purposes deemed appropriate by FINRA.

#### **(4) Timely Filing Requirements**

(A) A member that participates in a public offering that is required to be filed under paragraph (b)(9) must file the documents and information specified in paragraph (b)(5):

(i) no later than three business days after any documents are filed with or submitted to:

a. the SEC, including confidential filings or submissions;;

or

b. any state securities commission or other similar U.S. regulatory authority; or

(ii) if not filed with or submitted to any such regulatory authority, at least 15 business days prior to the commencement of sales.

#### **(5) Documents and Information Required to be Filed**

(A) The following documents required to be filed under paragraph (b)(4) must be filed in FINRA's Public Offering System for review by providing the SEC document identification number if available:

(i) the registration statement, offering circular, offering memorandum, notification of filing, notice of intention, application for conversion, and any other document used to offer securities to the public;

(ii) all documents relevant to the underwriting terms and arrangements, including any proposed underwriting agreement, agreement among underwriters, selected dealer's agreement, agency agreement, purchase agreement, letter of intent, engagement letter, consulting agreement, partnership agreement, underwriter's warrant agreement, or escrow agreement, provided that industry-standard master forms of agreement need not be filed unless otherwise specifically requested by FINRA;

(iii) if amendments to any documents previously filed contain changes that impact the underwriting terms and arrangements for the public offering, marked pages showing the changes to such document;

(iv) The final registration statement declared effective by the SEC or equivalent final offering document and a list of the members of the underwriting syndicate, if not indicated therein, and one copy of the executed form of the final underwriting documents and any other document submitted to FINRA for review.

(B) Documents that are filed with the SEC through the SEC's Electronic Data Gathering, Analysis, and Retrieval ("EDGAR") System that are referenced in FINRA's electronic filing system shall be treated as filed with FINRA.

#### **(6) Information Required to be Filed**



(A) Any person filing documents with FINRA pursuant to subparagraph (4) above shall provide the following information with respect to the offering through FINRA's electronic filing system:

(i) an estimate of the maximum public offering price;

(ii) an estimate of the maximum underwriting discount or commission; maximum reimbursement of underwriter's expenses, and underwriter's counsel's fees (except for reimbursement of "blue sky" fees); maximum financial consulting and/or advisory fees to the underwriter and related persons; maximum finder's fees; and a statement of any other type and amount of compensation which may accrue to the underwriter and related persons;

(iii) a statement of the association or affiliation with any participating member of any officer or director of the issuer, of any beneficial owner of 5% or more of any class of the issuer's securities, and of any beneficial owner of the issuer's unregistered equity securities that were acquired during the 180-day period immediately preceding the required filing date of the public offering, except for purchases described in paragraph (c)(3)(B)(iv) below. This statement must identify:

a. the person;

b. the member; and

c. the number of equity securities or the face value of debt securities owned by such person, the date such securities were acquired, and the price paid for such securities.

(iv) a detailed explanation of any other arrangement entered into during the 180-day period immediately preceding the required filing date of the public offering, which arrangement provides for the receipt of any item of value or the transfer of any warrants, options, or other securities from the issuer to the underwriter and related persons, provided however:

a. information regarding debt securities and derivative instruments not considered an item of value under paragraphs (c)(3)(B)(vi) and (vii) is not required to be filed; and

b. information initially filed in connection with debt securities and derivative instruments acquired or entered into for "fair price" as defined in paragraph (a)(9), but not excluded from items of value under paragraph (c)(3)(B)(vi) or (vii), may be limited to a brief description of the transaction (additional information may be required in the review process) and a representation by the member that a registered principal or senior manager on behalf of the member has determined that the transaction was or (if the pricing terms have not been set) will be entered into at a fair price as defined in paragraph (a)(9).

(v) a statement demonstrating compliance with all of the criteria of an exception from underwriting compensation in paragraph (d)(5) below, when applicable; and

(vi) a detailed explanation and any documents related to:

a. the modification of any information or representation previously provided to FINRA or of any item of underwriting compensation including the information required in paragraph (b)(6)(A)(iii) above with respect to any securities of the issuer acquired subsequent to the required filing date and prior to the effectiveness or commencement of the offering ; or

b. any new arrangement that provides for the receipt of any additional item of value by any participating member subsequent to the issuance of an opinion of no objections to the underwriting terms and arrangements by FINRA and within 90 days immediately following the date of effectiveness or commencement of sales of the public offering, provided, however, that information filed in connection with debt securities and derivative instruments acquired or entered into for a "fair price" as defined in paragraph (a)(9) may be limited as described in paragraph (b)(6)(A)(iv)b.

(vii) any other information required to be filed under this Rule.

(B) Any person filing documents pursuant to paragraph (b)(5) above shall notify FINRA through its electronic filing system that the offering has been declared effective or approved by the SEC or other agency no later than one business day following such declaration or approval or that the offering has been withdrawn or abandoned within three business days following the withdrawal or decision to abandon the offering.

