Proskauer

# Broker-Dealer Beat: Foreign Finders

**June 2015**

**Foreign Finders**

The longstanding rules on foreign finders – when a brokerage firm can pay transaction-based compensation to a non-registered foreign finder – will be incorporated into new FINRA Rule 2040, effective August 24, 2015.

This is a good time for firms to review their processes around foreign finders. For arrangements that go beyond the Rule's narrow scope, alternatives may include registering an individual as a foreign associate or establishing a foreign branch.

To recap, FINRA Rule 2040(c) (and predecessor NASD Rule 1060(b) and NYSE interp. 345 (a)(i)/03) permits payment of transaction-related compensation to a non-registered foreign finder where the finder's sole involvement is the initial referral to the member of non-US customers, and the firm complies with all of the following conditions:

- The firm has assured itself that the finder is not required to register as a US broker-dealer, is not subject to a statutory disqualification and the compensation arrangement does not violate applicable foreign law;

- The finder and the customer are foreign nationals or foreign entities domiciled abroad;

- Customers receive a descriptive document, similar to what’s required under the Advisers Act's Brochure Rule, disclosing what compensation is being paid to finders, and customers provide a written acknowledgment of the compensation arrangement, which the firm must maintain;

- Terms of payments to finders are recorded on the firm's books; and

- The transaction confirmation indicates that a finder’s fee is being paid pursuant to an agreement.

Provided the Rule's conditions are met, a firm can pay one-time or on-going transaction-related compensation to the non-registered foreign finder based on the business of non-US customers referred by that finder. The accounts referred by the foreign finder must be carried on the member's books.

The Supplementary Material (.01) under Rule 2040 requires the firm to make a reasonably supported determination that the proposed activities would not require the recipient of the payments to register as a broker-dealer. Where payments are on-going, the determination should be reviewed periodically. Thus, firms may wish to review the adequacy of their current procedures for obtaining, documenting and periodically reviewing the required assurances about the foreign finder and the foreign customer, as well as the mechanisms for assuring that finders do not engage in activities beyond the initial referral.

Since activities beyond the initial referral are not permitted by the Rule, they could subject the finder to registration, or in the case of an individual, the requirement to become an associated person of a member, subject to its supervision. A member firm paying an unregistered finder whose activities exceed the permissible scope of the foreign finder exemption would be in violation of FINRA Rule 2040.

Where an arrangement with a foreign individual goes beyond initial referrals, the member firm may register that individual as a foreign associate under NASD Rule 1100. Foreign associates must conduct all of their activities outside the US and cannot engage in any securities activities with US persons. Although deemed an associated person for whom a Form U4 must be filed, a foreign associate is not required to pass a qualifying examination. For arrangements with foreign groups whose activities for foreign customers go beyond the initial referral to the member, registration of a foreign branch may be an alternative. To the extent a foreign finder solicits or negotiates with US persons, entering into a 15a-6 agreement may be a viable alternative.