OCTOBER 2003

Notices to Members

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Notices to Members (December 1996 to current) are also available on the Internet at *www.nasd.com*.

Special Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Executive Representatives

Senior Management

KEY TOPICS

NASD Board of Governors

INFORMATIONAL

Board of Governors Nominees

Nominees for NASD Board of Governors

The Annual Meeting of members of NASD will be held on January 6, 2004. The formal notice of the meeting, including the precise date, time, and location of the Annual Meeting, will be mailed on or about December 2, 2003.

The individuals nominated by the NASD National Nominating Committee (NNC) for election to the NASD Board of Governors are identified in this *Special Notice.* Pursuant to Section 10 of Article VII of the NASD By-Laws, a person who has not been so nominated for election to the Board of Governors may be included on the ballot for the election of Governors if:

(a) within 45 days of the date of this *Special Notice* such person presents to the Secretary of NASD petitions in support of such nomination duly executed by at least 3 percent of the members of NASD. As of the date of this *Special Notice*, NASD has 5331 voting members; therefore, the applicable 3 percent threshold is 160 members. If, however, a candidate's name appears on a slate of nominees, the slate must be endorsed by 10 percent of NASD's voting members. The applicable 10 percent threshold is 533 members; and

(b) the Secretary certifies that such petitions have been duly executed by the Executive Representatives of the requisite number of members of NASD, and the person being nominated satisfies the classification of the governorship to be filled based on the information provided by the person as is reasonably necessary for the Secretary to make the certification.

Pursuant to Article VII, Section 4, of the NASD By-Laws, the NASD Board must consist of no fewer than 17 and no more than 27 Governors. The number of Governors within this range is set by the Board. On July 1, 2003, the NASD Executive Committee approved a reduction in the size of the Board from 25 to 21 Governors, effective with the January 6, 2004 Annual Meeting, to eliminate the positions occupied by members who simultaneously serve on the Board of Directors of The Nasdaq Stock Market, Inc., and whose terms are expiring. In August of 2002, the Board took a similar action by reducing the size of the Board for 2003 by three Governors who also served on the NASDAQ Board and who were not eligible for re-election. Additionally, pursuant to its authority under Article VII, Section 5(d) of the NASD By-Laws, the Board determined in August of 2002 that the remaining NASD Board members who simultaneously served on the NASDAQ Board and who were eligible to serve an additional term on the NASD Board would, if re-elected, serve a term of one additional year on the NASD Board or until NASDAQ was able to operate other than as a facility of NASD, whichever were to occur first. Governors Baldwin, Romano, and Simmons were elected to the one-year term on the NASD Board at the December 5, 2002 Annual Meeting. Each of these Governors is now ineligible for re-election. A fourth NASD Board member who simultaneously serves on the NASDAQ Board and whose three-year term on the NASD Board is expiring, Governor Sodhani, is also ineligible for re-election. Accordingly, the size of the Board has been reduced to 21 Governors.

On January 6, 2004, members will elect four Governors, one of whom will occupy an Industry position on the Board, and three of whom will occupy Public positions on the Board.

Questions regarding this *Special Notice* may be directed to:

Barbara Z. Sweeney
Senior Vice President and Corporate Secretary
NASD
1735 K Street, NW
Washington, DC 20006-1500
(202) 728-8062

or

T. Grant Callery
Executive Vice President and General Counsel
NASD
1735 K Street, NW
Washington, DC 20006-1500
(202) 728-8285

NASD Board of Governors Nominees

The following four persons (see attached profiles) have been nominated by the NNC to serve on the Board of Governors of NASD for a term of three years or until their successors are duly elected or qualified. Terms of office run from January 6, 2004, to January 2007.

Terms of Office 2004-2007

INDUSTRY

William C. Alsover, Jr.	Chairman, Centennial Securities Company, Inc. (Small Firm Representative)

PUBLIC

Charles A. Bowsher [1]	Former Comptroller General of the U.S.
Joel Seligman	Dean, Washington University School of Law
Sharon P. Smith	Dean, College of Business Administration, Fordham University

NASD Profile of Board Nominee for Industry Governor

Industry

William C. Alsover, Jr. is Chairman of Centennial Securities Company, Inc., a full service broker/dealer located in Grand Rapids, Michigan. Prior to joining Centennial, Mr. Alsover was with Fahnestock & Company. Mr. Alsover is currently Chairman of the Small Firm Advisory Board and serves on the Securities Advisory Committee, Office of Financial and Insurance Services for the State of Michigan. He has served on several industry committees, including the Securities Industry Association (SIA) Investor Education and Local Firms Committees, the New York Stock Exchange's Committee dealing with day trading and margin requirements. Mr. Alsover is the former Chairman of the SIA Local Firm Committee, and a former member of the NASD Chicago District 8 District Business Conduct Committee. He received his B.A. from Michigan State University.

NASD Profiles of Board Nominees for Public Governors

Public

Charles A. Bowsher is the former Comptroller General of the United States and head of the General Accounting Office (GAO). Mr. Bowsher was appointed to his 15-year term in 1981 by President Reagan. Prior to this appointment, Mr. Bowsher was associated with Arthur Andersen & Co. for 25 years, and also served as Assistant Secretary of the Navy for Financial Management. He served as Chairman of the Public Oversight Board and currently serves on the corporate boards of American Express Bank, DeVry, Inc., the Washington Mutual Investors Fund, and S.I. International, Inc. He is a trustee of the Center for Naval Analysis, the Logistics Management Institute, the United States Navy Memorial Foundation, the Corcord Coalition, the Hitachi Foundation and serves on the advisory boards at several universities. He is the recipient of honorary doctorate degrees from five universities. Mr. Bowsher graduated from the University of Illinois and received an M.B.A. from the University of Chicago after serving two years in the U.S. Army.

Joel Seligman is the Dean and Ethan A.H. Shepley University Professor at the Washington University School of Law. Before beginning his tenure as Dean in 1999, Mr. Seligman served as the Dean of the University of Arizona College of Law. He has also previously served on the law faculty of the universities of Michigan, George Washington and Northeastern. Since beginning as Dean at Washington University School of Law in 1999, Mr. Seligman served as Reporter for the National Conference of Commissioners on Uniform State Law, was Chair of the Securities and Exchange Commission Advisory Committee on Market Information; and has served as a member of the American Institute of Certified Public Accountants Professional Ethics Executive Committee. He is the author or co-author of 20 books and over 35 articles on legal issues related to securities and corporations. He is the co-author of *Fundamentals of Securities Regulation* and the casebook, *Securities Regulation,* which he co-wrote with John Coffee. His book, *The Transformation of Wall Street: A History of the Securities and Exchange Commission and Modern Corporate Finance,* is widely regarded as the leading history of the Commission. He received his bachelor's degree magna cum laude from the University of California Los Angeles and his law degree cum laude from Harvard University School of Law.

Sharon P. Smith is the Dean of the Schools of Business and of the Business Faculty at Fordham University, where she is also a Professor of Management Systems. Ms. Smith joined Fordham University in 1990 after serving as a Visiting Senior Research Economist at Princeton University from 1988 to 1990. Prior to this, she worked at American Telephone & Telegraph Co. for six years as a District Manager in various capacities, such as Corporate Strategy and Development, Labor Relations, and Economic Analysis Section. Before joining AT&T, she was a Senior Economist at the Federal Reserve Bank of New York. Ms. Smith currently serves as a public member of the Security Traders Association (STA) Board, the STA Foundation Advisory Council, as well as a variety of other professional organizations and associations. She holds a Ph.D. in Economics from Rutgers University.

Governors with Terms Expiring in January 2004

Industry

William C. Alsover, Jr.	Chairman, Centennial Securities Company, Inc. (Small Firm Representative)
Douglas L. Kelly[2]	A.G. Edwards & Sons, Inc. (Chair of the National Adjudicatory Council)
Richard C. Romano*	Chairman, Romano Brothers & Co.
Hardwick Simmons*	Retired Chairman and CEO The Nasdaq Stock Market, Inc.

Non-Industry

H. Furlong Baldwin*	Chairman (retired), Mercantile Bankshares Corporation
Arvind Sodhani*	Vice President and Treasurer, Intel Corporation

Public

Brian T. Borders	Borders Law Group
Charles A. Bowsher	Former Comptroller General of the U.S.
Sharon P. Smith	Dean, College of Business Administration, Fordham University

* Not eligible for re-election

Governors with Terms Expiring in January 2005

Industry

John W. Bachmann	Managing Partner, Edward D. Jones & Company
Richard F. Brueckner	Chief Executive Officer, Pershing, LLC (Representative of a Clearing Firm)
Raymond A. Mason	Chairman and CEO, Legg Mason Wood Walker, Inc. (Representative of a Regional Retail Firm)

Non-Industry

Harry P. Kamen*	Retired Chairman and Chief Executive Officer Metropolitan Life Insurance Company (Representative of an Insurance Company)

Public

James E. Burton	Chief Executive Officer, World Gold Council
Sir Brian Corby	Chairman (retired), Prudential Assurance Company
John Rutherfurd, Jr.	President and CEO, Moody's Corporation

* Not eligible for re-election

Governors with Terms Expiring in January 2006

Industry

M. LaRae Bakerink*	Chief Executive Officer Westfield Bakerink Brozak, LLC
David A. DeMuro	Managing Director, Director of Global Compliance and Regulation, Lehman Brothers, Inc. (Representative of a National Retail Firm)

Non-Industry

John J. Brennan	Chairman and CEO, The Vanguard Group (Representative of an Issuer of Investment Company Shares)
Eugene M. Isenberg*	Chairman and CEO, Nabors Industries, Inc.

Public

Kenneth M. Duberstein*	Chairman and CEO, The Duberstein Group, Inc.

* Not eligible for re-election

Endnotes

1 Elected in July 2003 to fill a vacancy on the Board.

2 The Chair of the National Adjudicatory Council serves a one-year term on the NASD Board.

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Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Executive Representatives
Legal & Compliance
Operations
Registered Representative
Registration
Senior Management

KEY TOPICS

IARD℠
Maintenance Fees
Registration
Renewals
Web CRD®

ACTION REQUIRED

Broker/Dealer and Investment Adviser Renewals

Broker/Dealer, Registered Representative, Investment Adviser Firm, and Investment Adviser Representative Renewals for 2004; Payment Deadline: December 5, 2003

Executive Summary

The 2004 NASD Broker/Dealer and Investment Adviser Renewal Program will begin November 3, 2003, when online Preliminary Renewal Statements are made available to all firms on Web CRD/IARD. This annual program simplifies the registration renewal process for more than 24,000 Broker/Dealer (BD) and Investment Adviser (IA) firms and approximately 700,000 registered representatives and investment adviser representatives with the payment of one amount to NASD by the published deadline. On **October 27, 2003,** firms may start submitting post-dated Forms U5, BDW, and Schedule E via Web CRD. Post-dated filings that are submitted by October 31, 2003, will not appear on the firm's Preliminary Renewal Statement. Joint (Broker/Dealer-Investment Adviser) firms may begin submitting post-dated ADV-Ws via IARD on **November 3, 2003.**

Renewal Statements will include the following fees: NASD Web CRD/IARD System Processing Fees and NASD Branch Office Fees, as well as New York Stock Exchange (NYSE), American Stock Exchange (Amex), Chicago Board Options Exchange (CBOE), International Securities Exchange (ISE), Pacific Exchange (PCX), and Philadelphia Stock Exchange (PHLX) Maintenance Fees. The statement will also include state Broker/Dealer, registered representatives, and, if applicable, state Investment Adviser firm and representative Renewal Fees.

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Members should read this *Notice to Members;* any instructions posted to NASD's Web Site at *www.nasdr.com/3400.asp,* especially the Registration and Disclosure Fall *Bulletin,* which will be a special Renewal Program edition; the Investment Adviser Web Site, if applicable, at *www.iard.com/renewals.asp;* and any mailed information to ensure continued eligibility to do business as of January 1, 2004. Members should also visit the Renewal Program Web Pages at *www.nasdr.com/3400_renewals_intro.asp* to review Renewal information.

Questions/Further Information

Questions concerning this *Notice* may be directed to the Gateway Call Center at (301) 869-6699.

Preliminary Renewal Statements

Beginning November 3, 2003, Preliminary Renewal Statements will be available for viewing and printing in Web CRD/IARD for all entitled users. The statements will include the following fees: Web CRD/IARD System Processing Fees; NASD Branch Office Fees; NYSE, Amex, CBOE, ISE, PCX, and PHLX Maintenance Fees; state Agent Renewal Fees; state Broker/Dealer, and, if applicable, Investment Adviser Firm and Representative Renewal Fees. NASD must receive **full** payment of the November Preliminary Renewal Statement amount **no later than December 5, 2003.**

If payment is **not** received by the December 5, 2003, Payment Due Date, the firm will be assessed a **Renewal Payment Late Fee.** This Renewal Payment Late Fee will be included as part of the firm's Final Renewal Statement and will be calculated as follows: 10% of a member firm's cumulative Final Renewal Assessment or $100, whichever is greater, with a cap of $5,000. Please see *Notice to Members (NtM) 02-48* at *www.nasdr.com/pdf-text/0248ntm.pdf* for more details.

Fees

A fee of $30 will be assessed for each person who renews his/her registration with **any regulator** through Web CRD. Please see *NTM 02-41* at *www.nasdr.com/pdf-text/0241ntm.pdf* for more details. Firms can access a listing of agents for whom they were assessed a fee in their Preliminary Renewal Statement by requesting the Renewals-Firm Renewal Roster. The report will be available when the Renewal Statements are available.

An NASD **Branch Office Assessment Fee** of $75 per branch will be assessed based on the number of active NASD branches at the time the Preliminary Renewal Statement is generated.

The **IARD Firm System Fee** of $100 will be assessed for every state-registered Investment Adviser firm who renews through the IARD Program.

The **RA Renewal System Processing Fee** of $45 will be assessed for every Investment Adviser Representative who renews through the IARD Program.

This year, as last year, NASD Personnel Assessment Fees will **not** be assessed through the NASD Renewal Program. NASD will mail all NASD member firms a separate billing for this during the first quarter of 2004.

Renewal Fees for NYSE, Amex, CBOE, PCX, ISE, PHLX, and state registrations are also assessed in the Preliminary Renewal Statement. NYSE, Amex, CBOE, PCX, ISE, and PHLX Maintenance Fees and state Renewal Fees collected by NASD for firms that are registered with those exchanges and jurisdictions, as well as NASD Renewal Fees, are based on the number of NASD, NYSE, Amex, CBOE, PCX, ISE, and PHLX and state-registered personnel employed by the member firm.

Some participating jurisdictions may require steps beyond the payment of Renewal Fees to NASD to complete the Broker/Dealer or Investment Adviser renewal process. Firms should contact each jurisdiction directly for further information on its renewal requirements (see the SRO/State Directory at *www.nasdr.com/3450.htm.*

For detailed information regarding Investment Adviser Renewals, you may also visit the Investment Adviser Web Site, *www.iard.com.* A matrix that includes a list of Investment Adviser Renewal Fees for jurisdictions that participate in the 2004 IARD Renewal Program is posted at *www.iard.com/pdf/reg_directory.pdf.*

Renewal Payment

Firms have four (4) payment methods available to pay 2004 Renewal Fees:

- Web CRD/IARD E-Pay,
- Wire transfer,
- Check, or
- Transfer of the entire amount from the firm's Daily to Renewal Account. (Note: The entire amount of the payment must be available.)

Web E-Pay Instructions

The E-Payment application is accessible from either the NASD *(www.nasdr.com/3400.asp)* or IARD *(www.iard.com)* Web Sites and from both the Preliminary and Final Renewal Statements and allows firms to make an ACH payment from a designated bank account to their Web CRD/IARD Renewal Account. In order for funds to be posted to the firm's Renewal Account by December 5, 2003, payment must be submitted electronically, **no later than** 8:30 p.m., Eastern Time (ET), on **December 3, 2003.**

Check Instructions

The check should be drawn on the member firm's account, with the firm's CRD Number included on the front of the check, along with the word "Renewals" in the memo line.

Firms should mail their Renewal Payment, along with the first page of their online Renewal Statement, directly to:

U.S. Mail

NASD, CRD-IARD

P.O. Box 7777-W8705

Philadelphia, PA 19175-8705

(Note: This P.O. Box will not accept courier or overnight deliveries)

or

Express/Overnight Delivery

NASD, CRD-IARD

W8705

c/o Mellon Bank, Rm 3490

701 Market Street

Philadelphia, PA 19106

Telephone No: (301) 869-6699

Member firms should use the blue, pre-addressed Renewal Payment envelope that they should receive the first week of November; or, if using their own payment envelope, firms should use the full address, as noted above, including the "W8705" number.

Please note: The addresses for Renewal Payments are different from the addresses for funding your firm's CRD or IARD Daily Account.

To ensure prompt processing of your Renewal Payment check:

- Include a printout of the first page of your Preliminary Renewal Statement with payment.
- Do **not** include any other forms or fee submissions.
- Write your Firm's CRD Number and the word "Renewals" on the check memo line.
- Be sure to send your payment either in the blue pre-addressed Renewal Payment envelope that will be mailed to you or write the address on the envelope exactly as noted above.

Wire Payment Instructions

Firms may wire full payment of the Preliminary Renewal Statement by requesting their bank to initiate the wire transfer to: The Riggs National Bank in Washington, DC Firms should provide their bank the following information:

Transfer funds to:	**Riggs National Bank in Washington, D.C.**
ABA Number:	**054-000030**
Beneficiary:	**NASD**
NASD Regulation Account Number:	**086-761-52**
Reference Number:	**Firm CRD Number and the word "Renewals"**

To ensure prompt processing of a Renewal Payment by wire transfer:

- Remember to inform the bank that the funds are to be credited to the **NASD Bank Account,**
- Provide the Firm's CRD Number and the word, "Renewals" as reference only, and
- Record the Confirmation Number of the wire transfer provided by the bank.

Transfer of Funds Instructions

Firms may also call the Gateway Call Center at (301) 869-6699 and request that a transfer of the **full** Renewal balance be transferred from the firm's Daily to Renewal Account. The firm must have the available funds in its Daily Account in order for the transfer to be processed.

Members are advised that failure to return full payment of their Preliminary Renewal Statement to NASD by the December 5, 2003, deadline could cause a member to become ineligible to do business in the jurisdictions effective January 1, 2004.

Renewal Reports

Beginning November 3, 2003, the Renewal Reports are available to request, print, and/or download via Web CRD. There will be three reports available for reconciliation with the Preliminary Renewal Statement. All three reports will also be available as downloads:

Firm Renewal Report – applicable to Broker/Dealer and Investment Adviser firms. This report lists individuals included in the 2004 Renewal Program processing and includes Billing Codes (if they have been supplied by the firm).

Branches Renewal Report – applicable to NASD members. This report lists each branch registered with NASD for which the firm is being assessed a fee. Firms should use this report to reconcile their records for Renewal purposes.

Approved AG Reg Without NASD Approval Report – applicable to NASD members. This report contains all individuals who are not registered with NASD but are registered with one or more jurisdictions. The report should be used throughout the year, including during the annual Renewal Program, as an aid for firms to reconcile personnel registrations. Firms should request this report in October to determine if any NASD registrations need to be requested or jurisdictions terminated prior to Renewal processing for the Preliminary Renewal Statement on November 1. Note: any post-dated U5, BDW, and/or Schedule E terminations submitted by 11:00 p.m., ET, on October 31, 2003, will not appear on the firm's Preliminary Renewal Statement.

Filing Forms U5

Firms may begin submitting post-dated U5 filings on October 27, 2003. If Forms U5 (either Full or Partial) are filed electronically via Web CRD by 11:00 p.m., ET, October 31, 2003, for Agents/Investment Adviser Representatives (RAs) terminating in one or more jurisdiction, those Renewal Fees will **not** be included on the firm's Preliminary Renewal Statement.

The deadline for electronic filing of Forms U5 for firms that want to terminate an agent affiliation before year-end 2003 is 6:00 p.m., ET, on December 20, 2003. Firms may file both Partial and Full Forms U5 with a post-dated **termination date of December 31, 2003.** (This is the only date that can be used for a post-dated Form U5.) The deadline for submission of all EFT (electronic file transfer) filings is also December 20, 2003 (2:00 p.m., ET). For more detailed information on post-dated Forms U5, see the section titled "Post-Dated Form Filings" below.

It is important for firms to be aware that once a post-dated Form U5 is filed for an individual, the firm will not be able to submit either a U4 or U5 Amendment to update disclosure until on or after January 2, 2004.