## **(7) Offerings Exempt from Filing**

Notwithstanding the provisions of subparagraph (1) above, documents and information related to the following public offerings need not be filed with FINRA for review, unless subject to the provisions of Rule 5121(a)(2). However, it shall be deemed a violation of this Rule or Rule 2310, for a member to participate in any way in such public offerings if the underwriting or other arrangements in connection with the offering are not in compliance with this Rule or Rule 2310, as applicable:



(A) securities offered by a corporate, foreign government or foreign government agency issuer which has unsecured non-convertible debt with a term of issue of at least four (4) years, or unsecured non-convertible preferred securities, rated by a nationally recognized statistical rating organization in one of its four (4) highest generic rating categories, except that the initial public offering of the equity of an issuer is required to be filed;

(B) non-convertible debt securities and non-convertible preferred securities rated by a nationally recognized statistical rating organization in one of its four (4) highest generic rating categories;

(C) offerings of securities:

(i) registered with the SEC on registration statement Forms S-3 or F-3 pursuant to the standards for those Forms prior to October 21, 1992 and offered pursuant to Rule 415 of SEC Regulation C; or

(ii) of a foreign private issuer incorporated or organized under the laws of Canada or any Canadian province or territory, and is registered with the SEC on Form F-10 pursuant to the standards for that Form approved in Securities Act Release No. 6902 (June 21, 1991) and offered pursuant to Canadian shelf prospectus offering procedures;

(D) securities offered pursuant to a redemption standby "firm commitment" underwriting arrangement registered with the SEC on Forms S-3, F-3 or F-10 (only with respect to Canadian issuers);

(E) financing instrument-backed securities which are rated by a nationally recognized statistical rating organization in one of its four (4) highest generic rating categories;

(F) exchange offers of securities where:

(i) the securities to be issued or the securities of the company being acquired are listed on The Nasdaq Global Market, the New York Stock Exchange, or the American Stock Exchange; or

(ii) the company issuing securities qualifies to register securities with the SEC on registration statement Forms S-3, F-3, or F-10, pursuant to the standards for those Forms as set forth in subparagraphs (C)(i) and (ii) of this paragraph;

(G) offerings of securities by a church or other charitable institution that is exempt from SEC registration pursuant to Section 3(a)(4) of the Securities Act; and

(H) offerings of securities issued by a pooled investment vehicle, whether formed as a trust, partnership, corporation, limited liability company or other collective investment vehicle, that is not registered as an investment company under the Investment Company Act and has a class of equity securities listed for trading on a national securities exchange; provided that such equity securities may be created or redeemed on any business day at their net asset value per share.

## **(8) Exempt Offerings**

Notwithstanding the provisions of subparagraph (1) above, the following offerings are exempt from this Rule, Rule 2310, and Rule 5121. Documents and information relating to the following offerings need not be filed for review:

(A) securities exempt from registration with the SEC pursuant to the provisions of Sections 4(1), 4(2) or 4(6) of the Securities Act or pursuant to Rule 504 of SEC Regulation D if the securities are "restricted securities" under Securities Act Rule 144(a)(3), Rule 505 of SEC Regulation D, or Rule 506 of SEC Regulation D;

(B) securities which are defined as "exempt securities" in Section 3(a)(12) of the Exchange Act, as amended;

(C) securities of "open-end" investment companies as defined in Section 5(a)(1) of the Investment Company Act and securities of any "closed-end" investment company as defined in Section 5(a)(2) of the Investment Company Act that:

(i) makes periodic repurchase offers pursuant to Rule 23c-3(b) under of the Investment Company Act; and

(ii) offers its shares on a continuous basis pursuant to Rule 415(a)(1)(xi) of SEC Regulation C;

(D) variable contracts as defined in Rule 2320(b);

(E) modified guaranteed annuity contracts and modified guaranteed life insurance policies, which are deferred annuity contracts or life insurance policies the value of which are guaranteed if held for specified periods, and the nonforfeiture value of which are based upon a market-value adjustment formula for withdrawals made before the end of any specified period;

(F) offerings of municipal securities as defined in Section 3(a)(29) of the Exchange Act;

(G) tender offers made pursuant to SEC Regulation 14D under the Exchange Act;

(H) securities issued pursuant to a competitively bid underwriting arrangement meeting the requirements of the Public Utility Holding Company Act;

(I) securities of a subsidiary or other affiliate distributed by a company in a spin-off or reverse spin-off or similar transaction to its existing security holders exclusively as a dividend or other distribution; and

(J) securities registered with the SEC in connection with a merger or acquisition transaction or other similar business combination, except for offerings required to be filed pursuant to subparagraph (9)(I) below.

#### **(9) Offerings Required to be Filed**

Documents and information relating to all other public offerings including, but not limited to, the following must be filed with FINRA for review:

(A) direct participation programs as defined in Rule 2310(a);

(B) mortgage and real estate investment trusts;

(C) rights offerings;

(D) securities exempt from registration with the SEC pursuant to Section 3(a)(11) of the Securities Act;

(E) securities exempt from registration with the SEC pursuant to Rule 504 of SEC Regulation D, unless the securities are "restricted securities" under Securities Act Rule 144(a)(3);

(F) securities offered by a bank, savings and loan association, or common carrier even though such offering may be exempt from registration with the SEC;

(G) securities offered pursuant to SEC Regulation A;

(H) exchange offers that are exempt from registration with the SEC under Sections 3(a)(4), 3(a)(9), or 3(a)(11) of the Securities Act (if a member's participation involves active solicitation activities) or registered with the SEC (if a member is acting as dealer-manager) (collectively "exchange offers"), except for exchange offers exempt from filing pursuant to subparagraph (7)(F) above that are not subject to filing by subparagraph (9)(I) below;

(I) any exchange offer, merger and acquisition transaction, or other similar corporate reorganization involving an issuance of securities that results in the direct or indirect public ownership of the member; and

(J) any offerings of a similar nature that are not exempt under subparagraph (7) or (8) above.

#### **(c) Underwriting Compensation and Arrangements**

##### **(1) General**

No member or person associated with a member shall participate in any manner in any public offering of securities in which the underwriting or other terms or arrangements in connection with or relating to the distribution of the securities, or the terms and conditions related thereto, are unfair or unreasonable.

