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FINRA IPO Allocation Rule; investment funds must now consider compliance

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Abstract

Purpose

The purpose of this paper is to describe the Financial Industry Regulatory Authority's new rule for IPO allocation and the requirements for compliance with the rule.

Design/methodology/approach

The paper provides an overview of the new FINRA Rule 5131, containing, among other things, provisions that prohibit the "spinning" of IPO shares to certain present and prospective investment banking clients. Specifically, the paper outlines the new regulations on "quid pro quo" allocations, "spinning", "flipping" and IPO pricing and trading practices. The paper also provides detailed guidance to broker-dealers regarding their obligations under the rule.

Findings

The proposed new rule is intended to prevent the following types of conduct: the allocation of IPO shares as consideration or inducement for the payment of excessive compensation for other services provided by the member; the acceptance of market orders of IPO shares prior to the development of a secondary market; the allocation of IPO shares to an executive officer or director of a company on the condition that the officer or director send the company's investment banking business to the member, or as consideration for investment banking services previously rendered; and the imposition of a penalty on registered representatives whose retail customers have "flipped" IPO

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The paper provides practical guidance from experienced regulatory lawyers regarding an important proposed change.

Keywords

Financial services

Regulation

Investment funds

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