Post-Dated Form Filings

Firms can begin electronically filing post-dated Forms U5, BDW, and Schedule E via Web CRD on **October 27, 2003.** This functionality allows firms to file a termination form on or after October 27, with a termination date of December 31, 2003. Firms that submit post-dated U5, BDW, and/or Schedule E termination filings by 11:00 p.m., ET, on October 31, 2003, *will not* be assessed Renewal Fees for the terminated jurisdictions on their Preliminary Renewal Statement in November. Joint (Broker/Dealer-Investment Adviser) firms may begin to submit post-dated ADV-Ws on **November 3, 2003.**

Firms that submit post-dated termination filings on or after **November 3, 2003,** will not be assessed Renewal Fees for the terminated jurisdictions on the Final Renewal Statement in January. If a credit is due the firm, it will be transferred to the firm's Daily Account in conjunction with Renewal processing and will be posted there on January 2, 2004. In the case of an overpayment, the firm's Final Renewal Statement will read "Amount Paid in Full," and the deposit will be posted under the Transfer Detail of the firm's Daily Account.

Firms may submit Forms U5, BDW, Schedule E, and ADV-W (both partial and full terminations) until **December 20, 2003,** with a post-dated termination date of **December 31, 2003.** (This is the only date that can be used for a post-dated form filing.) If a Form U5, BDW, Schedule E, or ADV-W indicates a termination date of December 31, 2003, a registered representative, Broker/Dealer, Investment Adviser (firm), or Investment Adviser representative (RA) may continue doing business in the jurisdiction until the end of the calendar year without being assessed 2004 Renewal Fees. Firms are encouraged to access the individual's or firm's form filing history after a termination filing is submitted to ensure that electronic Forms U5, BDW, Schedule E, and ADV-W have been successfully filed.

Members should exercise care when submitting post-dated Forms U5, BDW, Schedule E, and ADV-W. CRD and IARD will systematically process these forms as they are submitted and NASD **cannot** withdraw a post-dated termination once submitted and processed. If a post-dated, **full** Form U5, BDW, or ADV-W has been submitted but the firm decides it does not want to terminate registration, then a new Form U4, Form BD, or Form ADV must be submitted on or after January 2, 2004, to re-register the representative or firm with jurisdictions. All applicable registration fees will be assessed. If a post-dated **partial** Form U5, BDW, or ADV-W has been submitted but the firm decides it does not want to terminate registration(s), then a Form U4 Amendment, Form BD Amendment, or ADV Amendment, as appropriate, must be submitted on or after January 2, 2004, to re-request registration with those jurisdictions. All applicable registration fees will be assessed.

Filing Form BDW

The CRD Phase II Program allows firms requesting Broker/Dealer termination (either full or partial) to electronically file their Forms BDW via Web CRD. Firms that file either a Full or Partial Form BDW by 11:00 p.m., ET, October 31, 2003, will avoid the assessment of the applicable Renewal Fees on their Preliminary Renewal Statement, provided that the regulator is a CRD Phase II participant. Currently, there are four regulators that participate in Web CRD Renewals for agent fees, but they **do not** participate in CRD Phase II for BD terminations:

- American Stock Exchange
- New York Stock Exchange
- Pacific Exchange
- Philadelphia Stock Exchange

Firms requesting termination with any of the above-listed regulators must submit a paper Form BDW directly to the regulator, as well as submit one electronically to Web CRD.

The deadline for electronic filing of Forms BDW for firms that want to terminate an affiliation before year-end 2003 is 6:00 p.m., ET, December 20, 2003. This same date applies to the filing of Forms BDW with regulators that are not Phase II participants. For information regarding the post-dating of Forms BDW with the termination date of December 31, 2003, see the section titled "Post-Dated Form Filings."

Filing Forms ADV to Cancel Notice Filings or Forms ADV-W to Terminate Registrations

Joint (Broker/Dealer-Investment Adviser) firms that file a Form ADV Amendment, unmarking a state (generating the status of "Removal Requested at End of Year"), by 11:00 p.m., ET, October 31, 2003, will avoid the assessment of the applicable Renewal Fees on their Preliminary Renewal Statement. **Post-dated Forms ADV-W cannot be submitted until November 3, 2003.**

The deadline for electronic filing of Form ADV Amendments or Forms ADV-W for firms that want to cancel a Notice Filing or terminate a state registration before year-end 2003 is 6:00 p.m., ET, December 20, 2003. For information regarding post-dating Form ADV-W with the termination date of December 31, 2003, for state registrations see the "Post-Dated Form Filings" section.

Removing Open Registrations

Throughout the year, firms have access to the "Approved AG Reg Without NASD Approval" Report via Web CRD. This report identifies agents whose NASD registrations are either terminated or have been changed to a "purged" status due to the existence of a deficient condition (*i.e.,* Exams or Fingerprints) but maintain an approved registration with a state. Member firms should use this report to terminate obsolete state registrations through the submission of Forms U5 or reapply for NASD licenses through the filing of a Form U4 Amendment. This report should aid firms in the reconciliation of personnel registrations prior to year's end and should be requested prior to October 27, 2003. Requesting this report will enable firms to identify individuals who can be terminated by October 31, 2003, to avoid being charged for those individuals on their Preliminary Renewal Statement. Firms may continue to terminate individuals until the December 20, 2003, 6:00 p.m., ET, deadline.

Final Renewal Statements

Beginning January 2, 2004, NASD will make available Final Renewal Statements via Web CRD and IARD. These statements will reflect the final status of Broker/Dealer, Registered Representative (AG), Investment Adviser Firm, and Investment Adviser Representative (RA) registrations, and/or Notice Filings as of December 31, 2003. Any adjustments in fees owed as a result of registration terminations, approvals, Notice Filings, or transitions subsequent to the processing/posting of the Preliminary Renewal Statement will be made in the Final Renewal Statement on Web CRD.

If a firm has more agents, branch offices, or jurisdictions registered and/or Notice Filed on Web CRD and IARD at year-end than it did when the Preliminary Renewal Statement was generated, additional Renewal Fees will be assessed.

If a firm has fewer agents, branch offices, or jurisdictions registered and/or Notice Filed at year-end than it did when the Preliminary Renewal Statement was generated, a credit/refund will be issued. As of January 2, 2004, overpayments will be transferred to firms' Daily Accounts. Firms that have a credit (sufficient) balance in their Daily Account may request a refund by contacting the Gateway Call Center at (301) 869-6699 or faxing a written request signed by the designated signatory to the User Support Unit at (240) 386-4849.

After January 2, 2004, NASD member firms should access Web CRD Reports to request the **Firm Renewal Report,** which will list all renewed personnel with the NASD, NYSE, Amex, CBOE, PCX, ISE, PHLX, and each jurisdiction. Agents and RAs whose registrations are "approved" in any of these jurisdictions during November and December will be included in this report. Registrations that are "pending approval" or are "deficient" at year's end will not be included in the Renewal Program. Member firms will also be able to request the **Branches Renewal Report** that lists all NASD branches for which they have been assessed. Download versions of these reports will also be available.

Firms have until **February 6, 2004,** to report any discrepancies on the Renewal Reports. All discrepancies should be reported, in writing, to NASD. This is also the deadline for **receipt of final payment.** Specific information and instructions concerning the Final Renewal Statements and Renewal Reports will appear in the January 2004 *Notices to Members.* Firms may also refer to the Fall Registration and Disclosure *Bulletin,* which is devoted entirely to the 2004 NASD Renewal Program. Firms will be able to access the information at any time by viewing the CRD Information Pages of the NASD Web Site at *www.nasdr.com/3400_publications.asp.*

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Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Executive Representatives
Legal & Compliance
Registered Representatives
Senior Management

KEY TOPICS

Borrowing From and Lending to Customers
Rule 2370

INFORMATIONAL

Borrowing From and Lending to Customers

SEC Approves NASD Rule Proposal To Govern Lending Between Registered Persons and Customers; **Effective date: November 10, 2003**

Executive Summary

On August 29, 2003, the Securities and Exchange Commission (SEC) approved the adoption of NASD Rule 2370, which prohibits registered persons from borrowing money from or lending money to a customer unless (1) the member has written procedures allowing such lending arrangements consistent with the rule; (2) the loan falls within one of five prescribed permissible types of lending arrangements; and (3) the member pre-approves the loan in writing.[1] The text of Rule 2370 is provided in Attachment A and is effective on November 10, 2003.

Questions/Further Information

Questions concerning this *Notice* may be directed to Shirley H. Weiss, Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8844.

Background

Loans between registered persons and their customers are of legitimate interest to NASD and member firms because of the potential for misconduct. NASD has brought disciplinary action against registered persons who have violated just and equitable principles of trade by taking unfair advantage of their customers by inducing them to lend money in disregard of the customers' best interests, or by borrowing funds from, but not repaying, customers.

The potential for misconduct also exists when a registered person lends money to a customer. Rule 2370 provides the mechanism by which NASD and member firms can monitor lending arrangements between registered persons and their customers.

Discussion

First, under Rule 2370, lending arrangements between registered persons and customers are prohibited unless the member has written procedures allowing such lending arrangements. Second, if permitted by the member, the lending arrangement must fall within one of five permissible types of lending arrangements. The five types of permissible lending arrangements are:

- The customer is a member of the registered person's immediate family (as defined in the rule);
- The customer is in the business of lending money;
- The customer and the registered person are both registered persons of the same firm;
- The lending arrangement is based on a personal relationship outside of the broker-customer relationship; or
- The lending arrangement is based on a business relationship outside of the broker-customer relationship.

Third, the member must pre-approve the loan in writing.

This regulatory framework will give members control over, and supervisory responsibility for, lending arrangements between their registered persons and customers. Members can choose to permit their registered persons to borrow from or lend to customers consistent with the requirements of the rule or prohibit the practice in whole or in part. Members that permit lending arrangements between their registered persons and customers are required to have written procedures in place to monitor such lending arrangements. Registered persons who wish to borrow from or lend to customers will be required to provide prior notice of the lending arrangement to the member, and the member will be required to approve the loan in writing. Members will be permitted to approve loans only if the loan falls within one of the five types of permissible lending arrangements. These requirements will enhance members' ability to supervise the activities of registered personnel.

Rule 2370 gives members the ability to prohibit all lending arrangements between their registered persons and customers. However, if permitted, Rule 2370 establishes strict conditions under which such lending arrangements may take place. Under Rule 2370, firms are required to have written procedures in place evidencing their customer loan policy, and loans will be limited to five permissible types of arrangements that might not be problematic because of the relationship between the registered person and the customer. In addition, Rule 2370 provides additional safeguards by establishing a notice and approval requirement. These requirements will enable a member, to the extent it permits these loan arrangements, to assess the nature of each proposed arrangement and decide whether to approve it. These requirements also enhance NASD's ability to review these arrangements during the examination process. The safeguards provided under Rule 2370 are in addition to the general powers that NASD has to bring a disciplinary action against a registered person who has entered into an unethical lending arrangement with a customer under NASD Rule 2110.

It is important to note that this proposal does not change the application of Regulation T to lending activities by associated persons. Specifically, the definition of "creditor" under Regulation T extends to associated persons of broker/dealers and therefore, certain loans to customers by associated persons may require compliance with the provisions of Regulation T.

Effective Date

These amendments become effective on **November 10, 2003.**

Endnotes

1 *See* Release No. 34-48242 (Aug. 29, 2003), 68 FR 52806 (Sept. 5, 2003) (File No. SR-NASD-2003-92) ("SEC Approval Order").

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ATTACHMENT A – RULE TEXT

Below is the text of the proposed rule change. Proposed new language is underlined.

* * * * *

2370. Borrowing From or Lending to Customers

(a) No person associated with a member in any registered capacity may borrow money from or lend money to any customer of the member unless: (1) the member has written procedures allowing the borrowing and lending of money between such registered persons and customers of the member; (2) the lending or borrowing arrangement meets one of the following conditions: (A) the customer is a member of such person's immediate family; (B) the customer is a financial institution regularly engaged in the business of providing credit, financing, or loans, or other entity or person that regularly arranges or extends credit in the ordinary course of business; (C) the customer and the registered person are both registered persons of the same member firm; (D) the lending arrangement is based on a personal relationship with the customer, such that the loan would not have been solicited, offered, or given had the customer and the associated person not maintained a relationship outside of the broker/customer relationship; or (E) the lending arrangement is based on a business relationship outside of the broker-customer relationship; and (3) the member has pre-approved in writing the lending or borrowing arrangement.

(b) The term immediate family shall include parents, grandparents, mother-in-law or father-in-law, husband or wife, brother or sister, brother-in-law or sister-in-law, son-in law or daughter-in-law, children, grandchildren, cousin, aunt or uncle, or niece or nephew, and shall also include any other person whom the registered person supports, directly or indirectly, to a material extent.

Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Accounting
Executive Representatives
Internal Audit
Legal & Compliance
Operations
Senior Management

KEY TOPICS

Expense-Sharing Agreements
Net Capital
Recordkeeping
SEC Rule 15c3-1
SEC Rules 17a-3, 17a-4, and 17a-5

ACTION REQUIRED

Expense-Sharing Agreements

SEC Issues Guidance on the Recording of Expenses and Liabilities by Broker/Dealers

Executive Summary

On July 11, 2003, the Securities and Exchange Commission (SEC) Division of Market Regulation (DMR) issued a letter (the "Letter") to clarify its position under SEC Rules 15c3-1, 17a-3, 17a-4, and 17a-5 (collectively, the "financial responsibility rules") regarding the treatment of broker/dealer expenses and liabilities. The Letter addresses situations in which another party has agreed to pay expenses related to the business of the broker/dealer. The Letter's requirements became effective when it was issued; however, the DMR and NASD recognize that some firms may need time to revise existing agreements and to obtain required documentation. NASD members must be able to demonstrate compliance with the requirements stated in the Letter (a copy of which is attached) by no later than December 1, 2003.

Questions/Further Information

Questions concerning this *Notice to Members* may be directed to NASD's Financial Operations Department at (202) 728-8221.

Background

Both NASD and the New York Stock Exchange (NYSE) (collectively, the self-regulatory organizations or the SROs) have become increasingly concerned that some broker/dealers are using expense-sharing agreements as a basis for not recording expenses and liabilities on the broker/dealer's books and records.[1] In such circumstances, the books and records of the broker/dealer may not accurately reflect its operating performance and financial condition and may appear to artificially inflate its profitability and, ultimately, cause it to appear to be in capital compliance when it is not. Further, such firms may continue to conduct a securities business when not in capital compliance, which is a violation of the SEC's Net Capital Rule, as well as a violation of NASD Rule 2110. In addition, as the party paying the expenses of the broker/dealer is usually not a member of an SRO, obtaining books and records related to the broker/dealer's operations can be problematic. As a result, the SROs requested guidance from the DMR concerning the application of the financial responsibility rules when a third party, which may include a parent, holding company, or affiliate of a broker/dealer, agrees to assume responsibility for payment of the broker/dealer's expenses.

Recording Certain Broker/Dealer Expenses and Liabilities

The Letter addresses nine items/requirements based on how a broker/dealer incorporates an expense-sharing agreement into its operations. For clarification, the nine requirements are repeated below with additional information provided by NASD to explain the requirements of the letter.[2]

1. Pursuant to Exchange Act Rule 17a-3(a)(1) and (a)(2), a broker-dealer must make a record reflecting each expense incurred relating to its business and any corresponding liability, regardless of whether the liability is joint or several with any person and regardless of whether a third party has agreed to assume the expense or liability. A broker-dealer must make a record of each expense incurred relating to its business, including the value of any goods or services used in its business, when a third party has furnished the goods or services or has paid or has agreed to pay the expense or liability, whether or not the recording of the expense is required by GAAP and whether or not any liability relating to the expense is considered a liability of the broker-dealer for net capital purposes. One proper method is to record the expense in an amount that is determined according to an allocation made by the third party on a reasonable basis.

> *For purposes of this Letter, expenses include all costs for which a broker/dealer would derive direct or indirect benefit and/or for which a broker/dealer would be responsible if another entity had not agreed to pay for it. This would certainly include, but not be limited to, rent, telephone, copy services, etc. A broker/dealer's business is to be understood broadly. It includes the existence of the legal entity that is registered as a broker/dealer (even when not conducting a securities business) and all of that entity's activities (whether or not the activities are securities-related).*

The last sentence of this item indicates that a broker/dealer meets the requirements of the Letter if it records its expenses as incurred in amounts determined according to a reasonable allocation, applied on a consistent basis, of the costs assumed by the third party. A reasonable allocation is one that attempts to equate the proportional cost of a service or product to the proportional use of or benefit derived from the service or product. The broker/dealer must be prepared to provide the SROs with evidence of the reasonableness of the expenses.

Members are advised that to the extent a third party pays certain expenses of a broker/dealer, particularly those costs related to compensation of its registered personnel, the third party may be required to register with the Securities and Exchange Commission as a broker/dealer in accordance with Section 15 of the Exchange Act.

Further, members are cautioned that an arbitration award rendered against the broker/dealer is a liability of the broker/dealer until it is satisfied in an appropriate manner. See Notice to Members 00-63. *NASD will consider any attempt to move the obligations associated with an unsatisfied arbitration award to a third party as a violation of NASD Rule 2110, and the firm may be subject to severe disciplinary action.*

Examples:

Fact Patterns 1 and 2:

1. *An expense agreement provides that the broker/dealer will pay a certain monthly fee to an affiliated company "in consideration of the mutual covenants and agreements to be kept and performed on the part of the parties."*

2. *An expense agreement states that the broker/dealer will pay its parent $25,000 per month for "management services and other administrative services" that the parent provides. The written agreement does not further define the services. The broker/dealer does not record any expenses such as rent, utilities, telephone, etc., and management says that all such expenses are included in the $25,000 per month fee.*

Analysis: In the computations of net capital, each broker/dealer in Fact Patterns 1 and 2 must reduce net worth by its actual expenses as if there were no expense agreement. An expense agreement must enumerate the services or products being provided to the broker/dealer, with a reasonable cost assigned to each.

Fact Pattern 3:

An expense agreement specifies that the broker/dealer will pay its holding company $1,000 per month for rent and $500 per month for utilities and telephone services. The broker/dealer occupies two floors of a three-story building, while the holding company and another affiliate occupy the third floor; the holding company pays $25,000 per month to rent the building, and pays $15,000 per month for telephones and utilities. Management states that the rent and utilities fees specified in the expense agreement are consistent with the business goals and objectives of both firms, and therefore have been allocated on a reasonable basis.

Analysis: The expenses do not appear to be allocated on a reasonable basis. In its computation of net capital, the broker/dealer must reduce net worth by expenses allocated on a reasonable basis.

2. If the broker-dealer does not record certain expenses on the reports it is required to file with the Commission or with its designated examining authority ("DEA") under the financial responsibility rules, the broker-dealer may satisfy the Exchange Act Rule 17a-3(a)(1) and (a)(2) requirement to make a record of those expenses by making a separate schedule of the expenses.

To the extent a broker/dealer reflects its expenses and liabilities as part of its general ledger, and maintains proper backup documentation relative to the expense, no other documentation would be necessary relative to items 1 and 2 above. Otherwise, the broker/dealer must maintain the "record" as noted. This record must be updated as expenses are incurred similar to those records that support the broker/dealer's financial statements.

3. If a third party agrees or has agreed to assume responsibility for an expense relating to the business of the broker-dealer, and the expense is not recorded on the reports the broker-dealer is required to file with the Commission or with its DEA under the financial responsibility rules, any corresponding liability will be considered a liability of the broker-dealer for net capital purposes unless:

a. If the expense results in payment owed to a vendor or other party, the vendor or other party has agreed in writing that the broker-dealer is not directly or indirectly liable to the vendor or other party for the expense;

b. The third party has agreed in writing that the broker-dealer is not directly or indirectly liable to the third party for the expense;

c. There is no other indication that the broker-dealer is directly or indirectly liable to any person for the expense;

d. The liability is not a liability of the broker-dealer under GAAP; and

e. The broker-dealer can demonstrate that the third party has adequate resources independent of the broker-dealer to pay the liability or expense.

The Net Capital Rule requires broker/dealers to have sufficient liquid capital to protect the assets of customers and to meet their obligations to other broker/dealers. In calculating net capital, broker/dealers begin with their net worth and then make various positive and negative adjustments. Item 3 refers to the requirement to charge a firm's net worth, in the computation of net capital, for any "liability" noted unless the broker/dealer can comply with all five conditions enumerated in 3(a) through 3(e).

Item 3 indicates that a broker/dealer cannot avoid recording the expenses it incurs as a result of its activities by arranging to have a third party assume responsibility for such expenses, if the third party lacks adequate resources independent of the broker/dealer to pay the costs incurred by the broker/dealer. Further, if the broker/dealer remits funds to such third party, the broker/dealer is viewed as being indirectly liable for the expenses assumed by the third party, and would need to reflect those expenses on the reports it is required to file with the SEC under the financial responsibility rules, as a deduction from net worth in determining net capital.