##### **(2) Amount of Underwriting Compensation**

(A) No member or person associated with a member shall receive an amount of underwriting compensation in connection with a public offering that is unfair or unreasonable and no member or person associated with a member shall underwrite or participate in a public offering of securities if the underwriting compensation in connection with the public offering is unfair or unreasonable.

(B) For purposes of determining the amount of underwriting compensation, all items of value received or to be received from any source by the underwriter and related persons which are deemed to be in connection with or related to the distribution of the public offering as determined pursuant to subparagraph (3) below shall be included.

(C) All items of underwriting compensation shall be disclosed in the section on underwriting or distribution arrangements in the prospectus or similar document and, if the underwriting compensation includes items of compensation in addition to the commission or discount disclosed on the cover page of the prospectus or similar document, a footnote to the offering proceeds table on the cover page of the prospectus or similar document shall include a cross-reference to the section on underwriting or distribution arrangements.



(D) For purposes of determining the currently effective guideline on the maximum amount of underwriting compensation considered fair and reasonable, the following factors, as well as any other relevant factors and circumstances, shall be taken into consideration:

- (i) the offering proceeds;
- (ii) the amount of risk assumed by the underwriter and related persons, which is determined by:
  - a. whether the offering is being underwritten on a "firm commitment" or "best efforts" basis and
  - b. whether the offering is an initial or secondary offering; and
- (iii) the type of securities being offered.

(E) The maximum amount of compensation (stated as a percentage of the dollar amount of the offering proceeds) that is considered fair and reasonable generally will vary directly with the amount of risk to be assumed by participating members and inversely with the dollar amount of the offering proceeds.

### **(3) Items of Value**

(A) For purposes of determining the amount of underwriting compensation received or to be received by the underwriter and related persons pursuant to paragraph (c)(2) above, the following items and all other items of value received or to be received by the underwriter and related persons in connection with or related to the distribution of the public offering, as determined pursuant to paragraph (d) below shall be included:

- (i) discount or commission;
- (ii) reimbursement of expenses to or on behalf of the underwriter and related persons;
- (iii) fees and expenses of underwriter's counsel (except for reimbursement of "blue sky" fees);
- (iv) finder's fees, whether in the form of cash, securities or any other item of value;
- (v) wholesaler's fees;
- (vi) financial consulting and advisory fees, whether in the form of cash, securities, or any other item of value;
- (vii) common or preferred stock, options, warrants, and other equity securities, including debt securities convertible to or exchangeable for equity securities, received:
  - a. for acting as private placement agent for the issuer;
  - b. for providing or arranging a loan, credit facility, merger or acquisition services, or any other service for the issuer;
  - c. as an investment in a private placement made by the issuer; or
  - d. at the time of the public offering;
- (viii) special sales incentive items;
- (ix) any right of first refusal provided to any participating member underwrite or participate in future public offerings, private placements or other financings, which will have a compensation value of 1% of the offering proceeds or that dollar amount contractually agreed to by the issuer and underwriter to waive the right of first refusal;
- (x) compensation to be received by the underwriter and related persons or by any person nominated by the underwriter as an advisor to the issuer's board of directors in excess of that received by other members of the board of directors;
- (xi) commissions, expense reimbursements, previously or other compensation to be received by the underwriter and related persons as a result of the exercise or conversion within twelve months following the effective date of the offering of warrants, options, convertible securities, or similar securities distributed as part of the public offering;
- (xii) fees of a qualified independent underwriter; and
- (xiii) compensation, including expense reimbursements, paid to any member in connection with a proposed public offering that was not completed, unless the member does not participate in the revised public offering.



(B) Notwithstanding paragraph (c)(3)(A) above, the following shall not be considered an item of value:

- (i) expenses customarily borne by an issuer, such as printing costs; SEC, "blue sky" and other registration fees; FINRA filing fees; and accountant's fees, whether or not paid through a participating member;
- (ii) cash compensation for acting as placement agent for a private placement or for providing a loan, credit facility, or for services in connection with a merger/acquisition;
- (iii) listed securities purchased in public market transactions;
- (iv) securities acquired through any stock bonus, pension, or profit-sharing plan that qualifies under Section 401 of the Internal Revenue Code;
- (v) securities acquired by an investment company registered under the Investment Company Act;
- (vi) nonconvertible or non-exchangeable debt securities acquired for a fair price in the ordinary course of business in a transaction unrelated to the public offering; and
- (vii) derivative instruments entered into for a fair price in the ordinary course of business in a transaction unrelated to the public offering.

#### **(d) Determination of Whether Items of Value Are Included In Underwriting Compensation**

##### **(1) Pre-Offering Compensation**

All items of value received and all arrangements entered into for the future receipt of an item of value by the underwriter and related persons during the period commencing 180 days immediately preceding the required filing date of the registration statement or similar document pursuant to paragraph (b)(4) above until the date of effectiveness or commencement of sales of the public offering will be considered to be underwriting compensation in connection with the public offering.

##### **(2) Undisclosed and Post-Offering Compensation**

All items of value received and all arrangements entered into for the future receipt of an item of value by any participating member that are not disclosed to FINRA prior to the date of effectiveness or commencement of sales of a public offering, including items of value received subsequent to the public offering, are subject to post-offering review to determine whether such items of value are, in fact, underwriting compensation for the public offering.

##### **(3) Date of Receipt of Securities**

Securities of the issuer acquired by the underwriter and related persons will be considered to be received for purposes of paragraphs (d)(1) and (d)(5) as of the date of the:

- (A) closing of a private placement, if the securities were purchased in or received for arranging a private placement; or
- (B) execution of a written contract with detailed provisions for the receipt of securities as compensation for a loan, credit facility, or put option; or
- (C) transfer of beneficial ownership of the securities, if the securities were received as compensation for consulting or advisory services, merger or acquisition services, acting as a finder, or for any other service.