Upon entering into an expense-sharing agreement and annually thereafter, as of the broker/dealer's fiscal year-end, the broker/dealer has to obtain evidence that the third party has adequate resources independent of the broker/dealer to pay the costs incurred by the broker/dealer.

i. If the third party is a reporting company under the Securities Act of 1933 and is current on all financial filings required under that Act, the firm may rely on those filings to determine whether the third party has adequate resources apart from the broker/dealer.

ii. If the third party is not a reporting company under the Securities Act of 1933, the broker/dealer must obtain evidence pursuant to either a. or b. below, at a minimum, as well as further information as requested by NASD:

a. A signed and dated copy of a complete set of the third party's most recent audited financial statements, but in no event with an as-of date older than 12 months; or a signed and dated copy of the third party's most current required Federal income tax return as it has been filed with the Internal Revenue Service within the last 12 months.

b. If the shareholders, partners, or other owners of the third party want their abilities to infuse capital into the third party to be accepted as demonstrating adequate resources independent of the broker/dealer, they must, at a minimum, provide copies of their audited financial statements or Federal income tax returns, using the same twelve-month parameters as in a. Other additional evidence may also be required by NASD.

With respect to the third party's financial statements, if, for example, the broker/dealer and the third party have a December 31st fiscal year-end, the broker/dealer could submit a copy of the third party's financial statements as of December 31st for the year prior. If the third party's fiscal year-end were June 30th, the broker/dealer would need to provide the third party's financial statements as of June 30th for the current year.

Example:

Fact Pattern 4:

A broker/dealer has an expense agreement under which its parent pays the broker/dealer's rent of $10,000 per month, and GAAP (Generally Accepted Accounting Principles) does not require the broker/dealer to record a liability to either the vendor or the parent. The broker/dealer is unable to demonstrate to the SRO that the parent has adequate resources independent of the broker/dealer to pay the liability or expense.

Analysis: In its computation of net capital, the firm must reduce net worth by the actual $10,000 rent expense. The firm must maintain a separate record of the rent expense.

4. Any withdrawal of equity capital, as defined in paragraph (e)(4)(ii) of Exchange Act Rule 15c3-1, from a broker-dealer by a third party, other than a withdrawal described in paragraph (e)(4)(iii) of Exchange Act Rule 15c3-1, within three months before or within one year after the broker-dealer incurs an expense which the third party has paid or agreed to pay, will be presumed for net capital purposes to have been made to repay the third party for the expense of the broker-dealer, unless the broker-dealer's books and records reflect a liability to the third party relating to the expense.

Paragraph (e)(4)(iii) indicates that the notice and limitation provisions on capital withdrawals do not preclude broker/dealers from making required tax payments or paying partners reasonable compensation and that such amounts are not included in the calculation of withdrawals, advances, or loans for the purposes of these provisions.

Item 4 reaffirms the DMR's view that broker/dealers must maintain their financial records using an accrual basis of accounting. Capital withdrawals cannot be used as a means of timing the broker/dealer's recognition of the costs incurred in its operations.

5. For purposes of determining net capital, if the broker-dealer records a capital contribution from a third party that has assumed responsibility for paying an expense of the broker-dealer, and the expense is not recorded on the reports the broker-dealer is required to file with the Commission or with its DEA under the financial responsibility rules, the broker-dealer must be able to demonstrate that the recording of a contribution to capital is appropriate. Among other things, the broker-dealer must be able to demonstrate that the third party has paid the expense or has adequate resources independent of the broker-dealer to pay the expense and that the broker-dealer has no obligation, direct or indirect, to a vendor or other party to pay the expense. For net capital purposes, any equity capital withdrawn by the third party, other than a withdrawal described in paragraph (e)(4)(iii) of Exchange Act Rule 15c3-1, within three months before or one year after the broker-dealer incurs the expense, will be deemed to have been a repayment of the expense to the third party. For net capital purposes, if a contribution to capital is made to a broker-dealer with an understanding that the contribution can be withdrawn at the option of the contributor, the contribution may not be included in the firm's net capital computation

and must be re-characterized as a liability. Any withdrawal of capital as to that contributor within a period of one year, other than a withdrawal described in paragraph (e)(4)(iii) of Exchange Act Rule 15c3-1, shall be presumed to have been contemplated at the time of the contribution.

Item 5 is similar to item 4, and reaffirms the DMR's view that broker/dealers must maintain their financial records using an accrual basis of accounting. The difference in the two items relates to the type of accounting treatment that the broker/dealer uses. Item 5 applies, for example, where the broker/dealer's actual expense to a vendor or service provider was recorded on the broker/dealer's general ledger as an expense and a related liability owed to the third party; the third party then forgave the liability, and the broker/dealer removed (debited) the (forgiven) liability and credited a capital contribution from the third party.

The broker/dealer may not record the capital contribution until it demonstrates that the third party paid the expense, or has the financial wherewithal to pay the expense independent of the broker/dealer, and that the broker/dealer will not be obligated to repay the third party for any portion of the expense. To demonstrate the third party's ability to pay, the broker/dealer would need to provide the evidence discussed in the comments under item 3.

Under items 4 and 5, a firm from which capital is withdrawn as described in those items will be required to recalculate its net capital beginning at the date of the incurrence of the expense which was paid by the third party, and to provide telegraphic notice as required per SEC Rule 17a-11, if necessary, based upon the revised computation.

6. If a third party agrees or has agreed to assume responsibility for an expense of the broker-dealer, the broker-dealer must make, keep current, and preserve the following records pursuant to Exchange Act Rules 17a-3 and 17a-4:

a. If a vendor or other party has agreed that the broker-dealer is not liable directly or indirectly to the vendor or other party for an expense, a written agreement between the broker-dealer and the vendor or other party that clearly states that the broker-dealer has no liability, direct or indirect, to the vendor or other party; and

b. A record of each expense assumed by the third party.

7. A broker-dealer must make, keep current, and preserve a written expense sharing agreement between the broker-dealer and a third party that has paid or agreed to pay an expense of the broker-dealer. The agreement must set out clearly which party is obligated to pay each expense, whether the broker-dealer has any obligation, direct or indirect, to reimburse or otherwise compensate any party for paying the expense, and, when the broker-dealer records the expense in an amount that is determined according to an allocation made by the third party, the method of allocation.

8. Each broker-dealer and broker-dealer applicant must be able to demonstrate to the appropriate authorities that it is in compliance with the financial responsibility rules in connection with any expense-sharing agreement it has entered into, and therefore it may be required to provide these authorities with access to books and records, including those of unregistered entities, relating to the expenses covered by the agreement.

If the broker/dealer does not provide appropriate access to all relevant books and records, including those of a third party with which it has an expense-sharing agreement, an SRO may operate under the rebuttable presumption that the broker/dealer was not in capital compliance for the period covered by the expense-sharing agreement.

If the broker/dealer applicant does not provide appropriate access to all relevant books and records, including those of a party that has agreed to assume responsibility for paying all or a portion of the applicant's costs pursuant to paragraph (a)(7) of Membership and Registration Rule 1014, NASD will not permit the applicant to use an expense-sharing arrangement to demonstrate that it is capable of maintaining sufficient excess net capital to support its intended business operations on a continuing basis.

9. A broker-dealer must notify its DEA if it enters into, or has entered into, an expense sharing agreement and the broker-dealer does not record each of the expenses it incurs relating to its business on the reports it is required to file with the Commission or with its DEA under the financial responsibility rules. The notification must include the date of the agreement and the names of the parties to the agreement. The broker-dealer must provide a copy of the agreement to its DEA upon request.

The notification required in item 9 must be made, in writing, to a firm's assigned District Office for both existing and new expense-sharing agreements.

Endnotes

1 Expense-sharing agreements include any arrangement in which another party bears or pays for all or a portion of the costs incurred by a broker/dealer.

2 The redacted portions of the Letter, which are included in this *Notice to Members,* do not include the footnotes; a copy of the original Letter is attached to this *Notice.* The additional information provided by NASD is in italics.

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ATTACHMENT A
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Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Legal & Compliance

Senior Management

KEY TOPICS

Arbitration

INFORMATIONAL

SEC Approves Arbitrator Background Verification Process

New Arbitrator Applicants Must Undergo Background Verification and Pay Fee; **Effective October 1, 2003**

Executive Summary

On September 25, 2003, the Securities and Exchange Commission (SEC) approved a proposal to conduct background verification and charge an application fee for NASD neutral roster applicants.[1]

Questions/Further Information

Questions regarding this *Notice* may be directed to Jean I. Feeney, Vice President and Chief Counsel, NASD Dispute Resolution, at (202) 728-6959 or *jean.feeney@nasd.com;* or Barbara L. Brady, Associate Vice President and Director of Neutral Management, at (212) 858-4352 or *barbara.brady@nasd.com.*

Discussion

Background

NASD maintains a pool of approximately 7,000 available arbitrators. Arbitrator applicants submit biographical profile forms, together with two letters of reference. The biographical profile forms require applicants to provide detailed information on their business and employment histories, education, training, possible conflicts, experience, expertise, associations with industry members, and other matters. The application also requires a narrative background information statement in which applicants are asked to explain why they believe their experience and knowledge would benefit the process. Attorneys and accountants are further directed to provide specific details about their practices.

Arbitrator information is entered into NASD's database and is provided to parties in the form of a disclosure report during the arbitrator selection process. Arbitrators must update this biographical information on a regular basis. NASD sends frequent reminders to arbitrators about the importance of this obligation, especially after they are notified regarding possible service as an arbitrator. NASD requires arbitrators in each case to affirm that they have reviewed their disclosure report and that it is accurate, and to complete a disclosure checklist attached to the oath. NASD provides each arbitrator on a panel with the co-panelists' biographical profiles in order to facilitate peer reviews for accuracy.

In addition to gathering the above information, NASD currently checks records on the Central Registration Depository (CRD) for arbitrator applicants who have been registered with NASD, most of whom would be categorized as "non-public" arbitrators under NASD Rule 10308(a)(4). NASD has not verified the information provided by arbitrator applicants who do not have CRD records, most of whom would be classified as "public" arbitrators under NASD Rule 10308(a)(5).

New Background Verification Procedure

Effective October 1, 2003, NASD has expanded its verification of background information to cover all arbitrator applicants. This will provide additional protection to parties using the Dispute Resolution forum, raise the standards of the neutral roster, and enhance investor confidence in the integrity of the forum. NASD Dispute Resolution has engaged a vendor to provide the following verification services:

- Criminal check in the county of the applicant's residence;
- Federal criminal check;
- Employment verification; and
- Professional license verification.

The verification fee will be $80 per application. For this amount, the vendor will perform county and federal criminal record checks; verify any professional licenses; and check the last employer or, if the applicant has been employed for fewer than ten years by the same employer, then the last two employers. To keep the fee reasonable, NASD will assume that verification of professional licenses provides an indirect check on the applicant's education, since licensing authorities generally verify an applicant's educational history. If the applicant does not have a professional license, however, then the vendor will substitute verification of the last degree awarded.

The background verification fee will be charged for new arbitrator applications that are received by NASD after the effective date of the new procedure, which is October 1, 2003. It will not apply to arbitrators currently on NASD's arbitrator roster who wish to update information they supplied previously. Applications received after the effective date will not be processed until NASD receives the proper fee.

Effective Date

The new process is effective for arbitrator applications received after October 1, 2003.

Endnote

1. Securities Exchange Act Release No. 48541 (September 25, 2003), 68 Federal Register 56661 (October 1, 2003) (File No. SR-NASD-2003-122).

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Special Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Executive Representatives
Legal & Compliance
Registered Representatives
Senior Management

KEY TOPICS

NASD Sanction Guidelines
Rule 3030
Outside Business Activities
Rule 3040
Selling Away
Recidivists

INFORMATIONAL

Sanction Guidelines

NASD Revises *NASD Sanction Guidelines*

Executive Summary

The *NASD Sanction Guidelines* (Guidelines) are used by the various bodies that adjudicate disciplinary matters (Adjudicators) in determining appropriately remedial sanctions. NASD staff and respondents also may use these Guidelines in crafting settlements. The Guidelines were initially published in 1993 and have been periodically revised to promote consistency and uniformity in the imposition of sanctions in disciplinary matters. The Guidelines contain an introductory section that explains the purpose of NASD disciplinary sanctions and sets forth certain generally applicable principles and considerations for determining appropriately remedial sanctions. The Guidelines also specify the range of monetary and non-monetary sanctions generally used for particular violations.

This *Notice* advises NASD members and Adjudicators of modifications to: (1) *General Principles Applicable To All Sanction Determinations* regarding the concept of progressive discipline (General Principle No. 2); (2) the *Outside Business Activities - Failure to Comply With Rule Requirements* Guideline; and (3) the *Selling Away (Private Securities Transactions)* Guideline. These Guidelines and General Principle No. 2, as modified, supersede the *Outside Business Activities - Failure to Comply With Rule Requirements* and *Selling Away (Private Securities Transactions)* Guidelines and General Principle No. 2 previously published by NASD and referenced in prior *Notices to Members*. The changes are effective as of December 1, 2003, and apply to all actions as of that date, including pending disciplinary cases.

These Guidelines and General Principle No. 2, as modified, may be read in their entirety in Attachment A to this *Notice*. The revised Guidelines and General Principle No. 2 also will be available on the NASD Web Site (*www.nasdr.com*).

Questions/Further Information

Questions concerning this *Notice* may be directed to the Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8071.

Discussion

General Principle No. 2

The Guidelines advise that *General Principles Applicable to All Sanction Determinations* should be considered in connection with the imposition of sanctions in all cases. General Principle No. 2 addresses the concept of deterring future misconduct by imposing progressively escalating sanctions on respondents who have engaged in past misconduct. Although registered persons with significant histories of disciplinary events constitute a small minority of industry participants, the potential negative impact of these few individuals on public investors may be significant.

The changes to General Principle No. 2 reaffirm for Adjudicators that sanctions for recidivists should be more severe. General Principle No. 2 now clarifies, however, that more severe sanctions for recidivists need not remain within the range recommended in a particular guideline but can increase to a level beyond those recommended in a guideline. General Principle No. 2 also advises Adjudicators that progressively escalating sanctions for recidivists can include barring registered persons and expelling firms. Moreover, General Principle No. 2 advises Adjudicators always to consider a respondent's disciplinary history in determining sanctions.

Outside Business Activities - Failure To Comply With Rule Requirements (NASD Conduct Rules 2110 and 3030)

Rule 3030 requires registered persons to give their employer member firms prompt written notice of any business activity, other than a passive investment, that is outside the scope of their relationship with their firms. Private securities transactions are not covered by from this requirement and, instead, are subject to the requirements of Rule 3040.

NASD has modified the principal considerations in the *Outside Business Activities* Guideline to emphasize to Adjudicators the importance of determining whether:

- the outside activity involved customers of the firm;
- the registered person's marketing and sale of the product or service could have created the impression that the employing member firm had approved the product or service;
- the registered person misled his or her employer member firm about the existence of the outside activity or otherwise concealed the activity from the firm; and
- the outside business activity caused injury to customers of the firm.

The Guideline recommends that Adjudicators consider suspensions for up to 30 days in cases where the outside business activities do not involve aggravating conduct and suspensions of up to one year where there is aggravating conduct. In egregious cases, the Guideline recommends considering a longer suspension or a bar. Adjudicators should also consider other factors as described in the *Principal Considerations* for the *Outside Business Activities* Guideline and the *General Principles Applicable to All Guidelines*.

Selling Away (Private Securities Transactions) (NASD Conduct Rules 2110 and 3040)

Rule 3040 sets forth the reporting requirements for registered persons who wish to participate in any manner in a private securities transaction (*i.e.*, sell securities away from their firm). NASD has modified the *Selling Away* Guideline to give firms and Adjudicators guidance on the methodology to be used in determining sanctions and the factors that will be considered in determining the seriousness of the violation when the associated person has been found to have failed to comply with the requirements of Rule 3040.

The Guideline advises Adjudicators that the first step is to assess the extent of the selling away, including the dollar amount of sales, the number of customers, and the length of time over which the selling away occurred. Following this assessment, Adjudicators are advised to consider other factors as described in the *Principal Considerations* for the *Selling Away* Guideline and the *General Principles Applicable to All Guidelines*. The Guideline reminds Adjudicators that the presence of one or more mitigating or aggravating factors may either raise or lower sanctions.

With slight modifications, the five *Principal Considerations* in the previous Guideline have been kept in the revised *Selling Away* Guideline. To help Adjudicators determine appropriate sanctions, the revised Guideline adds eight new *Principal Considerations*. These include:

- a quantitative analysis of the dollar volume of sales, the number of customers, and the length of time over which the selling away activity occurred;
- whether the product sold away has been found to involve a violation of federal or state securities laws or federal, state or SRO rules;
- whether the selling away resulted in injury to the investing public;
- the extent of the respondent's involvement in the selling away, *i.e.*, whether the respondent referred customers or sold the product directly to customers and whether the respondent recruited other registered individuals to sell the product; and
- whether the respondent misled his or her employer about the existence of the selling away activity or otherwise concealed the selling away activity from the firm.

Effective Date

These Guidelines and General Principle No. 2, as modified, supersede the *Selling Away* and *Outside Business Activities* Guidelines and General Principle No. 2 published by NASD in 2002 and referenced in prior NASD *Notices to Members*. The changes are effective as of December 1, 2003, and apply to all actions as of that date, including pending disciplinary cases.

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1. Activity Away From Associated Person's Member Firm

Outside Business Activities—Failure To Comply With Rule Requirements

NASD Conduct Rules 2110 And 3030

Principal Considerations in Determining Sanctions	Monetary Sanction	Suspension, Bar or Other Sanction
See Principal Considerations in Introductory Section		
1. Whether the outside activity involved customers of the firm. 2. Whether the outside activity resulted directly or indirectly in injury to customers of the firm and, if so, the nature and extent of the injury. 3. The duration of the outside activity, the number of customers, and the dollar volume of sales. 4. Whether the respondent's marketing and sale of the product or service could have created the impression that the employer (member firm) had approved the product or service. 5. Whether the respondent misled his or her employer member firm about the existence of the outside activity or otherwise concealed the activity from the firm.	Fine of $2,500 to $50,000.[1]	When the outside business activities do not involve aggravating conduct, consider suspending respondent for up to 30 business days. When the outside business activities involve aggravating conduct, consider a longer suspension of up to one year. In egregious cases, including those involving a substantial volume of activity or significant injury to customers of the firm, consider a longer suspension or a bar.

1 As set forth in General Principle No. 6, Adjudicators may increase the recommended fine amount by adding the amount of a respondent's financial benefit.

Selling Away (Private Securities Transactions)

NASD Conduct Rules 2110 And 3040

Principal Considerations in Determining Sanctions	Monetary Sanction	Suspension, Bar or Other Sanction
See Principal Considerations in Introductory Section	*Associated Person*	*Associated Person*
1. The dollar volume of sales. 2. The number of customers. 3. The length of time over which the selling away activity occurred. 4. Whether the product sold away has been found to involve a violation of federal or state securities laws or federal, state or SRO rules. 5. Whether the respondent had a proprietary or beneficial interest in, or was otherwise affiliated with, the selling enterprise or issuer and, if so, whether respondent disclosed this information to his or her customers. 6. Whether respondent attempted to create the impression that his or her employer (member firm) sanctioned the activity, for example, by using the employer's premises, facilities, name, and/or goodwill for the selling away activity or by selling a product similar to the products that the employer (member firm) sells. 7. Whether the respondent's selling away activity resulted, either directly or indirectly, in injury to the investing public and, if so, the nature and extent of the injury.	Fine of $5,000 to $50,000.[1]	The first step in determining sanctions is to assess the extent of the selling away, including the dollar amount of sales, the number of customers, and the length of time over which the selling away occurred. Adjudicators should consider the following range of sanctions based on the dollar amount of sales: • Up to $100,000 in sales: 10 business days to 3 months • $100,000 to $500,000: 3 to 6 months • $500,000 to $1,000,000: 6 to 12 months • Over $1,000,000: 12 months to a bar Following this assessment, Adjudicators should consider other factors as described in the Principal Considerations for this Guideline and the General Principles applicable to all Guidelines. The presence of one or more mitigating or aggravating factors may either raise or lower the above-described sanctions.

Principal Considerations in Determining Sanctions	Monetary Sanction	Suspension, Bar or Other Sanction
See Principal Considerations in Introductory Section	*Member Firm*	*Member Firm*
8. Whether respondent sold away to customers of his or her employer (member firm). 9. Whether respondent provided his or her employer firm with verbal notice of the details of the proposed transaction and, if so, the firm's verbal or written response, if any. 10. Whether respondent sold away after being instructed by his or her firm not to sell the type of the product involved or to discontinue selling the specific product involved in the case. 11. Whether respondent participated in the sale by referring customers or selling the product directly to customers. 12. Whether respondent recruited other registered individuals to sell the product. 13. Whether respondent misled his or her employer (member firm) about the existence of the selling away activity or otherwise concealed the selling away activity from the firm.	Where member firm receives written notice of a private securities transaction, but fails to provide written notice of approval, disapproval, or acknowledgment, fine of $2,500 to $10,000.[2]	Where member firm receives written notice of a private securities transaction, but fails to provide written notice of approval, disapproval, or acknowledgment, consider suspending responsible supervisory personnel in any or all capacities for up to two years.

1 As provided for in General Principle No. 6, Adjudicators should increase the recommended fine amount by adding the amount of a respondent's financial benefit.

2 If the allegations involve a member's failure to supervise the selling away activity, then Adjudicators should also consider the Supervision-Failure To Supervise guideline.

General Principles Applicable To All Sanction Determinations

2. Disciplinary Sanctions Should Be More Severe For Recidivists.

An important objective of the disciplinary process is to deter and prevent future misconduct by imposing progressively escalating sanctions on recidivists beyond those outlined in these guidelines, up to and including barring registered persons and expelling firms. Adjudicators should always consider a respondent's disciplinary history in determining sanctions. Adjudicators should consider imposing more severe sanctions when a respondent's disciplinary history includes (a) past misconduct similar to that at issue; or (b) past misconduct that evidences disregard for regulatory requirements, investor protection, or commercial integrity. Even if a respondent has no history of relevant misconduct, however, the misconduct at issue may be so serious as to justify sanctions beyond the range contemplated in the guidelines, i.e., an isolated act of egregious misconduct could justify sanctions significantly above or different from those recommended in the guidelines.

Certain regulatory incidents are not relevant to the determination of sanctions. Arbitration proceedings, whether pending, settled, or litigated to conclusion, are not "disciplinary" actions. Similarly, pending investigations or the existence of ongoing regulatory proceedings prior to a final decision are not relevant.

In certain cases, particularly those involving quality-of-markets issues, these guidelines recommend increasingly severe monetary sanctions for second and subsequent disciplinary actions. This escalation is consistent with the concept that repeated acts of misconduct call for increasingly severe sanctions.

Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Legal & Compliance
Operations
Senior Management

KEY TOPICS

Margin Requirements
Regulation T
Rule 2520

Amendments to NASD Rules Regarding Margin Requirements

SEC Approves Proposed Changes to NASD Rule 2520; **Effective Date: December 1, 2003**

Executive Summary

On August 25, 2003, the Securities and Exchange Commission (SEC) approved amendments to NASD Rule 2520.[1] As amended, Rule 2520 (1) reduces the customer maintenance margin requirements for certain non-equity securities; and (2) redefines "exempt account" and permits the extension of good faith margin treatment to certain non-equity securities held in "exempt accounts"; and (3) limits the amount of capital charges a broker/dealer may take in lieu of collecting marked to the market losses.[2]

The amendments become effective on December 1, 2003. The text of the amendments is provided in Attachment A.

Questions/Further Information

Questions concerning this *Notice* may be directed to Susan M. DeMando, Director, Financial Operations, Department of Member Regulation, at (202) 728-8411.

Background And Discussion

Regulation T of the Federal Reserve Board establishes initial margin requirements for securities transactions effected in margin accounts. Regulation T also establishes margin requirements for transactions in non-equity securities held in "good faith" accounts. Such transactions are subject to the margin required by the creditor in "good faith" or the percentage set by the regulatory authority where the trade occurs, whichever is greater.[3] Consequently, the margin requirements of NASD Rule 2520 apply to non-equity positions maintained in customers' accounts.

The amendments to Rule 2520 provide for margin requirements for non-equity securities that are commensurate with the risk associated with positions in such securities held by customers. In particular, for positions not maintained in "exempt accounts," Rule 2520, as amended, reduces the customer maintenance margin requirement for certain non-equity securities and establishes a customer maintenance margin requirement of 20% of current market value for other marginable non-equity securities. The amended Rule 2520 also permits the extension of good faith margin to certain non-equity securities held in "exempt accounts" and limits the amount of capital charges a broker/dealer may take in lieu of collecting marked to the market losses.

Definitional Changes

Designated Account

The term "designated account" means the account of: a bank (as defined in Section 3(a)(6) of the Securities Exchange Act of 1934 (Act)); a savings association (as defined in Section 3(b) of the Federal Deposit Insurance Act), the deposits of which are insured by the Federal Deposit Insurance Corporation; an insurance company (as defined in Section 2(a)(17) of the Investment Company Act of 1940); an investment company registered with the SEC under the Investment Company Act; a state or political subdivision thereof; or a pension or profit sharing plan subject to Employee Retirement Income Security Act (ERISA) or of an agency of the United States or of a state or a political subdivision thereof.

Highly Rated Foreign Sovereign Debt Securities

The term "highly rated foreign sovereign debt securities" means any debt securities (including major foreign sovereign debt securities) issued or guaranteed by the government of a foreign country, its provinces, state or cities, or a supranational entity, if at the time of the extension of credit the issue, the issuer or guarantor, or any other outstanding obligation of the issuer or guarantor ranked junior to or on a parity with the issue or the guarantee is assigned a rating (implicitly or explicitly) in one of the top two rating categories by at least one nationally recognized statistical rating organization.

Investment Grade Debt Securities

The term "investment grade debt securities" means any debt securities (including those issued by the government of a foreign country, its provinces, states, or cities, or a supranational entity), if at the time of the extension of credit the issue, the issuer, or guarantor, or any other outstanding obligation of the issuer or guarantor ranked junior to or on a parity with the issue or the guarantee is assigned a rating (implicitly or explicitly) in one of the top four rating categories by at least one nationally recognized statistical rating organization.

Major Foreign Sovereign Debt

The term "major foreign sovereign debt" means any debt securities issued or guaranteed by the government of a foreign country or a supranational entity, if, at the time of the extension of credit, the issue, the issuer or guarantor, or any other outstanding obligation of the issuer or guarantor ranked junior to or on a parity with the issue or the guarantee is assigned a rating (implicitly or explicitly) in the top rating category by at least one nationally recognized statistical rating organization.

Mortgage-Related Securities

The term "mortgage-related securities" means securities falling within the definition in Section 3(a)(41) of the Act.

Exempt Account

The term "exempt account" means a member, non-member broker/dealer registered as a broker or dealer under the Act, or "designated account." In addition, an "exempt account" may be any person who has a net worth of at least $45 million and financial assets of at least $40 million for purposes of subparagraphs (e)(2)(F) and (e)(2)(G) and either: (1) has securities registered pursuant to Section 12 of the Act and has been subject to the reporting requirements of Section 13 of the Act for a period of at least 90 days and has filed all the reports required to be filed thereunder during the preceding 12 months (or such shorter period as it was required to file such reports), or (2) has securities registered pursuant to the Securities Act of 1933, has been subject to the reporting requirements of Section 15(d) of the Act for a period of at least 90 days and has filed all the reports required to be filed thereunder during the preceding 12 months (or such shorter period as it was required to file such reports); or (3) if such person is not subject to Section 13 or 15(d) of the Act, it is a person with respect to which there is publicly available the information specified in paragraphs (a)(5)(i) to (xiv), inclusive, of Rule 15c2-11 under the Act; or (4) furnishes information to the SEC as required by Rule 12g3-2(b) of the Act; or (5) makes available to the member such current information regarding such person's ownership, business, operations, and financial condition (including such person's current audited statement of financial condition, statement of income, and statement of changes in stockholder's equity or comparable financial reports), as reasonably believed by the member to be accurate, sufficient for the purposes of performing a risk analysis in respect of such person.

Non-Equity Securities

The term "non-equity securities" means any securities other than equity securities as defined in Section 3(a)(11) of the Act.

Listed Non-Equity Securities

The term "listed non-equity securities" means any non-equity securities that are listed on a national securities exchange or have unlisted trading privileges on a national securities exchange.

Other Marginable Non-Equity Securities

The term "other marginable non-equity securities" means any debt securities not traded on a national securities exchange meeting all of the following requirements: (1) at the time of the original issue, a principal amount of not less than $25,000,000 of the issue was outstanding; (2) the issue was registered under Section 5 of the Securities Act of 1933 and the issuer either files periodic reports pursuant to Section 13(a) or 15(d) of the Act or is an insurance company that meets all of the conditions specified in Section 12(g)(2)(G) of the Act; and (3) at the time of the extensions of credit, the creditor has a reasonable basis for believing that the issuer is not in default on interest or principal payments; or, "other marginable non-equity securities" means any private pass-through securities (not guaranteed by any agency of the U.S. government) meeting all of the following requirements: (1) an aggregate principal amount of not less than $25,000,000 (which may be issued in series) was issued pursuant to a registration statement filed with the SEC under Section 5 of the Securities Act of 1933; (2) current reports relating to the issue have been filed with the SEC; and (3) at the time of the credit extension, the creditor has a reasonable basis for believing that mortgage interest, principal payments, and other distributions are being passed through as required and that the servicing agent is meeting its material obligations under the terms of the offering.

Reduced Customer Maintenance Margin Requirements For Non-Equity Securities Held By Other Than Exempt Accounts

Amended Rule 2520 establishes margin requirements for investment-grade debt securities and exempted securities other than U.S. debt securities that are comparable to the highest haircut percentages under the SEC's Net Capital Rule for proprietary positions in similar securities. The margin requirements for retail customers for non-equity securities that are not held in exempt accounts are as follows:

- For investment-grade non-equity securities—reduced from 20% of current market value to 10% of current market value;
- For exempted securities other than U.S. government debt—reduced from 15% of the current market value to 7% of current market value;

- For highly rated foreign sovereign debt—the amounts specified for U.S. debt securities (1% to 6% of current market value, depending on the time to maturity);
- For all other listed non-equity securities and other marginable non-equity securities—the percentage remains at 20% of current market value or 7% of the principal amount, whichever is greater.

Good Faith Margin Treatment For Certain Non-Equity Securities Held By Exempt Accounts

Rule 2520(2)(e)(F), as amended, will permit broker/dealers to effect transactions by persons or entities that qualify as "exempt accounts" without being required to collect either margin or marked to the market losses on exempted securities, mortgage-related securities, or major foreign sovereign debt securities. However, a broker/dealer must take a capital charge for any uncollected marked to the market losses on exempt account positions in these securities.

Rule 2520(e)(2)(G), as amended, establishes a margin requirement of:

- 0.5% for transactions in exempt accounts involving highly rated foreign sovereign debt; and
- 3% for transactions in investment-grade debt.

Although a broker/dealer is not required to collect this margin, it must take a capital charge for any uncollected margin subject to the limitations provided in Rule 2520(e)(2)(H).

Limitation on Capital Charges

Rule 2520(e)(2)(H) limits the amount of capital charges a broker/dealer may take in lieu of collecting marked to the market losses. Specifically, when marked to market losses exceed either: (1) 5% of the broker/dealer's tentative net capital on any one account or group of commonly controlled accounts; or (2) 25% of the broker/dealer's tentative net capital on all accounts combined continue to exist on the fifth business day after they were incurred, the member must provide NASD with written notification and may not enter into any new transactions that would result in an increase in the amount of the excess.

Written Risk Analysis

Rule 2520(e)(2)(H) requires members to establish and maintain a "written risk analysis methodology" when extending margin on "good faith" securities transactions in "exempt accounts." This written risk methodology should include the following:

- Procedures for obtaining and reviewing the appropriate customer account documentation and the customer financial information necessary to determine exempt account status for the extension of credit under the Rule.
- Procedures and guidelines for the determination, review, and approval of credit limits to customers and across all customers who qualify as exempt accounts under the Rule.
- Procedures and guidelines for monitoring credit risk exposure to the organization relating to exempt account customers.
- Procedures and guidelines for the use of stress testing of exempt accounts in order to monitor market risk exposure from exempt accounts individually and in the aggregate.
- Procedures providing for the regular review and testing of these risk management procedures by an independent unit such as internal audit, risk management, or other comparable group.

Endnotes

1 *See* Release No. 34-48407 (File No. SR-NASD-2000-08 (August 25, 2003), 68 Federal Register 52259 (Sept. 2, 2003).

2 The provisions of the proposed rule change are consistent with revisions to New York Stock Exchange (NYSE) Rule 431 that were approved on by the SEC on August 19, 2003 (Exchange Act Rel. No. 34-48365).

3 Regulation T defines "good faith" margin as the amount of margin that a broker/dealer would require in exercising sound credit judgment.

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ATTACHMENT A

Additions are underlined; deletions are in brackets.

2520. Margin Requirements

(a) Definitions

For purposes of this paragraph, the following terms shall have the meanings specified below:

(1) through (3) No Change

(4) The term "designated account" means the account of: [a bank, trust company, insurance company, investment trust, state or political subdivision thereof, charitable or nonprofit educational institution regulated under the laws of the United States or any state, or pension or profit sharing plan subject to ERISA or of any agency of the United States or of a state or a political subdivision thereof.]

(A) a bank (as defined in Section 3(a)(6) of the Act),

(B) a savings association (as defined in Section 3(b) of the Federal Deposit Insurance Act), the deposits of which are insured by the Federal Deposit Insurance Corporation,

(C) an insurance company (as defined in Section 2(a)(17) of the Investment Company Act of 1940),

(D) an investment company registered with the Securities and Exchange Commission (SEC) under the Investment Company Act,

(E) a state or political subdivision thereof, or

(F) a pension or profit sharing plan subject to Employee Retirement Income Security Act (ERISA) or of an agency of the United States or of a state or a political subdivision thereof.

(5) through (8) No Change

(9) The term "highly rated foreign sovereign debt securities" means any debt securities (including major foreign sovereign debt securities) issued or guaranteed by the government of a foreign country, its provinces, state or cities, or a supranational entity, if at the time of the extension of credit the issue, the issuer or guarantor, or any other outstanding obligation of the issuer or guarantor ranked junior to or on a parity with the issue or the guarantee is assigned a rating (implicitly or explicitly) in one of the top two rating categories by at least one nationally recognized statistical rating organization.

(10) The term "investment grade debt securities" means any debt securities (including those issued by the government of a foreign country, its provinces, states or cities, or a supranational entity), if at the time of the extension of credit the issue, the issuer or guarantor, or any other outstanding obligation of the issuer or guarantor ranked junior to or on a parity with the issue or the guarantee is assigned a rating (implicitly or explicitly) in one of the top four rating categories by at least one nationally recognized statistical rating organization.

(11) The term "major foreign sovereign debt" means any debt securities issued or guaranteed by the government of a foreign country or a supranational entity, if at the time of the extension of credit the issue, the issuer or guarantor, or any other outstanding obligation of the issuer or guarantor ranked junior to or on a parity with the issue or the guarantee is assigned a rating (implicitly or explicitly) in the top rating category by at least one nationally recognized statistical rating organization.

(12) The term "mortgage related securities" means securities falling within the definition in Section 3(a)(41) of the Act.

(13) The term "exempt account" means: [a member, non-member broker/dealer registered as a broker or dealer under the Act, "designated account," or any person having a net worth of at least forty-five million dollars and financial assets of at least forty-million dollars.]

(A) a member, non-member broker/dealer registered as a broker or dealer under the Act, a "designated account," or

(B) any person that:

(i) has a net worth of at least forty-five million dollars and financial assets of at least forty-million dollars for purposes of subparagraphs (e)(2)(F) and (e)(2)(G), and

(ii) either:

a. has securities registered pursuant to Section 12 of the Act, has been subject to the reporting requirements of Section 13 of the Act for a period of at least 90 days and has filed all the reports required to be filed thereunder during the preceding 12 months (or such shorter period as it was required to file such reports), or

b. has securities registered pursuant to the Securities Act of 1933, has been subject to the reporting requirements of Section 15(d) of the Act for a period of at least 90 days and has filed all the reports required to be filed thereunder during the preceding 12 months (or such shorter period as it was required to file such reports), or

c. if such person is not subject to Section 13 or 15(d) of the Act, is a person with respect to which there is publicly available the information specified in paragraphs (a)(5)(i) to (xiv), inclusive, of Rule 15c2-11 under the Act, or

d. furnishes information to the Securities and Exchange Commission as required by Rule 12g3-2(b) of the Act, or

e. makes available to the member such current information regarding such person's ownership, business, operations and financial condition (including such person's current audited statement of financial condition, statement of income and statement of changes in stockholder's equity or comparable financial reports), as reasonably believed by the member to be accurate, sufficient for the purposes of performing a risk analysis in respect of such person.

(14) The term "non-equity securities" means any securities other than equity securities as defined in Section 3(a)(11) of the Act.

(15) The term "listed non-equity securities" means any non-equity securities that: (A) are listed on a national securities exchange; or (B) have unlisted trading privileges on a national securities exchange.

(16) The term "other marginable non-equity securities" means:

(A) Any debt securities not traded on a national securities exchange meeting all of the following requirements:

(i) At the time of the original issue, a principal amount of not less than $25,000,000 of the issue was outstanding;

(ii) The issue was registered under Section 5 of the Securities Act of 1933 and the issuer either files periodic reports pursuant to Section 13(a) or 15(d) of the Act or is an insurance company which meets all of the conditions specified in Section 12(g)(2)(G) of the Act; and

(iii) At the time of the extensions of credit, the creditor has a reasonable basis for believing that the issuer is not in default on interest or principal payments; or

(B) Any private pass-through securities (not guaranteed by any agency of the U.S. government) meeting all of the following requirements:

(i) An aggregate principal amount of not less than $25,000,000 (which may be issued in series) was issued pursuant to a registration statement filed with the SEC under Section 5 of the Securities Act of 1933;

(ii) Current reports relating to the issue have been filed with the SEC; and

(iii) At the time of the credit extension, the creditor has a reasonable basis for believing that mortgage interest, principal payments and other distributions are being passed through as required and that the servicing agent is meeting its material obligations under the terms of the offering.

(b)(1) through (e)(1) No change.

(e)(2) Exempted Securities, [Marginable Corporate Debt Securities] Non-equity Securities and Baskets

(A) Obligations of the United States and Highly Rated Foreign Sovereign Debt Securities

On net "long" or net "short" positions in obligations (including zero coupon bonds, i.e., bonds with coupons detached or non-interest bearing bonds) issued or guaranteed as to principal or interest by the United States Government or [issued or guaranteed] by corporations in which the United States has a direct or indirect interest as shall be designated for exemption by the Secretary of the Treasury, or in obligations that are highly rated foreign sovereign debt securities, the margin to be maintained shall be the percentage of the current market value of such obligations as specified in the applicable category below:

(i) Less than one year to maturity - 1 percent

(ii) One year but less than three years to maturity - 2 percent

(iii) Three years but less than five years to maturity - 3 percent

(iv) Five years but less than ten years to maturity - 4 percent

(v) Ten years but less than twenty years to maturity - 5 percent[, or]

(vi) Twenty years or more to maturity - 6 percent

Notwithstanding the above, on zero coupon bonds with five years or more to maturity the margin to be maintained shall not be less than 3 percent of the principal amount of the obligation.

When such obligations other than United States Treasury bills are due to mature in thirty calendar days or less, a member, at its discretion, may permit the customer to substitute another such obligation for the maturing obligation and use the margin held on the maturing obligation to reduce the margin required on the new obligation, provided the customer has given the member irrevocable instructions to redeem the maturing obligation.

(B) All Other Exempted Securities

On any positions in exempted securities other than obligations of the United States, the margin to be maintained shall be [15] 7 percent of the current market value [or 7 percent of the principal amount of such obligation, whichever amount is greater].

(C) [Non-Convertible Corporate Debt] Non-Equity Securities

On any positions in [non-convertible corporate debt] non-equity securities, [which are listed or traded on a registered national securities exchange or qualify as an "OTC margin bond," as defined in Section 220.2(t) of Regulation T of the Board of Governors of the Federal Reserve System], the margin to be maintained (except where a lesser requirement is imposed by other provisions of this Rule) shall be:

(i) 10 percent of the current market value in the case of investment grade debt securities; and

(ii) 20 percent of the current market value or 7 percent of the principal amount, whichever amount is greater, in the case of all other listed non-equity securities, and all other marginable non-equity securities as defined in paragraph (a)(16) of this Rule [except on mortgage related securities as defined in Section 3(a)(41) of the Act the margin to be maintained for an exempt account shall be 5 percent of the current market value. For purposes of this subparagraph, an exempt account shall be defined as a member, non-member broker/dealer, "designated account" or any person having net tangible assets of at least sixteen million dollars].