##### **(4) Definitions**

For purposes of paragraph (d)(5) below, the following terms will have the meanings stated below.

(A) An entity:

- (i) includes a group of legal persons that either:
  - a. are contractually obligated to make co-investments and have previously made at least one such investment; or
  - b. have filed a Schedule 13D or 13G with the SEC that identifies the legal persons as members of a group that have agreed to act together for the purpose of acquiring, holding, voting or disposing of equity securities of an issuer in connection with a previous investment; and
- (ii) may make its investment or loan through a wholly owned subsidiary (except when the entity is a group of legal persons).

(B) An institutional investor is any individual or legal person that has at least \$50 million invested in securities in the aggregate in its portfolio or under management, including investments held by its wholly owned subsidiaries; provided that no participating members direct or otherwise manage the institutional investor's investments or have an equity interest in the institutional investor, either individually or in the aggregate, that exceeds 5% for a publicly owned entity or 1% for a nonpublic entity.

(C) A bank or insurance company is only the regulated entity, not its subsidiaries or other affiliates.

(D) A right of pre-emption means the right of a shareholder to acquire additional securities in the same company in order to avoid dilution when additional securities are issued, pursuant to:

- (i) any option, shareholder agreement, or other contractual right entered into at the time of a purchase of securities;
- (ii) the terms of the security purchased;
- (iii) the issuer's charter or by-laws; or
- (iv) the domestic law of a foreign jurisdiction that regulates the issuance of the securities.

(E) "Total equity securities" means the aggregate of the total shares of:

- (i) common stock outstanding of the issuer; and
- (ii) common stock of the issuer underlying all convertible securities outstanding that convert without the payment of any additional consideration.

#### **(5) Exceptions From Underwriting Compensation**

Notwithstanding paragraph (d)(1) above, the following items of value are excluded from underwriting compensation, provided that the member does not condition its participation in the public offering on an acquisition of securities under an exception and any securities purchased are purchased at the same price and with the same terms as the securities purchased by all other investors.

(A) Purchases and Loans by Certain Entities — Securities of the issuer purchased in a private placement or received as compensation for a loan or credit facility before the required filing date of the public offering pursuant to paragraph (b)(4) above by certain entities if:

(i) each entity:

a. either:

1. manages capital contributions or commitments of \$100 million or more, at least \$75 million of which has been contributed or committed by persons that are not participating members;
2. manages capital contributions or commitments of \$25 million or more, at least 75% of which has been contributed or committed by persons that are not participating members;
3. is an insurance company as defined in Section 2(a)(13) of the Securities Act or is a foreign insurance company that has been granted an exemption under this Rule; or
4. is a bank as defined in Section 3(a)(6) of the Exchange Act or is a foreign bank that has been granted an exemption under this Rule; and

b. is a separate and distinct legal person from any member and is not registered as a broker-dealer;

c. makes investments or loans subject to the evaluation of individuals who have a contractual or fiduciary duty to select investments and loans based on the risks and rewards to the entity and not based on opportunities for the member to earn investment banking revenues;

d. does not participate directly in investment banking fees received by any participating member for underwriting public offerings; and

e. has been primarily engaged in the business of making investments in or loans to other companies; and

(ii) all entities related to each member in acquisitions that qualify for this exception do not acquire more than 25% of the issuer's total equity securities during the review period in paragraph (d)(1), calculated immediately following the transaction.



(B) Investments In and Loans to Certain Issuers — Securities of the issuer purchased in a private placement or received as compensation for a loan or credit facility before the required filing date of the public offering pursuant to paragraph (b)(4) above by certain entities if:

(i) each entity:

- a. manages capital contributions or commitments of at least \$50 million;
- b. is a separate and distinct legal person from any member and is not registered as a broker-dealer;
- c. does not participate directly in investment banking fees received by the member for underwriting public offerings;
- and
- d. has been primarily engaged in the business of making investments in or loans to other companies; and

(ii) institutional investors beneficially own at least 33% of the issuer's total equity securities, calculated immediately prior to the transaction;

(iii) the transaction was approved by a majority of the issuer's board of directors and a majority of any institutional investors, or the designees of institutional investors, that are board members; and

(iv) all entities related to each member in acquisitions that qualify for this exception do not acquire more than 25% of the issuer's total equity securities, calculated immediately following the transaction.

(C) Private Placements With Institutional Investors — Securities of the issuer purchased in, or received as placement agent compensation for, a private placement before the required filing date of the public offering pursuant to paragraph (b)(4) above if:

(i) institutional investors purchase at least 51% of the "total offering" (comprised of the total number of securities sold in the private placement and received or to be received as placement agent compensation by any member);

(ii) an institutional investor was the lead negotiator or, if the terms were not negotiated, was the lead investor with the issuer to establish or approve the terms of the private placement; and

(iii) underwriters and related persons did not, in the aggregate, purchase or receive as placement agent compensation more than 20% of the "total offering" (excluding purchases by any entity qualified under paragraph (d)(5)(A) above).