(D) and (E) No Change.

(F) [Cash] Transactions With [Customers] Exempt Accounts Involving Certain "Good Faith" Securities

[When a customer purchases an issued exempted security from or through a member in a cash account, full payment shall be made promptly. If, however, delivery or payment therefor is not made promptly after the trade date, a deposit shall be required as if it were a margin transaction, unless it is a transaction with a "designated account."]

On any position resulting from a transaction [in issued] involving exempted securities, mortgage related securities, or major foreign sovereign debt securities [made for a member, or a non-member broker/dealer, or] made for or with [a "designated] an "exempt account," no margin need be required and any marked to the market loss on such position need not be [marked to the market] collected. However, [where such position is not marked to the market, an amount equal to the loss at the market in such position] the amount of any uncollected marked to the market loss shall be [charged against] deducted in computing the member's net capital as provided in SEC Rule 15c3-1, subject to the limits provided in paragraph (e)(2)(H) below.

(G) Transactions With Exempt Accounts Involving Highly Rated Foreign Sovereign Debt Securities and Investment Grade Debt Securities

On any position resulting from a transaction made for or with an "exempt account" (other than a position subject to paragraph (e)(2)(F)), the margin to be maintained on highly rated foreign sovereign debt and investment grade debt securities shall be, in lieu of any greater requirements imposed under this Rule, (i) 0.5 percent of current market value in the case of highly rated foreign sovereign debt securities, and (ii) 3 percent of current market value in the case of all other investment grade debt securities. The member need not collect any such margin, provided the amount equal to the margin required shall be deducted in computing the member's net capital as provided in SEC Rule 15c3-1, subject to the limits provided in paragraph (e)(2)(H) below.

(H) Limits on Net Capital Deductions for Exempt Accounts

(i) Members [organizations] shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraphs (e)(2)(F) and (e)(2)(G) which shall be made available to the Association upon request.

(ii) In the event that the deductions of securities positions from net capital deductions taken by a member as a result of marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) (exclusive of the percentage requirements established thereunder) exceed:

a. on any one account or group of commonly controlled accounts, 5 percent of the member's tentative net capital, or

b. on all accounts combined, 25 percent of the member's tentative net capital, and, such excess exists on the fifth business day after it was incurred, the member shall give prompt written notice to the Association and shall not enter into any new transaction(s) subject to the provisions of paragraphs (e)(2)(F) or (e)(2)(G) that would result in an increase in the amount of such excess under, as applicable, subparagraph a. or b. above.

* * * * *

Notice to Members

OCTOBER 2003

SUGGESTED ROUTING

Legal & Compliance
Operations
Senior Management

KEY TOPICS

Rule 3130
Rule 3131
Rule 9160
Rule 9400 Series
Net Capital
SEC Rule 15c3-1

INFORMATIONAL

Amendments to NASD Rules Regarding the Regulation of Activities of Members Experiencing Financial and/or Operational Difficulties

SEC Approves Proposed Changes to NASD Rules 3130 and 3131, Rule 9160, and the Rule 9410 Series;

Effective Date: December 1, 2003

Executive Summary

On September 4, 2003, the Securities and Exchange Commission (SEC) approved amendments to NASD Rules 3130, 3131, 9160, and the Rule 9410 Series.[1] The amended Rules 3130 and 3131 and Rule 9410 Series permit NASD to act on an expedited basis to place restrictions on the operations of any member when NASD's Department of Member Regulation (Member Regulation) has reason to believe that the member is experiencing financial or operational difficulties or suspend the operations of any member that is not in compliance with its applicable net capital requirements.

The amendments become effective on **December 1, 2003.** The text of the amendments is provided in Attachment A.

Questions/Further Information

Questions concerning this *Notice* may be directed to Susan DeMando Director, Financial Operations, at (202) 928-8411.

Background and Discussion

Prior to these amendments, NASD's authority under Rules 3130 and 3131 was limited to the ability to direct members with a net capital requirement of $100,000 or more to either limit their business or not expand their business in order to maintain appropriate net capital levels; under these Rules, NASD did not have authority to require a member to suspend its business operations when it failed to maintain its minimum net capital.[2] Rules 3130 and 3131, as amended, and the Rule 9410 Series permit NASD to act on an expedited basis to place restrictions on the operations of **any** member, regardless of its minimum net capital requirement, when Member Regulation has reason to believe that the member is in financial or operational difficulty. These Rules also permit NASD to suspend the business operations of a member during any period of time when the member is not in compliance with its applicable net capital requirements.

Amendments to Rules 3130 and 3131

The amendments to Rules 3130 and 3131 have significantly expanded NASD's authority. Prior to the rule change, NASD could only direct members with a net capital requirement of $100,000 or more either to limit their business or not expand their business in order to maintain appropriate net capital levels. Now, under amended Rules 3130 and 3131, NASD has the authority to regulate the activities of **all** member firms subject to the requirements of SEC Rule 15c3-1 (Net Capital Rule),[3] regardless of their minimum capital requirement, and **all** member firms subject to the requirements of Section 402.2(c) (Liquid Capital Requirements for Government Securities Firms) of the rules of the Treasury Department.

Further, in addition to having authority to direct members either not to expand their business operations or to restrict their business operations, NASD may now direct members to suspend all business operations during any period of time when the member is not in compliance with its applicable net capital requirements as set forth in the SEC's Net Capital Rule or Section 402.2(c) of the rules of the Treasury Department. NASD's ability to direct members to suspend their business operations should protect investors, market participants, and the general public from the risks posed by members operating securities businesses without appropriate levels of capital.[4]

Rule 9410 Series

NASD's Rule 9410 Series provides the procedural framework for actions taken under Rules 3130 and 3131. The first step in the process requires Member Regulation to issue a notice directing a member experiencing financial and operational difficulties as described in Rules 3130 and 3131 to restrict its business activities, either by limiting or ceasing to conduct those activities. The notice will specify the grounds on which such restrictions are being imposed, the nature of the restrictions to be imposed, the effective date of the restrictions, a fitting sanction that will be imposed if the member fails to comply with any of the restrictions set forth in the notice, and the conditions for terminating such restrictions.

The member then has five days from the date of service of the notice to request a hearing. The request must state the specific grounds for withdrawing or modifying any of the restrictions specified in the notice. Generally, a request for hearing will stay the effective date of the notice. If a hearing is not requested, the restrictions prescribed in the notice become effective at least seven days after the date of service of the notice. If the member requests a hearing, the hearing must be held within 14 days of the notice. During that time, the parties will exchange exhibits and witness lists.

Within seven days after the hearing,[5] the hearing panel will issue a written decision. The decision will approve, modify, or withdraw the restrictions specified in the notice. If the decision imposes restrictions, it will state the grounds for the restrictions, the conditions for termination of the restrictions, and provide for a fitting sanction to be imposed if the member fails to comply with the restrictions. If a member does not comply with the limitations described in any effective notice or remedial action imposed by a hearing panel, Member Regulation may order the sanction set forth in the notice or specified in the hearing panel decision against the member. The member has the opportunity to request a second hearing if such sanctions are ordered.

If a member continues to experience financial or operational difficulty, Member Regulation may issue a notice imposing additional restrictions, from which the member may seek relief by filing a written application for a hearing. If Member Regulation determines that any restrictions previously imposed should be reduced or removed, Member Regulation will so advise the member by written notice. Members have the right to have the SEC review any action taken by NASD pursuant to the Rule 9400 Series; however, the filing of an application for review will not stay the effectiveness of NASD action unless the SEC orders otherwise.

Endnotes

1 *See* Release No. 34-48438 (File No. SR-NASD-2003-74) (Sept. 4, 2003), 68 Federal Register 53766 (Sept. 12, 2003).

2 NASD Rule 9512 (Summary Proceedings) is available to address severe financial or operational difficulties. However, because this procedure allows NASD to suspend a member before a hearing is held and requires authorization from the Board of Governors, it is reserved for the most serious of circumstances and generally would be inappropriate to address certain instances of net capital deficiencies.

3 Rule 15c3-1 under the Securities Exchange Act of 1934 requires that firms maintain certain specified levels of net capital. Section 402.2 of the Treasury Department rules contains liquid capital requirements for government securities broker/dealers. NASD does not set net capital requirements, but enforces these provisions as part of its regulatory function. However, Rules 3130 and 3131 effectively allow NASD to require net capital and liquid capital requirements in excess of those respective capital requirements stated above.

4 Members are reminded that notwithstanding NASD's authority under Rules 3130 and 3131 and the Rule 9400 Series to direct members that are experiencing financial and/or operational difficulties not to expand, restrict, or suspend business operations, NASD may also determine to take disciplinary action against such members when appropriate for the same conduct.

5 Rule 9160(g) was deleted because Member Regulation staff does not participate as an adjudicator in a Rule 9410 decision.

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EXHIBIT I

Below is the text of the proposed rule change. Additions are underlined; deletions are in brackets.

* * * * *

3130. Regulation of Activities of Members Experiencing Financial and/or Operational Difficulties

(a) Application—For the purposes of this Rule, the term "member" shall be limited to any NASD member [of the Association who] that is not designated to another self-regulatory organization by the Commission for financial responsibility pursuant to Section 17 of the Act and SEC Rule 17d-1 thereunder. Further, the term shall not be applicable to any member [who] that is [subject to paragraphs (a)(2)(iv), (a)(2)(v) or (a)(2)(vi) of SEC Rule 15c3-1, or is otherwise exempt from the provisions of said rule or is] subject to Rule 3131.

(b) Each member subject to SEC Rule 15c3-1 shall comply with the net capital requirements prescribed therein and with the provisions of this Rule.

[(b)] (c) A member, when so directed by [the Association] NASD, shall not expand its business during any period in which:

(1) Any of the following conditions continue to exist, or have existed, for more than 15 consecutive business days:

(A) A firm's net capital is less than 150 percent of its net capital minimum requirement or such greater percentage thereof as may from time to time be prescribed by [the Association] NASD;

(B) If subject to the aggregate indebtedness requirement under SEC Rule 15c3-1, a firm's aggregate indebtedness is more than 1,000 per centum of its net capital;

(C) If, in lieu of paragraph [(b)](c)(1)(B) above, the specified percentage of the aggregate debit items in the Formula for Determination of Reserve Requirements for Brokers and Dealers under SEC Rule 15c3-3 (the alternative net capital requirement) is applicable, a firm's net capital is less than 5 percent of the

aggregate debit items thereunder; or

(D) The deduction of capital withdrawals including maturities of subordinated debt scheduled during the next six months would result in any one of the conditions described in subparagraph (A), (B) or (C).

(2) [The Association] NASD restricts the member for any other financial or operational reason.

[(c)] (d) A member, when so directed by [the Association] NASD, shall forthwith reduce its business:

(1) to a point [enabling its available capital to comply with the standards] at which the member would not be subject to a prohibition against expansion of its business as set forth in paragraph [(b)](c)(1)(A), (B) or (C) of this Rule if any of the following conditions continue to exist, or have existed, for more than [fifteen (15)] 15 consecutive business days:

(A) A firm's net capital is less than 125 percent of its net capital minimum requirement or such greater percentage thereof as may from time to time be prescribed by [the Association] NASD;

(B) No Change.

(C) If, in lieu of paragraph [(c)](d)(1)(B) above, the specified percentage of the aggregate debit items in the Formula for Determination of Reserve Requirements for Brokers and Dealers, under SEC Rule 15c3-3 (the alternative net capital requirement) is applicable, a firm's net capital is less than 4 percent of the aggregate debit items thereunder; or

(D) If the deduction of capital withdrawals including maturities of subordinated debt scheduled during the next six months would result in any one of the conditions described in paragraph [(c)](d)(1)(A), (B) or (C) of this Rule.

(2) As required by [the Association] NASD when it restricts a member for any

other financial or operational reason.

(e) A member shall suspend all business operations during any period of time when the member is not in compliance with applicable net capital requirements as set forth in SEC Rule 15c3-1. The Department of Member Regulation may issue a notice to such member directing it to suspend all business operations; however, the member's obligation to suspend all business operations arises from its obligations under SEC Rule 15c3-1 and is not dependent on any notice that may be issued by the Department of Member Regulation.

(f) Any notice directing a member to limit or suspend its business operations shall be issued by the Department of Member Regulation pursuant to Rule 9412.

* * * * *

3131. Regulation of Activities of Section 15C Members Experiencing Financial and/or Operational Difficulties

(a) Application—For the purposes of this Rule, the term "member" shall be limited to any member of [the Association] NASD registered with the Commission pursuant to Section 15C of the Act that is not designated to another self-regulatory organization by the Commission for financial responsibility pursuant to Section 17 of the Act and Rule 17d-1 thereunder. [Further, the term shall not be applicable to any member that is subject to Section 402.2(c) of the rules of the Treasury Department, or is otherwise exempt from the provisions of said rule].

(b) Each member subject to Section 402.2 of the rules of the Treasury Department shall comply with the capital requirements prescribed therein and with the provisions of this Rule.

[(b)](c) A member, when so directed by [the Association] NASD, shall not expand its business during any period in which:

(1) Any of the following conditions continue to exist, or have existed, for more than [fifteen (15)] 15 consecutive business days:

(A) A firm's liquid capital is less than 150 percent of the total haircuts or such greater percentage thereof as may from time to time be prescribed by

[the Association] NASD.

(B) through (C) No Change.

(2) [The Association] NASD restricts the member for any other financial or operational reason.

[(c)] (d) A member, when so directed by [the Association] NASD, shall forthwith reduce its business:

(1) To a point [enabling its available capital to comply with the standards] at which the member would not be subject to a prohibition against expansion of its business as set forth in subparagraphs [(b)](c)(1)(A), (B), or (C) of this Rule if any of the following conditions continue to exist, or have existed, for more than [fifteen (15)] 15 consecutive business days:

(A) A firm's liquid capital is less than 125 percent of total haircuts or such greater percentage thereof as may from time to time be prescribed by [the Association] NASD.

(B) through (C) No Change.

(2) As required by [the Association] NASD when it restricts a member for any other financial or operational reason.

(e) A member shall suspend all business operations during any period of time when the member is not in compliance with applicable net capital requirements as set forth in Section 402.2 of the rules of the Treasury Department. The Department of Member Regulation may issue a notice to such member directing it to suspend all business operations; however, the member's obligation to suspend all business operations arises from its obligations under Section 402.2 of the rules of the Treasury Department and is not dependent on any notice that may be issued by the Department of Member Regulation.

(f) Any notice directing a member to limit or suspend its business operations shall be issued by the Department of Member Regulation pursuant to Rule 9412.

* * * * *

9160. Recusal or Disqualification

No person shall participate as an Adjudicator in a matter governed by the Code as to which he or she has a conflict of interest or bias, or circumstances otherwise exist where his or her fairness might reasonably be questioned. In any such case the person shall recuse himself or herself, or shall be disqualified as follows:

(a) through **(f)** No change.

[(g) NASD Regulation Staff As Adjudicator]

[The President of NASD Regulation shall have authority to order the disqualification of a member of the staff of the Department of Member Regulation participating in a Rule 9410 Series decision.]

* * * * *

9400. [LIMITATION] PROCEDURES FOR ACTIONS TAKEN UNDER RULES 3130 AND 3131

* * * * *

Rule 9412. Notice [of Limitations]

The Department of Member Regulation may issue a notice directing a member to [limit] restrict its business activities, either by limiting or ceasing to conduct those activities, if the Department of Member Regulation has reason to believe that [any] a condition specified in Rule 3130 or Rule 3131 exists. The notice shall specify the grounds on which such [action is being taken] restrictions are being imposed, the nature of the [limitations] restrictions to be imposed, the effective date of the restrictions [limitations], a fitting sanction that will be imposed if the member fails to comply with any [the] restrictions [limitations] set forth in the notice, and the conditions for terminating such [limitations] restrictions. The effective date of the [limitations] restrictions shall be at least seven days after the date of service of the notice. The notice also shall inform the member that it may request a hearing before the [Department

of Member Regulation] Office of Hearing Officers under Rule 9413. The Department of Member Regulation shall serve the notice by facsimile or overnight courier.

9413. Hearing Panel Review

(a) Request for a Hearing

A member subject to a notice issued under Rule 9412 may file a written request for hearing before a Hearing Panel with the Office of Hearing Officers. The request shall state the specific grounds for withdrawing or modifying any of the [limitations] restrictions specified in the notice. The request shall be filed pursuant to Rules 9135, 9136, and 9137 within five days after service of the notice under Rule 9412. The member may withdraw its request at any time by filing a written notice with the Office of Hearing Officers pursuant to Rules 9135, 9136, and 9137. The time limits set forth herein are to be strictly construed and cannot be modified except for good cause shown.

(b) No Change.

(c) Stay

Unless otherwise ordered by the NASD Board Executive Committee, the [initiation of a review under this paragraph shall stay the decision of the Department of Member Regulation or an uncontested notice until a decision constituting final action of the Association is issued] request for a hearing shall stay the effective date of the notice.

(d) through (h) No Change.

(i) Evidence Not Admitted

Evidence that is proffered but not admitted during the hearing shall not be part of the record, but shall be retained by the custodian of the record until the date when [the Association's] NASD's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

(j) Failure to Request Hearing

If a member does not request a hearing under paragraph (a), the [limitations] restrictions specified in the notice shall become effective on the date specified in the notice. Unless the Executive Committee calls the notice for review under Rule 9415, the [limitations] restrictions specified in the notice shall remain in effect until the Department of Member Regulation reduces or removes the [limitations] restrictions pursuant to Rule 9417(b).

(k) Decision

(1) Within seven days after the hearing, the Hearing Panel shall issue a written decision approving, modifying, or withdrawing the [limitations] restrictions specified in the notice. If the decision imposes [limitations] restrictions, the decision shall state the grounds for the [limitations] restrictions, the conditions for terminating such [limitations] restrictions, and provide for a fitting sanction to be imposed under Rule 9416 if the member fails to comply with the [limitations] restrictions. The Office of Hearing Officers shall promptly serve the decision by facsimile or overnight courier pursuant to Rules 9132 and 9134. The [limitations] restrictions imposed shall become effective upon service of the decision.

(2) Contents of Decision

The decision shall include:

(A) a description of the Department of Member Regulation's [decision] notice, including its rationale;

(B) a description of the principal issues regarding the imposition of [limitations] restrictions raised in the review and a statement supporting the disposition of such issues;

(C) No Change.

(D) a statement of whether the Department of Member Regulation's [decision] notice is affirmed, modified, or reversed, and a rationale therefor; and

(E) if any restrictions [limitations] are imposed:

(i) a description of the [limitations] restrictions and a statement describing a fitting sanction that will be imposed under Rule 9416 if the member fails to comply with any of the [limitations] restrictions; and

(ii) the conditions for terminating the [limitations] restrictions.

(l) Issuance of Decision After Expiration of Call for Review Period

The Hearing Panel shall provide its proposed written decision to the NASD Board Executive Committee. The NASD Board Executive Committee may call the proceeding for review pursuant to Rule 9415. If the NASD Board Executive Committee does not call the proceeding for review, the proposed written decision of the Hearing Panel shall constitute the final action of [the Association] NASD.

(m) Ex Parte Communications

The prohibitions against ex parte communications in Rule 9143 shall become effective under the Rule 9410 Series when [Association] NASD staff has knowledge the NASD Board Executive Committee intends to review a decision on its own motion under this Rule.

9414. No change.

9415. Discretionary Review by the NASD Board Executive Committee

(a) through **(c)** No change.

(d) Decision of NASD Board Executive Committee, Including Remand

After review, the NASD Board Executive Committee may affirm, modify, or reverse the proposed written decision of the Hearing Panel. Alternatively, the NASD Board Executive Committee may remand the proceeding with instructions. The NASD Board Executive Committee shall prepare a written decision that includes all of the elements described in Rule [9414(k)(2)] 9413(k)(2).

(e) Issuance of Decision

The NASD Board Executive Committee shall issue and serve its written decision on the member and the Department of Member Regulation pursuant to Rules 9132 and 9134. The decision shall be effective upon service. The decision shall constitute the final action of [the Association] NASD, unless the NASD Board Executive Committee remands the proceeding.

9416. Enforcement of Sanctions

(a) Order

If the Department of Member Regulation determines that a member has failed to comply with any [limitations] restrictions imposed by a decision or an effective notice under the Rule 9410 Series that has not been stayed, the Department of Member Regulation shall issue an order imposing the sanctions set forth in the decision or notice and specifying the effective date and time of such sanctions. The Department of Member Regulation shall serve the order on the member by facsimile or overnight courier.

(b) through (c) No Change.

(d) Decision

Within four days after the hearing, the Hearing Panel shall affirm, modify, or reverse the order issued under paragraph (a). The Office of Hearing Officers shall serve the decision on the member pursuant to Rules 9132 and 9134. The decision shall become effective upon service and shall constitute final action of [the Association] NASD.

9417. Additional [Limitations] Restrictions; Reduction or Removal of [Limitations] Restrictions

(a) Additional [Limitations] Restrictions

If a member continues to experience financial or operational difficulty specified in Rule 3130 or 3131, notwithstanding an effective notice or decision under the Rule 9410 Series, the Department of Member Regulation may impose additional [limitations] restrictions by issuing a

notice under Rule 9412. The notice shall state that the member may apply for relief from the additional [limitations] restrictions by filing a written application for a hearing under Rule 9413 and that the procedures in Rules 9413 through 9416 shall be applicable. An application for a hearing also shall include a detailed statement of the member's objections to the additional [limitations] restrictions.

(b) Reduction or Removal of [Limitations] Restrictions

If the Department of Member Regulation determines that any [limitations] restrictions previously imposed under the Rule 9410 Series should be reduced or removed, the Department of Member Regulation shall serve a written notice on the member pursuant to Rules 9132 and 9134.

9418. Application to Commission for Review

The right to have any action taken by [the Association] NASD pursuant to this Rule Series reviewed by the Commission is governed by Section 19 of the Act. The filing of an application for review shall not stay the effectiveness of the action taken by [the Association] NASD, unless the Commission otherwise orders.

9419. Other Action Not Foreclosed

Action by [the Association] NASD under the Rule 9410 Series shall not foreclose action by [the Association] NASD under any other Rule.

* * * * *

Disciplinary and Other NASD Actions

REPORTED FOR OCTOBER

NASD® has taken disciplinary actions against the following firms and individuals for violations of NASD rules; federal securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board (MSRB). The information relating to matters contained in this *Notice* is current as of the end of September 2003.

Firm Expelled, Individual Sanctioned

Investors Advocate, LLC (CRD #45801, Houston, Texas), Steven Maczka (CRD #2799300, Registered Principal, Grand Blanc, Michigan), and Jason Watkins (CRD #2242396, Registered Principal, Flint, Michigan). The firm was expelled from NASD membership and Maczka and Watkins were barred from association with any NASD member in any capacity. The sanctions were based on findings that the respondents intentionally or recklessly provided false and misleading information to NASD. In addition, the firm, acting through Maczka, conducted a securities transaction while it failed to maintain the required minimum net capital. The findings also stated that the firm, acting through Maczka, failed to maintain complete, accurate, and current books and records and filed false and inaccurate quarterly FOCUS reports. Furthermore, the firm, acting through Maczka, failed to file its audited annual financial statement and failed to respond completely to NASD requests for information. **(NASD Case #C8A020007)**

Firms Fined, Individuals Sanctioned

Andover Brokerage, LLC (CRD #33848, Montebello, New York) and Michael Picozzi, III (CRD #2504808, Registered Principal, Montebello, New York) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined $320,000, of which $300,000 is joint and several with Picozzi. Picozzi was also suspended from association with any NASD member in any capacity for 22 business days and barred from acting in any supervisory capacity with a right to re-apply after five years. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm executed short-sale transactions at or below the preceding (best) inside bid in NASDAQ National Market® (NNM®) securities. NASD also found that the firm failed to make and annotate an affirmative determination for short-sale orders and reported transactions to the Automated Confirmation Transaction Service℠ (ACT℠) as long sales when the firm's records indicate the transactions were, in fact, short sales. The findings also stated that the firm failed to maintain and preserve certain trade records relating to its short sales. In addition, NASD found that the firm and Picozzi failed to adequately supervise its short-sale transactions and failed to institute a supervisory system and establish and implement written procedures reasonably designed to prevent and detect the violations of the short sale rules. Furthermore, the findings stated that the firm failed to submit required information to the Order Audit Trail System℠ (OATS℠) on

222 business days and transmitted to OATS execution reports that contained inaccurate, incomplete, or improperly formatted data. NASD also found that the firm failed to timely report to OATS Reportable Order Events.

Picozzi's suspension began September 15, 2003, and will conclude at the close of business October 14, 2003. **(NASD Case #CMS030184)**

Wells Investment Securities, Inc. (CRD #15252, Norcross, Georgia) and Leo Fred Wells, III (CRD #1076916, Registered Principal, Alpharetta, Georgia) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined $150,000, jointly and severally with Wells. Wells was also suspended from association with any NASD member in a principal capacity for one year. Without admitting or denying the allegations, the firm and Wells consented to the described sanctions and to the entry of findings that they provided non-cash compensation worth more than $100 to registered representatives whose guests attended firm conferences and used a predetermined sales goal to determine invitees. The findings also stated that the firm and Wells provided non-cash compensation in connection with conferences that did not qualify for any training and education expense exception that prohibits persons associated with member firms from giving, or permitted to be given, anything of value in excess of $100 per individual per year where such payment or gift is in relation to the business of the recipient's firm. NASD also found that the firm and Wells provided non-cash sales incentive items in excess of $100 per person per year in connection with offerings of registered, non-traded real estate investment trusts and direct participation partnerships sold through firms with which Wells Investment Securities has contractual relationships. Furthermore, NASD found that the firm and Wells failed to adhere to previous undertakings made not to engage in non-cash compensation activities.

Wells' suspension began October 6, 2003, and will conclude at the close of business October 5, 2004. **(NASD Case #CAF030046)**

Firms and Individuals Fined

Allen C. Ewing & Co. (CRD #26102, Jacksonville, Florida) and Otis Forrest Travis, Jr. (CRD #448967, Registered Principal, Jacksonville, Florida) submitted a Letter of Acceptance, Waiver, and Consent in which they were censured and fined $10,000, jointly and severally. Without admitting or denying the allegations, the firm and Travis consented to the described sanctions and to the entry of findings that the firm, acting through Travis, conducted a securities business while failing to maintain the required minimum net capital. The findings also stated that the firm, acting through Travis, prepared a materially inaccurate net capital computation. **(NASD Case #C07030059)**

Freedom Financial Inc. (CRD #45850, Omaha, Nebraska), and Jon Patrick Pierce (CRD #1612372, Registered Principal, Omaha, Nebraska) submitted a Letter of Acceptance, Waiver, and Consent in which they were fined $15,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanction and to the entry of findings that the firm, acting through Pierce, participated in private placement contingency offerings, failed to promptly transmit funds received from investors to an appropriate escrow account, and transmitted funds received from investors to the offering before the minimum contingency was attained, thus rendering false and misleading the representations in the placement memorandum that investor funds would be returned if the minimum contingency was not attained. **(NASD Case #C04030045)**

Janssen Partners, Inc. (CRD #43940, Lake Success, New York) and Peter William Janssen (CRD #1041680, Registered Principal, Syosset, New York) submitted a Letter of Acceptance, Waiver, and Consent in which they were censured and fined $12,500. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Janssen, extended a private placement beyond the period specified in the offering memorandum without disclosing the extension to prior investors. The findings also stated that the firm, acting through Janssen, sold shares in an extended offering of the private placement, thereby increasing the total number of shares sold and the total dollar amount raised, and that the sale of additional shares rendered false the representations in the offering memorandum. In addition, NASD found that the firm, acting through Janssen, failed to establish an escrow account, for which it was a party to the escrow agreement, for the deposit of investor funds. **(NASD Case #C8A030066)**

Firms Fined

Blackbeard Securities, LLC (CRD #46748, San Francisco, California) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined $12,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to record the time of entry on order tickets and incorrectly reported, via the ACT system, principal transactions as agency transactions. The findings also stated that the firm failed to keep a written record of its "affirmative determination" obligation for short-sale transactions, and its relevant written supervisory procedures and supervisory system were not reasonably designed to achieve compliance with the transaction-reporting requirements of NASD. **(NASD Case #C01030022)**

Carey Financial Corporation (CRD #15246, New York, New York) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined $10,000. Without

admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to timely file Uniform Termination Notices for Securities Industry Registration (Forms U5) for representatives registered with NASD through the firm. **(NASD Case #C05030041)**

Carlin Equities Corporation (CRD #31295, New York, New York) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined $10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it submitted to OATS reports with respect to equity securities traded on The Nasdaq Stock Market, Inc., that were not in the electronic form prescribed by NASD. In addition, NASD found that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations, and NASD rules concerning OATS. **(NASD Case #CMS030185)**

E*Trade Professional Trading, LLC (CRD #39293, New York, New York) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured, fined $20,000, and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations concerning NASD Conduct Rule 3350 and the reporting of short-sale transactions to NASD within 30 business days. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it executed short-sale transactions in NNM securities at or below the current inside bid when the current inside bid was below the preceding inside bid in the securities. NASD also found that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws and regulations concerning NASD Conduct Rule 3350 and the reporting of short-sale transactions to NASD. **(NASD Case #CMS030201)**

Hold Brothers On-Line Investment Services LLC (CRD #36816, Jersey City, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured, fined $40,000, and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations concerning short sales and OATS within 30 business days. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to submit required information to OATS on 92 business days. NASD also found that the firm executed short-sale transactions in NNM securities at or below the current inside bid when the current inside bid was below the preceding inside bid in each of the securities. The findings stated that the firm executed short-sale transactions and failed to report each of these transactions to ACT with a short-sale modifier. In addition, NASD found that the firm executed long-sale transactions and incorrectly reported each of these transactions to ACT with a short-sale modifier. Furthermore, the findings stated that the firm executed short-sale orders and failed to properly mark the order tickets as short for those orders. NASD also found that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws and regulations concerning short sales and OATS. **(NASD Case #CMS030196)**

Peters Securities Co., L.P. (CRD #15970, Chicago, Illinois) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured, fined $19,500, and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations concerning NASD Rule 3350 within 30 business days. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it executed short-sale transactions in certain securities, all of which were NNM securities, at or below the current inside bid when the current inside bid was below the proceeding inside bid the security. NASD also found that the firm failed to report to ACT the correct symbol indicating whether the transaction was a buy, sell, sell short, sell short exempt, or cross for transactions in eligible securities. The findings also stated that the firm failed to accurately mark sale order tickets for securities listed on a national exchange as long or short. In addition, NASD found that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws and regulations concerning NASD Rule 3350. **(NASD Case #CMS030202)**

Sands Brothers & Co., Ltd. (CRD #26816, New York, New York) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured, fined $10,000, and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations concerning the Securities and Exchange Commission (SEC) and NASD firm quote rules within 30 business days. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that, as a registered market maker in securities, it failed to execute the orders upon presentment and thereby failed to honor its published quotation. In addition, NASD found the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to applicable securities laws and regulations concerning the SEC and NASD firm quote rules. **(NASD Case #CMS030192)**

Wien Securities, Corp. (CRD #10467, Jersey City, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined $20,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that, as a registered market maker in securities, it failed to execute the orders upon presentment and thereby failed to honor its published quotation. **(NASD Case #CMS030193)**

Wien Securities Corp. (CRD #10467, Jersey City, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which it was censured and fined $20,000, of which $7,500 was assessed jointly and severally. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to disclose information on an individual's Uniform Application for Securities Registration or Transfer (Form U4). NASD also found that the firm permitted an individual who was statutorily disqualified to be associated with, and conduct activities on behalf of, the firm. **(NASD Case #C9B030056)**

Individuals Barred or Suspended

Richard Allen Adler (CRD #846959, Registered Principal, Bluffon, South Carolina) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $108,948, including disgorgement of $88,948 in ill-gotten gains, and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Adler reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Adler consented to the described sanctions and to the entry of findings that he recommended unsuitable mutual fund transactions to a public customer without a reasonable basis to believe that the transactions were suitable for the customer in light of the nature of the transactions and the facts disclosed by the customer regarding her other securities holdings, financial situation, and needs.

Adler's suspension began September 15, 2003, and will conclude at the close of business September 14, 2004. **(NASD Case #C02030049)**

Robert Russell Aikens (CRD #4558740, Registered Representative, Canton, Michigan) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Aikens consented to the described sanction and to the entry of findings that he prepared and provided a forged diploma as proof that he had graduated from a university, when in fact he had not. **(NASD Case #C8A030069)**

Alexander Altman (CRD #500333, Registered Representative, Cliffside Park, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Altman consented to the described sanctions and to the entry of findings that he made payments totaling $229,243.83 to public customers to make up for the interest customers lost when bonds defaulted. NASD also found that Altman failed to disclose these payments to his member firm.

Altman's suspension began September 29, 2003, and concluded at the close of business October 10, 2003. **(NASD Case #C9B030066)**

Daniel Joseph Ashbaker (CRD #1657652, Registered Representative, O'Fallon, Illinois) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $2,500 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Ashbaker consented to the described sanctions and to the entry of findings that he participated in an outside business activity for compensation without providing prompt written notice to his member firm.

Ashbaker's suspension began September 15, 2003, and concluded at the close of business September 26, 2003. **(NASD Case #C8A030064)**

Christopher Gregory Barnes (CRD #3060496, Registered Representative, Overland Park, Kansas) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for nine months. The fine must be paid before Barnes reassociates with any NASD member or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Barnes consented to the described sanctions and to the entry of findings that he submitted a forged paramedical form in connection with an application for a variable life insurance policy for a public customer that included forged signatures, stamps of the paramedical examiner, and false information regarding the customer's health. The findings also stated that Barnes received a $5,280 commission as a result of the forged paramedical form. In addition, NASD found that the commission was rescinded after the underwriter declined the application without issuing the policy because the customer failed to submit blood and urine samples for testing.

Barnes' suspension began September 15, 2003, and will conclude at the close of business June 14, 2004. **(NASD Case #C04030047)**

Dominick Michael Bianco (CRD #2723092, Registered Principal, S. Amityville, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $30,000 and barred from association with any NASD member in any principal or supervisory capacity. Without admitting or denying the allegations, Bianco consented to the described sanctions and to the entry of findings that he failed to adequately and properly supervise the trading activity by individuals employed at his member firm. NASD also found that Bianco failed to prevent registered representatives from effecting excessive and/or unsuitable option and equity transactions in heavily leveraged margin accounts. **(NASD Case #C9B030060)**

Christian William Blake (CRD #2216784, Registered Representative, Brooklyn, New York) was barred from association with any NASD member in any capacity. The sanction

was based on findings that Blake engaged in unauthorized transactions in the account of a public customer. The findings also stated that Blake failed to respond to NASD requests to appear for an on-the-record interview. **(NASD Case #C10030012)**

Glenn Daniel Bone, III (CRD #1638202, Registered Representative, Chicago, Illinois) was barred from association with any NASD member in any capacity. The sanction was based on findings that Bone signed the name of his supervisory principal on new account applications without the principal's knowledge or consent. The findings also stated that Bone distributed unapproved sales or advertising literature and engaged in outside business activity without giving prompt written notice to his member firm. In addition, NASD found that Bone failed to respond completely to NASD requests for information and documents. **(NASD Case #C8A030022)**

Rodney Douglas Bowman (CRD #1619178, Registered Representative, Wilmington, North Carolina) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $10,000, suspended from association with any NASD member in any capacity for eight months, and required to pay $12,437.50, plus interest, in restitution to public customers. Without admitting or denying the allegations, Bowman consented to the described sanctions and to the entry of findings that he knowingly and intentionally entered priced limit orders in NASDAQ securities at prices that he knew would improve, and were intended to improve, the National Best Bid or Offer (NBBO) in such securities, in that the full price and size of such orders would be reflected in the public quotation system as the best prices and sizes at which a market participant was willing to buy or sell such securities. The findings also stated that Bowman knowingly and intentionally entered orders to buy or sell shares of such securities because he knew, and intended, that they would be routed to market makers whose automated execution systems were programmed to buy or sell, and did buy or sell, such securities on an automated basis at prices equal to the NBBO and in an amount greater than the NBBO. NASD further found that, by knowingly and intentionally engaging in this course of conduct, Bowman bought (sold) shares of these securities at prices that were lower (higher) than he would otherwise have been able to buy (sell) shares of these securities. NASD found that, immediately after Bowman received the executions of the orders that he had entered in the trading account, he intentionally and knowingly canceled priced limit orders that he had entered. The findings further stated that, in all, Bowman bought and sold these NASDAQ securities, in at least 44 instances, thereby obtaining a financial benefit of approximately $12,437.50.

Bowman's suspension began October 6, 2003, and will conclude at the close of business June 5, 2004. **(NASD Case #CMS030194)**

Jesse Jackson Bradin (CRD #2676199, Registered Representative, Manchester, Connecticut) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000, suspended from association with any NASD member in any capacity for two years, required to pay $70,300 in disgorgement of commissions, and required to pay partial restitution, plus interest, to public customers. Without admitting or denying the allegations, Bradin consented to the described sanctions and to the entry of findings that he engaged in private securities transactions without prior written notice to, or approval from, his member firm.

Bradin's suspension began September 15, 2003, and will conclude at the close of business September 14, 2005. **(NASD Case #C11030028)**

Tommy Christopher Brown (CRD #3089765, Registered Principal, Chatsworth, Arizona) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Brown consented to the described sanction and to the entry of findings that, while employed by a bank affiliated with a member firm, he withdrew $8,500 from the bank account of a public customer by signing the customer's name on a withdrawal slip without the customer's authorization. **(NASD Case #C02030053)**

Robert Thomas Bullock (CRD #1904732, Registered Representative, New Hartford, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. In light of Bullock's financial situation, no monetary sanction has been imposed. Without admitting or denying the allegations, Bullock consented to the described sanction and to the entry of findings that he engaged in private securities transactions without prior written notice to, or approval from, his member firm. The findings also stated that Bullock prepared and sent false and misleading account statements to a public customer. In addition, NASD found that Bullock, in connection with the offer and sale of stock to a public customer, made written and verbal misstatements. Furthermore, NASD found that Bullock received a $50,000 check from a public customer for investment purposes and, rather than investing the funds, he deposited the funds into an account of a company Bullock owned in part. **(NASD Case #C11030029)**

Michael James Burbage (CRD #2217929, Registered Representative, Bronxville, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Burbage consented to the described sanction and to the entry of findings that he converted $14,173.76 from the account of a public customer without the customer's prior knowledge, authorization, or consent. NASD also found that Burbage altered an internal firm document used to authorize the refund of money to customer

accounts by changing the dollar amount listed and approved by a supervisor from $488.26 to $14,488.26 in an effort to reimburse the public customer's account for the money Burbage converted. **(NASD Case #C10030068)**

Barry Francis Cassese (CRD #2080657, Registered Principal, E. Northport, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for 40 days. Without admitting or denying the allegations, Cassese consented to the described sanctions and to the entry of findings that he effected a transaction in the account of a public customer without the customer's prior knowledge, authorization, or consent.

Cassese's suspension began September 15, 2003, and will conclude at the close of business October 24, 2003. **(NASD Case #C10030070)**

Judith Van Brocklin Clarke (CRD #1014789, Registered Representative, Littleton, Colorado) submitted an Offer of Settlement in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Clarke consented to the described sanction and to the entry of findings that she failed to respond to NASD requests to appear for an on-the-record interview and to respond to NASD requests for information and documentation. **(NASD Case #C3A030027)**

Robert D'Agosta (CRD #1903105, Registered Representative, Bethlehem, Pennsylvania) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, D'Agosta consented to the described sanctions and to the entry of findings that he engaged in private securities transactions and failed to provide his member firm with prior written notification describing in detail the transaction and stating whether he had, or would receive, selling compensation in connection with the transaction.

D'Agosta's suspension began October 6, 2003, and will conclude at the close of business November 4, 2003. **(NASD Case #C02030050)**

John Joseph DePrimo (CRD #2046322, Registered Representative, Lake Ariel, Pennsylvania) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity and ordered to disgorge $46,480 of commissions in partial restitution to public customers. Restitution must be paid before DePrimo requests relief from any statutory disqualification. Without admitting or denying the allegations, DePrimo consented to the described sanctions and to the entry of findings that he engaged in outside business activities for which he received compensation without providing prior written notification to, or obtaining written approval from, his member firm. **(NASD Case #C9A030028)**

Stephen Joseph Drunasky (CRD #1476191, Registered Representative, Beaver Dam, Wisconsin) submitted an Offer of Settlement in which he was fined $10,000 and suspended from association with any NASD member in any capacity for six months. The fine must be paid before Drunasky reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Drunasky consented to the described sanctions and to the entry of findings that he engaged in outside business activities without providing his member firm with written notice of such outside business activity.