(D) Acquisitions and Conversions to Prevent Dilution — Securities of the issuer if:

(i) the securities were acquired as the result of:

- a. a right of preemption that was granted in connection with securities that were purchased either:
  - 1. in a private placement and the securities are not deemed by FINRA to be underwriting compensation; or
  - 2. from a public offering or the public market; or
- b. a stock-split or a pro-rata rights or similar offering where the securities upon which the acquisition is based were acquired more than 180 days before the required filing date of the public offering pursuant to paragraph (b)(4) above; or
- c. the conversion of securities that have not been deemed by FINRA to be underwriting compensation; and

(ii) the only terms of the purchased securities that are different from the terms of securities purchased by other investors are pre-existing contractual rights that were granted in connection with a prior purchase;

(iii) the opportunity to purchase in a rights offering or pursuant to a right of preemption, or to receive additional securities as the result of a stock-split or conversion was provided to all similarly situated security holders; and

(iv) the amount of securities purchased or received did not increase the recipient's percentage ownership of the same generic class of securities of the issuer or of the class of securities underlying a convertible security calculated immediately prior to the investment, except in the case of conversions and passive increases that result from another investor's failure to exercise its own rights.



(E) Purchases Based On A Prior Investment History — Purchases of securities of the issuer if:

(i) the amount of securities purchased did not increase the purchaser's percentage ownership of the same generic class of securities of the issuer or of the class of securities underlying a convertible security calculated immediately prior to the investment; and

(ii) an initial purchase of securities of the issuer was made at least two years and a second purchase was made more than 180 days before the required filing date of the public offering pursuant to paragraph (b)(4) above.

#### **(e) Valuation of Non-Cash Compensation**

For purposes of determining the value to be assigned to securities received as underwriting compensation, the following criteria and procedures shall be applied.

##### **(1) Limitation on Securities Received Upon Exercise or Conversion of Another Security**

An underwriter and related person may not receive a security (including securities in a unit), a warrant for a security, or a security convertible into another security as underwriting compensation in connection with a public offering unless:

(A) the security received or the security underlying the warrant or convertible security received is identical to the security offered to the public or to a security with a bona fide independent market; or

(B) the security can be accurately valued, as required by paragraph (f)(2)(i) below.

##### **(2) Valuation of Securities That Do Not Have an Exercise or Conversion Price**

Securities that do not have an exercise or conversion price shall have a compensation value based on:

(A) the difference between:

(i) either the market price per security on the date of acquisition, or, if no bona fide independent market exists for the security, the public offering price per security; and

(ii) the per security cost;

(B) multiplied by the number of securities received or to be received as underwriting compensation;

(C) divided by the offering proceeds; and

(D) multiplied by one hundred.

##### **(3) Valuation of Securities That Have an Exercise or Conversion Price**

Options, warrants or convertible securities that have an exercise or conversion price ("warrants") shall have a compensation value based on the following formula:

(A) the public offering price per security multiplied by .65;

(B) minus the resultant of the exercise or conversion price per warrant less either:

(i) the market price per security on the date of acquisition, where a bona fide independent market exists for the security, or

(ii) the public offering price per security;

(C) divided by two;

(D) multiplied by the number of securities underlying the warrants;

(E) less the total price paid for the warrants;

(F) divided by the offering proceeds; and

(G) multiplied by one hundred;

(H) provided, however, that, notwithstanding paragraph (e)(4) below, such warrants shall have a compensation value of at least .2% of the offering proceeds for each amount of securities that is up to 1% of the securities being offered to the public (excluding securities subject to an overallotment option).

##### **(4) Valuation Discount For Securities With a Longer Resale Restriction**

A lower value equal to 10% of the calculated value shall be deducted for each 180-day period that the securities or underlying securities are restricted from sale or other disposition beyond the 180-day period of the lock-up restriction required by paragraph (g)(1) below. The transfers permitted during the lock-up restriction by paragraphs (g)(2)(A)(iii) through (iv) are not available for such securities.

#### **(5) Valuation of Items of Value Acquired in Connection with a Fair Price Derivative or Debt Transaction**

Any debt or derivative transaction acquired or entered into at a "fair price" as defined in paragraph (a)(9) and item of value received in or receivable in the settlement, exercise or other terms of such debt or derivative transaction shall not have a compensation value for purposes of determining underwriting compensation. If the actual price for the debt or derivative security is not a fair price, compensation will be calculated pursuant to this paragraph (e) or based on the difference between the fair price and the actual price.

#### **(f) Unreasonable Terms and Arrangements**

##### **(1) General**

No member or person associated with a member shall participate in any manner in a public offering of securities after any arrangement proposed in connection with the public offering, or the terms and conditions relating thereto, has been determined to be unfair or unreasonable pursuant to this Rule or inconsistent with any By-Law or any rule or regulation of FINRA.

##### **(2) Prohibited Arrangements**

Without limiting the foregoing, the following terms and arrangements, when proposed in connection with a public offering of securities, shall be unfair and unreasonable.

(A) Any accountable expense allowance granted by an issuer to the underwriter and related persons that includes payment for general overhead, salaries, supplies, or similar expenses of the underwriter incurred in the normal conduct of business.

(B) Any non-accountable expense allowance in excess of 3% of offering proceeds.

(C) Any payment of commissions or reimbursement of expenses directly or indirectly to the underwriter and related persons prior to commencement of the public sale of the securities being offered, except a reasonable advance against out-of-pocket accountable expenses actually anticipated to be incurred by the underwriter and related persons, which advance is reimbursed to the issuer to the extent not actually incurred.

(D) Any compensation by an issuer to a member or person associated with a member in connection with an offering of securities that is not completed according to the terms of agreement between the issuer and underwriter, except:

(i) the reimbursement of out-of-pocket accountable, bona fide expenses actually incurred by the member or person associated with a member; and

(ii) a termination fee or a right of first refusal, as set forth in a written agreement between the issuer and the participating member, provided that:

a. the agreement specifies that the issuer has a right of "termination for cause," which shall include the participating member's material failure to provide the underwriting services contemplated in the written agreement;

b. an issuer's exercise of its right of "termination for cause" eliminates any obligations with respect to the payment of any termination fee or provision of any right of first refusal;

c. the amount of any termination fee must be reasonable in relation to the underwriting services contemplated in the agreement and any fees arising from underwriting services provided under a right of first refusal must be customary for those types of services; and

d. the issuer shall not be responsible for paying the termination fee unless an offering or other type of transaction (as set forth in the agreement) is consummated within two years of the date the engagement is terminated by the issuer.