Drunasky's suspension began September 15, 2003, and will conclude on March 14, 2004. **(NASD Case #C8A030042)**

Kurtis Bradley Etherton (CRD #2039332, Registered Representative, Edina, Minnesota) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Etherton consented to the described sanction and to the entry of findings that he executed, or caused to be executed, wire transfers from the accounts of public customers to his personal account totaling $309,717.45 without the authorization, knowledge, or consent of the customers, thereby converting and/or misusing the funds for his own personal use and benefit. **(NASD Case #C04030043)**

Leon Fintz (CRD #2251978, Registered Principal, N. Bellmore, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Fintz consented to the described sanction and to the entry of findings that, acting on behalf of his member firm, he employed an accountant to perform its annual audits who was not "independent" in accordance with SEC Regulation S-X. NASD found that the individual's independence was impaired as the result of a $500,000 loan from the firm issued by Leon Fintz at the direction of his member firm. The findings also stated that Fintz concealed the existence of the loan to the auditor by posting inaccurate and misleading entries in his firm's general ledger. NASD also found that Fintz, on behalf of his member firm, prepared and filed monthly FOCUS reports that contained inaccurate and misleading information and willfully filed monthly FOCUS reports that misrepresented his firm's financial condition by including the subject $500,000 asset in the firm's financial statement. The findings also included that Fintz filed his member firm's audited financial statement on SEC Form X-17-a in which he willfully misrepresented that such statement was true and accurate. The findings also stated that the statement was materially misleading and inaccurate in that Fintz' member firm's financial statement overstated the firm's net capital position by $500,000. **(NASD Case #C9B030062)**

Thomas Paul Francis (CRD #1847184, Registered Principal, Union, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Francis consented to the described sanction and to the entry of findings that he failed to adequately and properly supervise the trading activity by individuals employed by his member firm so as to prevent securities violations. NASD also found that Francis exercised control over the account of a public customer and effected excessive securities transactions in the account using unsuitable levels of margin in a manner that was inconsistent with the customer's investment objectives. **(NASD Case #C9B030058)**

Mia H. Gilchrist (CRD #2894991, Registered Representative, Mount Laurel, New Jersey) submitted an Offer of Settlement in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Gilchrist consented to the described sanction and to the entry of findings that she submitted to her member firm the purported request of a public customer to change the address of record for the customer's account that was not made or authorized by the customer. The findings also stated that Gilchrist, acting without authorization or knowledge of a public customer, caused money market funds in the account of the customer to be liquidated and a check totaling $3,232.04 to be issued and sent to the new address of record for the account. NASD also found that, by unknown means, Gilchrist secured possession of the check and falsified, or caused to be falsified, the purported endorsement of the customer signature on the check and caused it to be deposited into the securities account of another customer. In addition, NASD determined that Gilchrist failed to respond to NASD requests for information. **(NASD Case #C9A030026)**

James Nelson Gould (CRD #872305, Registered Principal, Princeton Junction, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any principal capacity for 20 business days. Without admitting or denying the allegations, Gould consented to the described sanctions and to the entry of findings that he failed to supervise an individual engaged in fraudulent private securities transactions. The findings stated that Gould sent a letter to the individual requesting that he stop his selling away activities three months after he was requested to do so, and sent the letter to a branch office other than the one at which the individual was based. NASD also found that Gould failed to ensure that there was meaningful follow-up after the letter was sent because the individual failed to initial and return the letter as requested. In addition, NASD found that the individual continued to participate in fraudulent private securities transactions.

Gould's suspension began October 6, 2003, and will conclude at the close of business October 31, 2003. **(NASD Case #C02030052)**

Gabriel Antonio Grullon, Jr. (CRD #2287985, Registered Representative, Manhasset, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Grullon consented to the described sanction and to the entry of findings that he failed to respond to NASD requests for documents. The findings also stated that Grullon forged the signatures of public customers on bank checks, converting approximately $94,498 from their brokerage accounts for his own use and benefit without the customers' prior knowledge, authorization, or consent. **(NASD Case #C10030071)**

Richard Leroy Harden (CRD #236740, Registered Representative, Denver, Colorado) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity and ordered to pay $1,448,041 in restitution to public customers. Restitution must be paid before Harden reassociates with any NASD member or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Harden consented to the described sanctions and to the entry of findings that he participated in private securities transactions without providing written notification to, or obtaining written approval from, his member firm. NASD also found that Harden failed to respond to NASD requests for information and to appear for an NASD on-the-record interview. **(NASD Case #C3A030035)**

Kent William Helgeson (CRD #1647497, Registered Representative, Overland Park, Kansas) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Helgeson consented to the described sanction and to the entry of findings that he submitted falsified receipts and expense reports to his member firm and received payment of $8,329.12, thereby converting the funds to his own personal use and benefit. The findings also stated that Helgeson failed to respond truthfully to NASD requests for documents and information. **(NASD Case #C04030042)**

Bobby Lee Hunt (CRD #4523496, Registered Representative, Lansing, Michigan) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Hunt consented to the described sanction and to the entry of findings that he willfully failed to disclose material facts on his Form U4. **(NASD Case #C8A030046)**

Gregory Allen Jasick (CRD #1440504, Registered Representative, Grand Rapids, Michigan) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for six months. Without admitting or denying the allegations, Jasick consented to the described sanctions and to the entry of findings that he willfully failed to disclose a material fact on a (Form U4).

Jasick's suspension began September 15, 2003, and will conclude on March 14, 2004. **(CRD #C8A030065)**

Kevin Scott Jones (CRD #1504897, Registered Representative, Houston, Texas) submitted an Offer of Settlement in which he was fined $10,900, including disgorgement of $8,500 in commissions received; suspended from association with any NASD member in any capacity for 10 business days; and ordered to pay $1,600, plus interest, in restitution to a public customer. Without admitting or denying the allegations, Jones consented to the described sanctions and to the entry of findings that he recommended and effected the surrender of one variable annuity contract to finance the purchase of another variable annuity contract by a public customer in the amount of $315,000 and earned a net commission of $8,500. The findings also stated that Jones made the recommendation without having reasonable grounds for believing that the recommendation and resultant transactions were suitable for the customer based on her financial situation and needs.

Jones' suspension began September 15, 2003, and concluded at the close of business September 26, 2003. **(NASD Case #C05030015)**

Robert John Kaczorowski (CRD #2951779, Registered Representative, Branford, Connecticut) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Kaczorowski consented to the described sanction and to the entry of findings that he solicited a public customer to invest in real estate limited partnerships that did not exist, and fraudulently represented to the customer that, by investing in the purported limited partnerships, she would double her investments. The findings also stated that the customer, relying on Kaczorowski's representations, invested $10,000 in the limited partnerships, and Kaczorowski misappropriated the funds for his own use and benefit. **(NASD Case #C11030030)**

Yakov (Jack) Shulm Koppel (CRD #2448735, Registered Representative, Loch Sheldrake, New York) was suspended from association with any NASD member in any capacity for seven business days. The sanction was based on findings that Koppel committed gun jumping by soliciting a public customer to purchase securities when no registration statement was in effect or had otherwise been approved by the SEC.

Koppel's suspension began September 15, 2003, and concluded at the close of business September 23, 2003. **(NASD Case C10010004)**

Rebecca Sue Lancaster (CRD #4237068, Registered Representative, Abilene, Texas) submitted a Letter of Acceptance, Waiver, and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Lancaster consented to the described sanction and to the entry of findings that she failed to respond to NASD requests for information. **(NASD Case #C04030046)**

John Murk Lockman, Jr. (CRD #818709, Registered Principal, Maitland, Florida) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $10,000 and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Lockman reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Lockman consented to the described sanctions and to the entry of findings that he effected private securities transactions without prior notice to, or written approval from, his member firm. The findings also stated that Lockman engaged in outside business activities and failed to provide prompt written notice to his member firm.

Lockman's suspension began September 15, 2003, and will conclude at the close of business September 14, 2004. **(NASD Case #C07030058)**

Paul Douglas Maraman (CRD #2758471, Registered Representative, Omaha, Nebraska) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Maraman consented to the described sanction and to the entry of findings that he submitted, or caused to be submitted, falsified brokerage account statements on his firm letterhead to a public customer, which reflected incorrect money balances and transactions. The findings also stated that Maraman converted customer funds for his own use and benefit without their knowledge, authorization, or consent. The findings further stated that Maraman executed unauthorized transactions in the accounts of customers without their prior knowledge, authorization, or consent. NASD also found that Maraman failed to respond to NASD requests for information. **(NASD Case #C04030040)**

Jeffrey John Miller (CRD #2576559, Registered Representative, Onalaska, Wisconsin) was barred from association with any NASD member in any capacity. The sanction was based on findings that Miller recommended to, and effected securities transactions for, public customers without having reasonable grounds for believing that the recommendations and resulting transactions were suitable for the customers based on their financial situations, investment objectives, and needs. The findings also stated that Miller fraudulently misrepresented and omitted material facts in connection with the sale of securities and wrongfully retained commissions. The findings further stated that Miller failed to respond completely to NASD requests for information. **(NASD Case #C8A030026)**

Richard Craig Niece (CRD #1001706, Registered Representative, Pocatello, Idaho) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $10,000 and suspended from association with any NASD member in any capacity for three months. Without admitting or denying the allegations, Niece consented to the described sanctions and to the entry of findings that he engaged in private securities transactions without prior written notice to, and approval from, his member firm.

Niece's suspension will begin October 20, 2003, and will conclude at the close of business January 19, 2004. **(NASD Case #C3B030013)**

David Earl Peterson (CRD #1704206, Registered Principal, Irvine, California) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any principal capacity for 20 business days. Without admitting or denying the allegations, Peterson consented to the described sanctions and to the entry of findings that he failed to supervise a registered representative in a manner reasonably designed to achieve compliance with SEC and NASD rules. The findings stated that Peterson, after learning of the representative's selling away activities, ignored red flag warnings that the representative continued to sell away, consistently failed to monitor the representative's incoming and outgoing correspondence as prescribed by firm procedures, and failed to conduct required site inspections of "detached" representatives who worked out of their own offices. The findings also stated that Peterson failed to implement heightened or other special supervision of the representative who continued to participate in the sale of unregistered securities.

Peterson's suspension began October 6, 2003, and will conclude at the close of business October 31, 2003. **(NASD Case #C02030051)**

George William Phillips (CRD #362561, Registered Principal, Stony Brook, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Phillips consented to the described sanction and to the entry of findings that he pled guilty to charges that he violated Title 18, Section 1954 of the United States Code. The charges asserted that Phillips unlawfully and knowingly, directly and indirectly, gave and offered and/or promised to give and offer fees, kickbacks, commissions, gifts, money, and/or things of value in violation of said status in connection with Phillips' dealings with a member of the board of trustees of two union pension funds while registered with NASD as a general securities principal and general securities representative. **(NASD Case #C10030069)**

Thomas Michael Rohrer (CRD #858539, Registered Representative, Glenview, Illinois) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Rohrer consented to the described sanction and to the entry of findings that he recommended and effected purchases or sales of securities transactions that constituted excessive trading activity for a public customer's individual retirement account (IRA) without having a reasonable basis for believing that the recommendations and resultant transactions were suitable for the customer. The findings also stated that Rohrer purchased or sold, or caused the purchase or sale of, various securities for the IRA of a customer, without the knowledge or consent of the customer, and the absence of written or oral authorization to Rohrer to exercise discretion in the account. In addition, NASD found that Rohrer failed to provide truthful and non-misleading information during an on-the-record interview conducted by NASD. **(NASD Case #C8A030012)**

Michael Allyn Rose (CRD #2891577, Registered Principal, Lawrence, New York) submitted an Offer of Settlement in which he was required to disgorge $84,997 in commissions in partial restitution to public customers, and suspended from association with any NASD member in any capacity for two years. Restitution must be paid before Rose reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Rose consented to the described sanctions and to the entry of findings that he made purchase recommendations and failed to disclose to public customers that his compensation would include a sales credit. NASD also found that Rose predicted the future price of a common stock in order to induce public customers to follow his recommendation and made certain representations to public customers concerning his personal ownership of stock in a company, his expected compensation for the recommended transactions, the business and business prospects of the company, the company's financial circumstances and financing prospects, its expected news announcements, and the industry in which the company was a participant. Rose did not have a reasonable basis for making these representations.

Rose's suspension began September 15, 2003, and will conclude at the close of business September 14, 2005. **(NASD Case #C3A030014)**

Shawn Elliot Russell (CRD #4081056, Registered Representative, Boca Raton, Florida) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Russell consented to the described sanction and to the entry of findings that he recommended the purchase of shares of stock to public customers, made misrepresentations of material facts and unwarranted price predictions, and failed to disclose material facts to the customers. The findings also stated that Russell told a public customer that his member firm would place a stop loss

order on the stock if the price dropped below a certain point when, in fact, no such order had been placed. NASD also found that Russell placed unauthorized purchases of stock in the accounts of public customers by selling shares of another stock even though the accounts were not discretionary and Russell had no written authority to trade on discretion in these accounts. In addition, Russell failed to respond to NASD requests to appear and give testimony. **(NASD Case #CAF030045)**

David Lloyd Rutkoske (CRD #1496393, Registered Principal, Allen, Texas) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity with a right to reapply after three years. Without admitting or denying the allegations, Rutkoske consented to the described sanction and to the entry of findings that, acting through his member firm, he participated in the sale of unregistered securities. The findings also stated that, while engaged in a continuous distribution of stock, Rutkoske actively bid for, purchased, and attempted to induce others to purchase stock during the distribution period in violation of SEC Regulation M. NASD also found that Rutkoske controlled and participated with his member firm in charging unfair and fraudulent markups in the sale of stocks. In addition, NASD found that Rutkoske failed to respond to NASD requests for information or documents. **(NASD Case #CAF020012)**

John Battista Sacco (CRD #2410017, Registered Representative, Brooklyn, New York) was barred from association with any NASD member in any capacity and ordered to pay $10,000 in restitution to a public customer. The sanctions were based on findings that Sacco induced a public customer to invest $10,000 in securities and made misrepresentations and omissions of material fact regarding the company's ownership and pending public offerings of stock. The findings also stated that Sacco participated in private securities transactions without prior written notice to his member firm. NASD also found that Sacco failed to respond to NASD requests for information. **(NASD Case #C10030005)**

Ramzi J. Sarkis (CRD #2280252, Registered Representative, Randolph, Massachusetts) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Sarkis consented to the described sanction and to the entry of findings that he engaged in an outside business activity without prompt written notice to his member firm. The findings also stated that Sarkis failed to respond to an NASD request to appear for an on-the-record interview. **(NASD Case #C11030032)**

Juan C. Sarmiento (CRD #4421729, Associated Person, Passaic, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Sarmiento consented to the described sanction and to the entry of findings that he willfully failed to disclose material facts on his Form U4. **(NASD Case #C9B030061)**

Tonya Marie Scott (CRD #3253312, Registered Representative, Columbus, Ohio) submitted a Letter of Acceptance, Waiver, and Consent in which she was fined $2,500, suspended from association with any NASD member in any capacity for 20 business days, and ordered to disgorge $1,423.51, plus interest, in unjust profits or ill-gotten gains to a public customer. The fine and disgorgement amount must be paid before Scott reassociates with any NASD member in any capacity following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Scott consented to the described sanctions and to the entry of findings that she met with a public customer to discuss the investment of proceeds of a life insurance policy for which the customer was the beneficiary, and negligently misrepresented the details of a mutual fund to the customer, thereby inducing the customer to invest the life insurance policy proceeds in the mutual fund. The findings also stated that Scott received $1,423.51 in commissions as a result of the customer's investment.

Scott's suspension began September 15, 2003, and concluded at the close of business October 10, 2003. **(NASD Case #C8B030016)**

Linda Joan Shenko (CRD #2324137, Registered Representative, Whitesboro, New York) was barred from association with any NASD member in any capacity. The sanction was based on findings that Shenko converted public customer funds. **(NASD Case #C11030014)**

Kathleen Whorley Sommer (CRD #2750036, Registered Representative, Phoenix, Arizona) submitted an Offer of Settlement in which she was barred from association with any NASD member in any capacity, and ordered to disgorge $22,500 in commissions earned in partial restitution to public customers. Restitution must be paid before Sommer reassociates with any NASD member or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Sommer consented to the described sanctions and to the entry of findings that she participated in outside business activities without providing written notice to her member firm. NASD also found that Sommer appeared for an NASD on-the-record interview and failed to answer staff questions. **(NASD Case #C3A030009)**

Edwardo Xavier Sosa (CRD #2703160, Registered Representative, New York, New York) submitted an Offer of Settlement in which he was fined $7,500 and suspended from association with any NASD member in any capacity for 20 business days. Without admitting or denying the allegations, Sosa consented to the described sanctions and to the entry of findings that he opened brokerage accounts in the names of

public customers and purchased, or caused to be purchased, shares of common stock and warrants into the accounts without the customers' authorization.

Sosa's suspension began September 2, 2003, and concluded at the close of business September 29, 2003. **(NASD Case #CAF020071)**

Christopher Kenneth Stirk (CRD #2957284, Registered Representative, Bothell, Washington) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Stirk consented to the described sanction and to the entry of findings that he converted $12,313.15 in public customer funds to his own use and benefit. NASD also found that Stirk sold, or caused to be sold, bonds from the account of public customers without the customers' knowledge or authorization and in the absence of written or oral authorization to exercise discretion in the account. **(NASD Case #C3B030012)**

Frank Sullivan (CRD #4186907, Registered Representative, Patchogue, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for 30 days. The fine must be paid before Sullivan reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Sullivan consented to the described sanctions and to the entry of findings that he failed to respond to NASD requests for information in a timely manner.

Sullivan's suspension began September 15, 2003, and concluded at the close of business October 14, 2003. **(NASD Case #CLI030019)**

Janice Poland Tanno (CRD #365017, Registered Representative, Hudson, Ohio) submitted a Letter of Acceptance, Waiver, and Consent in which she was suspended from association with any NASD member in any capacity for three months. In light of the financial status of Tanno, no monetary sanctions have been imposed. Without admitting or denying the allegations, Tanno consented to the described sanction and to the entry of findings that she participated in private securities transactions and failed and neglected to give written notice of her intention to engage in such activities to her member firm, and failed to receive written approval from her firm prior to engaging in such activities.

Tanno's suspension began September 15, 2003, and will conclude December 14, 2003. **(NASD Case #C8B030017)**

Jeffrey James Tegethoff (CRD #2768285, Registered Representative, St. Louis, Missouri) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Tegethoff consented to the described sanction and to the entry of findings that he failed to respond to NASD requests for information. **(NASD Case #C04030044)**

Regan Andrea Tegge (CRD #2488648, Registered Principal, Sea Cliff, New York) submitted a Letter of Acceptance, Waiver, and Consent in which she was fined $20,000 and suspended from association with any NASD member in any principal and supervisory capacity for one year. Tegge must also requalify by exam as an options principal and a general securities principal before serving again in either capacity. The fine must be paid before Tegge reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Tegge consented to the described sanctions and to the entry of findings that she failed to adequately and properly supervise the options trading activity of various individuals employed by her member firm so as to prevent violations of securities laws, regulations, and NASD rules.

Tegge's suspension began October 6, 2003, and will conclude at the close of business October 5, 2004. **(NASD Case #C9B030057)**

Thomas Michael Tiernan, Jr. (CRD #1010579, Registered Principal, West Islip, New York) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Tiernan consented to the described sanction and to the entry of findings that he failed to adequately and properly supervise the trading activity of individuals employed by his member firm in that he permitted registered representatives to effect excessive and/or unsuitable option and equity transactions in heavily leveraged margin accounts. **(NASD Case #C9B030059)**

Bruce Lynn Troyer (CRD #2567737, Registered Representative, Lake St. Louis, Missouri) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000, ordered to pay $87,250, plus interest, in restitution to public customers, and barred from association with any NASD member in any capacity. The fine must be paid before Troyer reassociates with any NASD member following the bar or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Troyer consented to the described sanctions and to the entry of findings that he participated in private securities transactions for compensation and failed to provide his member firm with detailed written notice of the transactions, his role therein, and to receive permission from his member firm to engage in the transactions. The findings also stated that Troyer received checks totaling $28,000 from public customers to be invested, and, without the knowledge or consent of the customers, endorsed and

deposited the checks into an account under his control, thereby converting customers funds to his own use and benefit. In addition, the findings stated that Troyer received a $5,000 check from a representative on behalf of a public customer to be invested, endorsed and deposited the customer's check into his personal bank account, held the funds for a period of time, and invested the funds at a later time, thereby misusing customer funds. **(NASD Case #C04030049)**

Joan Eileen Vaccaro, (CRD #4251895, Registered Representative, Pompton Plains, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Vaccaro consented to the described sanction and to the entry of findings that she was suspended from a job as an accountant with an employer for failing to inform them that she was employed by an NASD member firm. NASD also found that Vaccaro falsely claimed that she had lost wages from the accounting position as a result of the September 11, 2001, World Trade Center disaster when she applied for benefits from the Federal Emergency Management agency (FEMA), in which she falsely claimed that she had lost wages from the accounting position as a result of the September 11, 2001 World Trade Center disaster. The findings also stated that Vaccaro willfully failed to amend her Form U4 to disclose material facts. **(NASD Case #C9B030064)**

David Lowell Walch (CRD #1242890, Registered Principal, Provo, Utah) submitted a Letter of Acceptance, Waiver, and Consent in which he was suspended from association with any NASD member in any capacity for 18 months. In light of the financial status of Walch, no monetary sanction has been imposed. Without admitting or denying the allegations, Walch consented to the described sanction and to the entry of findings that he recommended and effected high-risk mutual fund transactions for public customers without having reasonable grounds for believing that the recommendations and resultant transactions were suitable for the customers on the basis of the customers' financial situation and needs.