(E) Any right of first refusal provided to the underwriter or related persons to underwrite or participate in future public offerings, private placements or other financings that:

(i) has a duration of more than three years from the date of commencement of sales of the public offering or the termination date of the engagement between the issuer and underwriter; or

(ii) has more than one opportunity to waive or terminate the right of first refusal in consideration of any payment or fee.



(F) Any payment or fee to waive or terminate a right of first refusal regarding future public offerings, private placements or other financings provided to the underwriter and related persons that:

(i) has a value in excess of the greater of 1% of the offering proceeds in the public offering where the right of first refusal was granted (or an amount in excess of 1% if additional compensation is available under the compensation guideline of the original offering) or 5% of the underwriting discount or commission paid in connection with the future financing (including any overallotment option that may be exercised), regardless of whether the payment or fee is negotiated at the time of or subsequent to the original public offering; or

(ii) is not paid in cash.

(G) The terms or the exercise of the terms of an agreement for the receipt by the underwriter and related persons of underwriting compensation consisting of any option, warrant or convertible security that:

(i) is exercisable or convertible more than five years from the effective date of the offering;

(ii) is not in compliance with paragraph (e)(1) above;

(iii) has more than one demand registration right at the issuer's expense;

(iv) has a demand registration right with a duration of more than five years from the date of effectiveness or the commencement of sales of the public offering;

(v) has a piggyback registration right with a duration of more than seven years from the date of effectiveness or the commencement of sales of the public offering;

(vi) has anti-dilution terms that allow the underwriter and related persons to receive more shares or to exercise at a lower price than originally agreed upon at the time of the public offering, when the public shareholders have not been proportionally affected by a stock split, stock dividend, or other similar event; or

(vii) has anti-dilution terms that allow the underwriter and related persons to receive or accrue cash dividends prior to the exercise or conversion of the security.

(H) The receipt by the underwriter and related persons of any item of compensation for which a value cannot be determined at the time of the offering.

(I) When proposed in connection with the distribution of a public offering of securities on a "firm commitment" basis, any overallotment option providing for the overallotment of more than 15% of the amount of securities being offered, computed excluding any securities offered pursuant to the overallotment option.

(J) The receipt by a member or person associated with a member, pursuant to an agreement entered into at any time before or after the effective date of a public offering of warrants, options, convertible securities or units containing such securities, of any compensation or expense reimbursement in connection with the exercise or conversion of any such warrant, option, or convertible security in any of the following circumstances:

(i) the market price of the security into which the warrant, option, or convertible security is exercisable or convertible is lower than the exercise or conversion price;

(ii) the warrant, option, or convertible security is held in a discretionary account at the time of exercise or conversion, except where prior specific written approval for exercise or conversion is received from the customer;

(iii) the arrangements whereby compensation is to be paid are not disclosed:

a. in the prospectus or offering circular by which the warrants, options, or convertible securities are offered to the public, if such arrangements are contemplated or any agreement exists as to such arrangements at that time, and

b. in the prospectus or offering circular provided to security holders at the time of exercise or conversion; or

(iv) the exercise or conversion of the warrants, options or convertible securities is not solicited by the underwriter or related person, provided however, that any request for exercise or conversion will be presumed to be unsolicited unless the customer states in writing that the transaction was solicited and designates in writing the broker-dealer to receive compensation for the exercise or conversion.

(K) For a member to participate with an issuer in the public distribution of a non-underwritten issue of securities if the issuer hires persons primarily for the purpose of distributing or assisting in the distribution of the issue, or for the purpose of assisting in any way in connection with the underwriting, except to the extent in compliance with SEA Rule 3a4-1 and applicable state law.



## **(g) Lock-Up Restriction on Securities**

### **(1) Lock-Up Restriction**

In any public equity offering, other than a public equity offering by an issuer that can meet the requirements in paragraph (b)(7)(C)(i) or (ii) any common or preferred stock, options, warrants, and other equity securities of the issuer, including debt securities convertible to or exchangeable for equity securities of the issuer, that are unregistered and acquired by an underwriter and related person during 180 days prior to the required filing date, or acquired after the required filing date of the registration statement and deemed to be underwriting compensation by FINRA, and securities excluded from underwriting compensation pursuant to paragraph (d)(5)(A), (B), (C) and (E) above, shall not be sold during the offering, or sold, transferred, assigned, pledged, or hypothecated, or be the subject of any hedging, short sale, derivative, put, or call transaction that would result in the effective economic disposition of the securities by any person for a period of 180 days immediately following the date of effectiveness or commencement of sales of the public offering, except as provided in paragraph (g)(2) below.

### **(2) Exceptions to Lock-Up Restriction**

Notwithstanding paragraph (g)(1) above, the following shall not be prohibited:

(A) the transfer of any security:

(i) by operation of law or by reason of reorganization of the issuer;

(ii) to any member participating in the offering and the officers or partners thereof, if all securities so transferred remain subject to the lock-up restriction in paragraph (g)(1) above for the remainder of the time period;

(iii) if the aggregate amount of securities of the issuer held by the underwriter and related persons do not exceed 1% of the securities being offered;

(iv) that is beneficially owned on a pro-rata basis by all equity owners of an investment fund, provided that no participating member manages or otherwise directs investments by the fund, and participating members in the aggregate do not own more than 10% of the equity in the fund;

(v) that is not an item of value under paragraphs (c)(3)(B)(iii) through (vii) above;

(vi) that is eligible for the limited filing requirement in paragraph (b)(6)(A)(iv)b. and has not been deemed to be underwriting compensation under the Rule;

(vii) that was previously but is no longer subject to the lock-up restriction in paragraph (g)(1) above in connection with a prior public offering (or a lock-up restriction in the predecessor rule), provided that if the prior restricted period has not been completed, the security will continue to be subject to such prior restriction until it is completed; or

(viii) that was acquired subsequent to the issuer's initial public offering in a transaction exempt from registration under Securities Act Rule 144A; or

(B) the exercise or conversion of any security, if all securities received remain subject to the lock-up restriction in paragraph (g)(1) above for the remainder of the time period.

## **(h) Non-Cash Compensation**

### **(1) Definitions**

The terms "compensation," "non-cash compensation" and "offeror" as used in this paragraph (i) shall have the following meanings:

(A) "Compensation" shall mean cash compensation and non-cash compensation.

(B) "Non-cash compensation" shall mean any form of compensation received in connection with the sale and distribution of securities that is not cash compensation, including but not limited to merchandise, gifts and prizes, travel expenses, meals and lodging.

(C) "Offeror" shall mean an issuer, an adviser to an issuer, an underwriter and any affiliated person of such entities.

### **(2) Restrictions on Non-Cash Compensation**

In connection with the sale and distribution of a public offering of securities, no member or person associated with a member shall directly or indirectly accept or make payments or offers of payments of any non-cash compensation, except as provided in this provision. Non-cash compensation arrangements are limited to the following:

(A) Gifts that do not exceed an annual amount per person fixed periodically by the Board of Governors<sup>1</sup> and are not preconditioned on achievement of a sales target.

(B) An occasional meal, a ticket to a sporting event or the theater, or comparable entertainment which is neither so frequent nor so extensive as to raise any question of propriety and is not preconditioned on achievement of a sales target.

(C) Payment or reimbursement by offerors in connection with meetings held by an offeror or by a member for the purpose of training or education of associated persons of a member, provided that:

(i) associated persons obtain the member's prior approval to attend the meeting and attendance by a member's associated persons is not conditioned by the member on the achievement of a sales target or any other incentives pursuant to a non-cash compensation arrangement permitted by paragraph (h)(2)(D);

(ii) the location is appropriate to the purpose of the meeting, which shall mean an office of the issuer or affiliate thereof, the office of the member, or a facility located in the vicinity of such office, or a regional location with respect to regional meetings;

(iii) the payment or reimbursement is not applied to the expenses of guests of the associated person; and

(iv) the payment or reimbursement by the issuer or affiliate of the issuer is not conditioned by the issuer or an affiliate of the issuer on the achievement of a sales target or any other non-cash compensation arrangement permitted by paragraph (h)(2)(D).

(D) Non-cash compensation arrangements between a member and its associated persons or a company that controls a member company and the member's associated persons, provided that no unaffiliated non-member company or other unaffiliated member directly or indirectly participates in the member's or non-member's organization of a permissible non-cash compensation arrangement; and

(E) Contributions by a non-member company or other member to a non-cash compensation arrangement between a member and its associated persons, provided that the arrangement meets the criteria in paragraph (h)(2)(D).

A member shall maintain records of all non-cash compensation received by the member or its associated persons in arrangements permitted by paragraphs (h)(2)(C) through (E). The records shall include: the names of the offerors, non-members or other members making the non-cash compensation contributions; the names of the associated persons participating in the arrangements; the nature and value of non-cash compensation received; the location of training and education meetings; and any other information that proves compliance by the member and its associated persons with paragraphs (h)(2)(C) through (E).

#### **(i) Exemptions**

Pursuant to the Rule 9600 Series, the appropriate FINRA staff, for good cause shown after taking into consideration all relevant factors, may conditionally or unconditionally grant an exemption from any provision of this Rule to the extent that such exemption is consistent with the purposes of the Rule, the protection of investors, and the public interest.

---

<sup>1</sup> The current annual amount fixed by the Board of Governors is \$100.

Amended by SR-FINRA-2019-012 eff. Mar. 20, 2020.  
Amended by SR-FINRA-2014-006 eff. April 11, 2016.  
Amended by SR-FINRA-2014-003 eff. May 28, 2014.  
Amended by SR-FINRA-2014-004 eff. May 15, 2014.  
Amended by SR-FINRA-2010-060 eff. Dec. 15, 2010.  
Amended by SR-FINRA-2010-047 eff. Oct. 15, 2010.  
Amended by SR-FINRA-2009-062 eff. Oct. 19, 2009.  
Amended by SR-FINRA-2007-009 eff. Sep. 14, 2009.  
Amended by SR-FINRA-2009-046 eff. Aug. 17, 2009.  
Amended by SR-FINRA-2008-057 eff. Dec. 15, 2008.  
Amended by SR-FINRA-2008-039 eff. Dec. 15, 2008.  
Amended by SR-NASD-2006-068 eff. July 1, 2006.  
Amended by SR-NASD-2000-04 eff. March 22, 2004.  
Amended by SR-NASD-2003-139 eff. Oct. 15, 2003.  
Amended by SR-NASD-2003-75 eff. July 9, 2003.  
Amended by SR-NASD-2003-68 eff. April 7, 2003.  
Amended by SR-NASD-2001-46 eff. July 12, 2002.  
Amended by SR-NASD-2000-13 eff. April 16, 2001.  
Amended by SR-NASD-99-74 eff. June 20, 2000.  
Amended by SR-NASD-99-02 eff. Dec. 7, 1999.  
Amended by SR-NASD-99-01 eff. May 17, 1999.  
Amended by SR-NASD-98-81 eff. Dec. 21, 1998.  
Amended by SR-NASD-98-87 eff. Nov. 23, 1998.  
Amended by SR-NASD-97-38 eff. Dec. 15, 1997.  
Amended by SR-NASD-97-68 eff. Oct. 3, 1997.  
Amended by SR-NASD-97-28 eff. Aug. 7, 1997.  
Amended by SR-NASD-97-18 eff. Mar. 14, 1997.  
Amended by SR-NASD-97-15 eff. Mar. 4, 1997.  
Amended by SR-NASD-95-29 eff. Jan. 1, 1996.  
Amended by SR-NASD-95-18 eff. June 19, 1995.  
Amended by SR-NASD-94-61 eff. Mar. 2, 1995.  
Amended by SR-NASD-94-64 eff. Feb. 9, 1995.  
Amended by SR-NASD-94-12 eff. Mar. 7, 1994.  
Amended by SR-NASD-93-13 eff. Feb. 1, 1994.  
Amended by SR-NASD-93-45 eff. Dec. 13, 1993.  
Corporate Financing Rule adopted by SR-NASD-91-19 eff. Apr. 15, 1992.

Replaced *Interpretation of the Board of Governors — Review of Corporate Financing*, Art. III, Sec. 1 of the Rules of Fair Practice, which was amended eff. May 4, 1971; June 17, 1971; Mar. 19, 1982; amended by SR-NASD-83-27 eff. May 31, 1983; Aug. 4, 1983; July 13, 1984; Sept. 12, 1985; amended by SR-NASD-86-6 eff. Mar. 1, 1986; Oct. 14, 1988; amended by SR-NASD-88-13 eff. Jan. 1, 1989.

**Selected Notices:** 75-14, 76-27, 81-16, 81-17, 83-12, 83-15, 83-43, 83-44, 84-37, 85-6, 86-27, 88-32, 88-88, 88-92, 90-10, 92-28, 93-84, 93-88, 94-82, 95-22, 95-73, 95-95, 97-80, 98-88, 99-17, 99-50, 00-53, 02-26, 04-13, 08-57, 09-49, 14-22, 15-02, 20-10.

## VERSIONS

Mar 20, 2020 - Jun 29, 2020





> FINRA RULES > 5000. SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES  
> 5100. SECURITIES OFFERINGS, UNDERWRITING AND COMPENSATION > 5120. OFFERINGS OF MEMBERS' SECURITIES

## 5121. Public Offerings of Securities With Conflicts of Interest

The Rule

Notices

**This version is valid from May 08, 2019 through Sep 15, 2020.**

**Amendments have been announced but are not yet effective. To view other versions open the versions tab on the right.**

### (a) Requirements for Participation in Certain Public Offerings

No member that has a conflict of interest may participate in a public offering unless the offering complies with subparagraphs (1) or (2).

(1) There must be prominent disclosure of the nature of the conflict of interest in the prospectus, offering circular or similar document for the public offering, and one of the following conditions must be met:

(A) the member(s) primarily responsible for managing the public offering does not have a conflict of interest, is not an affiliate of any member that does have a conflict of interest, and meets the requirement of paragraph (f)(12)(E);

(B) the securities offered have a bona fide public market; or

(C) the securities offered are investment grade rated or are securities in the same series that have equal rights and obligations as investment grade rated securities.

(2) (A) A qualified independent underwriter has participated in the preparation of the registration statement and the prospectus, offering circular, or similar document and has exercised the usual standards of "due diligence" in respect thereto; and

(B) there must be prominent disclosure in the prospectus, offering circular or similar document for the offering of:

(i) the nature of the conflict of interest;

(ii) the name of the member acting as qualified independent underwriter; and

(iii) a brief statement regarding the role and responsibilities of the qualified independent underwriter.

### (b) Escrow of Proceeds; Net Capital Computation

(1) All proceeds from a public offering by a member of its securities shall be placed in a duly established escrow account and shall not be released therefrom or used by the member in any manner until the member has complied with subparagraph (2) hereof.

(2) Any member offering its securities pursuant to this Rule shall immediately notify FINRA when the public offering has been terminated and settlement effected and shall file with FINRA a computation of its net capital computed pursuant to the provisions of SEA Rule 15c3-1 (the net capital rule) as of the settlement date. If at such time its net capital ratio as so computed is more than 10:1 or, net capital fails to equal 120 percent of the minimum dollar amount required by Rule 15c3-1 or, in the event the member calculates its net capital requirement using the alternative standard (set forth in Rule 15c3-1(a)(1)(ii)), its net capital is less than seven percent of aggregate debit items as computed in accordance with Rule 15c3-3a, all monies received from sales of securities of the public offering must be returned in full to the purchasers thereof and the offering withdrawn, unless the member has obtained from the SEC a specific exemption from the net capital rule. Proceeds from the sales of securities in the public offering may be taken into consideration in computing net capital ratio for purposes of this paragraph.

(3) Any member offering its securities pursuant to this Rule shall disclose in the registration statement, offering circular or similar document a date by which the offering is reasonably expected to be completed and the terms upon which the proceeds will be released from the escrow account described in paragraph (b)(1).

### (c) Discretionary Accounts

Notwithstanding Rule 3260, no member that has a conflict of interest may sell to a discretionary account any security with respect to which the conflict exists, unless the member has received specific written approval of the transaction from the account holder and retains documentation of the approval in its records.

### (d) Application of Rule 5110