Walch's suspension will begin October 20, 2003, and will conclude at the close of business April 19, 2004. **(NASD Case #C06030019)**

Paul Clifford Wentzlaff (CRD #1811761, Registered Representative, Sioux Falls, South Dakota) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $5,000 and suspended from association with any NASD member in any capacity for two years. The fine must be paid before Wentzlaff reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Wentzlaff consented to the described sanctions and to the entry of findings that he engaged in outside business activities and failed to provide prompt written notice to his member firm and the compensation he was receiving for these transactions.

Wentzlaff's suspension began October 6, 2003, and will conclude at the close of business October 5, 2005. **(NASD Case #C04030048)**

Gary David Winter (CRD #1533705, Registered Principal, Fresno, California) submitted a Letter of Acceptance, Waiver, and Consent in which he was suspended from association with any NASD member in capacity for one month. In light of the financial status of Winter, no monetary sanction has been imposed. Without admitting or denying the allegations, Winter consented to the described sanction and to the entry of findings that he recommended and effected the sale of a $180,000 deferred variable annuity contract to a public customer without having reasonable grounds for believing that the recommendation and resultant sale were suitable for the customer on the basis of the customer's financial situation, investment objectives, and needs. The findings also stated that Winter recommended and effected the sale to a public customer of a variable life insurance contract that was unsuitable because the amounts invested were insufficient to cover the annual cost, and the customer had insufficient income or other available funds to otherwise pay the cost of insurance charges.

Winter's suspension began October 6, 2003, and will conclude at the close of business November 5, 2003. **(NASD Case #C05030044)**

Richard Scott Wood (CRD #2158798, Registered Principal, Wichita, Kansas) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in capacity. Without admitting or denying the allegations, Wood consented to the described sanction and to the entry of findings that he converted customers' funds in that, without the knowledge or consent of public customers, he transferred, or caused to be transferred, funds from the public customers' credit union accounts to an account under his control. The findings also stated that Wood partially failed to respond to NASD requests for information. **(NASD Case #C04030041)**

Gina Jie Wu (CRD #4544811, Registered Representative, Irvine, California) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Wu consented to the described sanction and to the entry of findings that she willfully misrepresented a material fact on her Form U4. **(NASD Case #C02030046)**

Steven Dean Yarn (CRD #1745954, Registered Principal, Randallstown, Maryland) submitted a Letter of Acceptance, Waiver, and Consent in which he was fined $10,000, ordered to pay $120,000 in restitution to a public customer, and suspended from association with any NASD member in any capacity for six months. The fine must be paid before Yarn reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Yarn consented to the described

sanctions and to the entry of findings that he participated in private securities transactions outside the scope of his association with his member firm and without providing prior written notice of such activities to his member firm.

Yarn's suspension began October 6, 2003, and will conclude at the close of business April 5, 2004. **(NASD Case #C9A030027)**

Brent L. Zimmerman (CRD #4549694, Associated Person, Altoona Pennsylvania) submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Zimmerman consented to the described sanction and to the entry of findings that he willfully failed to disclose material facts on a Form U4 and failed to respond to NASD requests for information. **(NASD Case #C9A030030)**

Decisions Issued

The following decisions have been issued by the DBCC or the Office or Hearing Officers and have been appealed to or called for review by the NAC as of September 5, 2003. The findings and sanctions imposed in the decision may be increased, decreased, modified, or reversed by the NAC. Initial decisions whose time for appeal has not yet expired will be reported in the next *Notices to Members.*

Davrey Financial Services, Inc. (CRD #38914, Tacoma, Washington) and Pravin Roy Davrey (CRD #2243197, Registered Principal, Tacoma, Washington). Davery Financial Services, Inc. ("firm") is censured, fined $35,000, and required to submit all of its proposed advertising to NASD's Advertising Regulation Department for "pre-use" approval for a period of two years. Pravin Davrey is suspended from association with any NASD member in any capacity for two years and ordered to requalify by exam as a financial and operations principal (FINOP) before again serving in such capacity. The sanctions were based on findings that the firm, acting through Davrey, failed to maintain accurate books and records, in that the firm made payments out of its operating account to certain shareholders pursuant to the terms of two Stock Redemption Agreements, but did not record the corresponding liability on the firm's books and records. NASD found, in addition, that Davrey allowed the firm to engage in a securities business when the firm did not meet its minimum net capital requirement. NASD also found that the firm, acting through Davrey, made exaggerated, unwarranted, and misleading statements, and that Davrey failed to provide specific warnings and disclosures required in advertisements regarding options. In addition, NASD determined that Davrey failed to submit every advertisement pertaining to options to NASD's Advertising Regulation Department at least 10 days prior to use, and failed to include in the advertisement certain required information about how an investor can obtain an Options Disclosure Document, as required by SEC Exchange Act Rule 134.

This case is on appeal to the National Adjudicatory Council (NAC), and the sanctions are not in effect pending consideration of the appeal. (NASD Case #C3B020015)

Complaints Filed

The following complaints were issued by NASD. Issuance of a disciplinary complaint represents the initiation of a formal proceeding by NASD in which findings as to the allegations in the complaint have not been made, and does not represent a decision as to any of the allegations contained in the complaint. Because these complaints are unadjudicated, you may wish to contact the respondents before drawing any conclusions regarding the allegations in the complaint.

Robert Michael Dooley (CRD #2735594, Registered Representative, Highlands Ranch, Colorado) was named as a respondent in an NASD complaint alleging that he made unsuitable recommendations to a public customer to purchase mutual funds, without having a reasonable basis for believing that the recommendations were suitable based on the customer's circumstances and needs. **(NASD Case #C3A030036)**

Doyle Scott Elliott (CRD #1727061, Registered Principal, Anna Maria, Florida) was named as a respondent in an NASD complaint alleging that he received $35,000 from a public customer for investment purposes, failed to deposit the funds into an account at his member firm, and provided the customer with trade confirmations purporting to confirm sell transactions in stock from Elliott's account at his member firm. The complaint also alleges that the trade confirmations were fictitious, Elliott did not have an account at his member firm, and the transactions did not occur at his member firm. In addition, the complaint alleges that Elliott failed to provide the customer with the proceeds from any securities transactions and failed to return any of the $35,000 to the customer. The complaint also alleges that Elliott failed to respond to NASD requests for information. **(NASD Case #C07030057)**

Salvatore John Fabrizio (CRD #2505827, Registered Representative, Long Island City, New York) was named as a respondent in an NASD complaint alleging that he executed transactions in the accounts of public customers without their knowledge, authorization, or consent. The complaint also alleges that Fabrizio failed to respond to NASD written requests for information and documentation, but did provide information responsive to the requests during an NASD on-the-record interview. **(NASD Case #C10030073)**

Maxine Elaine Fowler (CRD #2416814, Registered Representative, Greer, South Carolina) was named as a respondent in an NASD complaint alleging that she made misrepresentations in selling long-term, callable certificates of deposit (CDs) to public customers, in that Fowler made customers believe they were buying CDs with short-term

maturities. The complaint also alleges that Fowler failed to respond to NASD requests for information. **(NASD Case #C05030043)**

Gordon Philip Lewis (CRD #1443906, Registered Representative, Lakeport, California) was named as a respondent in an NASD complaint alleging that he recommended and effected transactions in a public customer's account without having reasonable grounds for believing that his recommendations were suitable for the customer based on the facts disclosed by the customer as to her other securities holdings, financial situation, and needs. The complaint also alleges that Lewis prepared and submitted to his member firm order tickets that falsely represented that the purchases were unsolicited when, in fact, they were solicited. In addition, the complaint alleges that Lewis paid $24,000 to a customer for the losses suffered by the customer without disclosing the payment to his member firm. **(NASD Case #C01030026)**

Sampson McKie, III (CRD #4209727, Associated Person, Staten Island, New York) was named as a respondent in an NASD complaint alleging that he caused $1,072.94 in a public customer's funds to be moved from his account with his member firm into his personal account at the firm without authorization. The Complaint also alleges that McKie withdrew the funds from the account for his own personal use. **(NASD Case #C9B030055)**

Gregory Alan Newton (CRD #2714180, Registered Representative, Tucson, Arizona) was named as a respondent in an NASD complaint alleging that he made unsuitable recommendations to public customers without having a reasonable basis for believing that the recommendations were suitable based on information provided to him about the customers' financial situation, needs, and other security holdings. **(NASD Case #C3A030037)**

Stephen Michael O'Donnell (CRD #1931363, Registered Representative, Brooklyn, New York) was named as a respondent in an NASD complaint alleging that he intentionally or recklessly failed to disclose materially adverse information to public customers. The complaint also alleges that O'Donnell intentionally or recklessly failed to disclose to customers his financial incentive for recommending a stock. In addition, the complaint alleges that O'Donnell acted in contravention of Section 10(b) of the Securities Exchange act of 1934 and Rule 10b-5, promulgated thereunder, in that, by use of the means or instrumentalities of interstate commerce or of the mails, or of any facility of any national securities exchange, he employed a device, scheme, or artifice to defraud; omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading; or engaged in acts, practices, or a course of business which operated or could operate as a fraud or deceit upon persons in connection with the recommendations he made to customers. **(NASD Case #C3A030039)**

Rahman Rose (CRD #4466642, Registered Representative, Central Islip, New York) was named as a respondent in an NASD complaint alleging that, while exercising effective control over a public customer's account, he effected or caused to be effected excessive purchase and sale transactions in the customer's account. The complaint also alleges that Rose, by the use of the means of instrumentalities of interstate commerce or of the mails, knowingly or recklessly used or employed, in connection with the purchase or sale of securities, manipulative or deceptive devices or contrivances; and knowingly or recklessly effected transactions in, or induced the purchase or sale of, securities by means of manipulative, deceptive, or other fraudulent devices or contrivances. In addition, the complaint alleges that Rose recommended purchase and sale transactions to a public customer without having reasonable grounds for believing that such transactions were suitable for the customer in view of the size and frequency of the transactions, the nature of the account, and the customer's financial situation and needs. The complaint further alleges that Rose failed to respond to NASD requests to appear for an on-the-record interview. **(NASD Case #C9B030063)**

Terrence Richard Sprague (CRD #1612506, Registered Representative, Seattle, Washington) was named as a respondent in an NASD complaint alleging that he made misrepresentations of material facts in selling long-term, callable CDs to public customers. The complaint also alleges that Sprague failed to respond to NASD requests for information. **(NASD Case #C05030045)**

Brett James Sandman (CRD #4018124, Registered Representative, Boca Raton, Florida) was named as a respondent in an NASD complaint alleging that he failed to disclose material facts and made material misrepresentations to public customers in his solicitation of the customers to purchase shares of stock that were highly speculative and not registered with the SEC. The complaint also alleges that Sandman failed to perform adequate due diligence on the stock. The complaint further alleges that Sandman failed to respond to NASD requests to appear for testimony. **(NASD Case #CAF030044)**

Robert Tedeschi (CRD #2616329, Registered Principal, Brooklyn, New York) was named as a respondent in an NASD complaint alleging that he intentionally or recklessly failed to disclose materially adverse information to public customers in connection with his recommendation that they purchase a stock, and failed to disclose his financial incentive for recommending the stock. The complaint also alleges that Tedeschi acted in contravention of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, promulgated thereunder, in that, by use of the means or instrumentalities of interstate commerce, or of the mails, or of any facility of any national securities exchange, he employed a device, scheme, or artifice to defraud; omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading; or engaged in acts, practices, or a course of business

which operated, or could operate, as a fraud or deceit upon persons, in connection with the recommendations he made to customers. **(NASD Case #C3A030038)**

Yankee Financial Group, Inc. (CRD #17966, Melville, New York), Richard Francis Kresge (CRD #729077, Registered Principal, Bay Shore, New York), and Gary Joseph Giordano (CRD #2722480, Registered Principal, Brooklyn, New York) were named as respondents in an NASD complaint alleging that the firm, Kresge, and Giordano entered into an oral agreement and, in connection with the purchase or sale of securities and by the use of means or instrumentalities of interstate commerce or by the mails, directly or indirectly, knowingly or recklessly employed devices, schemes, or artifices to defraud; made untrue statements of material facts or omission to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or engaged in acts, practices, or courses of business which operated, or would operate, as a fraud or deceit upon any person. Furthermore, the complaint alleges that the firm, acting through Kresge and Giordano, egregiously failed to supervise the sales activities and other highly suspicious conduct of the brokers and unregistered individuals in the firms and allowed the firms to operate without any written supervisory procedures. The complaint also alleges that the firm failed to report customer complaints to NASD. In addition, the complaint alleges that the firm, acting through Kresge, allowed an unregistered person to participate in discussions and decision-making about the division of responsibilities for the operation, management, and supervision of branch offices, and allowed the individual to have branch employees remain on the premises and to operate the branch office on a daily basis. **(NASD Case #CMS030182)**

Firm Expelled for Failing to Pay Fines and/or Costs in Accordance with NASD Rule 8320

M.A. Berman Co.
Boca Raton, Florida
(August 20, 2003)

Firm Suspended for Failure to Supply Financial Information

The following firm was suspended from membership in NASD for failure to comply with formal written requests to submit financial information to NASD. The action was based on the provisions of NASD Rule 8221. The date the suspension commenced is listed after the entry. If the firm has complied with the requests for information, the listing also includes the date the suspension concluded.

E Street Access
Englishtown, New Jersey
(August 7, 2003)

Suspension Lifted

NASD has lifted the suspension from membership on the date shown for the following firm because it has complied with formal written requests to submit financial information.

Clarity Securities, Inc.
Miami, Florida
(August 7, 2003)

Individuals Barred Pursuant to NASD Rule 9544 for Failure to Provide Information Requested Under NASD Rule 8210.

(The date the bar became effective is listed after the entry.)

Boston, Michael A.
S. Richmondhill, New York
(August 20, 2003)

Bridges, III, William
Florence, South Carolina
(August 27, 2003)

Bruteyn, Jeffrey Charles
Dallas, Texas
(August 27, 2003)

Burgdorf, Richard B.
Birmingham, Alabama
(August 25, 2003)

Glikberg, Carmen
Chicago, Illinois
(August 26, 2003)

Gomez, IV, Jose Angel
Miami Beach, Florida
(August 27, 2003)

Guirand, Gary D.
Baldwin, New York
(August 20, 2003)

Hedberg, Russell Glen
Rockford, Illinois
(August 13, 2003)

Kanabroski, Daniel J.
Union, Kentucky
(August 14, 2003)

Robinson, Paul,
Marietta, Georgia
(August 6, 2003)

Ross, William M.
Uniondale, New York
(August 28, 2003)

Individuals Suspended Pursuant to NASD Rule 9541(b) for Failure to Provide Information Requested under NASD Rule 8210.

(The date the suspension began is listed after the entry. If the suspension has been lifted, the date follows the suspension date.)

Brisbin, May Yan
Denton, Texas
(August 12, 2003)

Cobb, Edward Peter
Glen Rock, New Jersey
(August 11, 2003)

Cohen, Alvin Marc
Irvine, California
(August 12, 2003)

Eltzroth, Geoffrey
Marion, Indiana
(August 13, 2003)

Frambes, Steven C.
Dunn Loring, Virginia
(August 25, 2003)

Gura, Lee
Vista, California
(August 11, 2003)

Jin, Yanshi Rock
Vienna, Virginia
(August 5, 2003)

Larue, David E.
West Palm Beach, Florida
(August 14, 2003)

Nelson, Thomas E.
Scottsdale, Arizona
(August 7, 2003)

Plata, Edwin
Lodi, New Jersey
(August 18, 2003)

Tran, Jack
Boca Raton, Florida
(August 13, 2003)

Wolf, Tim Lee
Chandler, Arizona
(August 26, 2003)

Young, Christopher K.
Shreveport, Louisiana
(August 5, 2003)

Individual Suspended Pursuant to NASD Rule Series 9510 for Failure to Comply With an Arbitration Award or a Settlement Agreement

(The date the suspension began is listed after the entry. If the suspension has been lifted, the date follows the suspension date.)

Vogt, Michael
Riverhead, New York
(August 7, 2003 – August 13, 2003)

Individuals Suspended Pursuant to NASD Rule Series 9514(g) for Failure to Comply With an Arbitration Award or a Settlement Agreement

(The date the suspension began is listed after the entry. If the suspension has been lifted, the date follows the suspension date.)

Bendetsen, Brookes M.
Burlingame, California
(August 5, 2003 – September 15, 2003)

Dirks, Raymond L.
New York, New York
(August 5, 2003 – September 3, 2003)

Tye, Walter A.
Boca Raton, Florida
(August 5, 2003)

Visconti, Joseph C.
Palm Beach, Florida
(August 5, 2003)

Individuals Revoked for Failing to Pay Fines and/or Costs in Accordance with NASD Rule 8320

Adler, Len
Brooklyn, New York
(August 20, 2003)

Gillen, Frank J.
Salt Lake City, Utah
(August 20, 2003)

Gregory, Richard S.
Allen, Texas
(August 20, 2003)

Komorsky, Adolph
Tarrytown, New York
(August 20, 2003)

Travis, David T.
Aurora, Colorado
(August 20, 2003)

NASD Fines Morgan Stanley $2 Million for Prohibited Mutual Fund Sales Contests; Managing Director of Firm's Retail Sales Force Also Fined for Supervisory Violations

NASD announced today that it had censured and fined Morgan Stanley DW Inc. $2 million for conducting prohibited sales contests for its brokers and managers to promote the sale of Morgan Stanley mutual funds and a selected few variable annuities. Between October 1999 and December 2002, the firm conducted 29 contests, and offered or awarded various forms of non-cash compensation to the winners, including tickets to Britney Spears and Rolling Stones concerts, tickets to the NBA finals, tuition for a high-performance automobile racing school, and trips to resorts.

Morgan Stanley conducted at least two national contests, 10 regional contests, and 17 branch contests that violated NASD conduct rules. The 29 contests violated NASD rules because they favored Morgan Stanley's own proprietary mutual funds. The estimated value of the contest rewards totaled $1 million.

NASD also charged Morgan Stanley and the head of its retail sales division, Bruce F. Alonso, with supervisory violations. Morgan Stanley failed to have any supervisory systems or procedures in place to detect and prevent this widespread misconduct. In fact, NASD found that the firm did not have any systems or monitoring procedures in place until January of this year. Alonso, who led the effort to promote MSDW proprietary mutual funds, failed to supervise the sales force to prevent the sales contest violations in question. He was censured and fined $250,000.

"It is not acceptable for NASD-regulated firms to hold contests for prizes that promote the sale of one fund, especially their own, over other mutual fund products," said Mary L. Schapiro, NASD's Vice Chairman and President of Regulatory Policy and Oversight. "NASD rules are designed to prevent brokers from placing their interest in receiving lucrative rewards over the investment needs of their customers.

"NASD also requires firms to establish supervisory systems and procedures to achieve proper compliance. Morgan Stanley's failure to have any related systems or procedures in place allowed this misconduct to occur."

In enacting the non-cash compensation rules, the SEC and NASD recognized that the types of sales contests seen in this case increased the potential for investors to be steered into investments that are less suitable than some alternatives. These rules were designed to prevent the conflicts of interest that might arise for the broker when faced with such a choice.

NASD's investigation found that national managers at Morgan Stanley pressured regional managers to meet sales goals, and regional managers, in turn, pressured branch managers to meet these goals. The prohibited sales contests were a by-product of that pressure.

For example, in July 2002, the firm initiated a sales campaign called "Finding the Right Fit." The goal of that campaign was to achieve sales of $5 billion of Morgan Stanley funds for the fourth quarter of fiscal year 2002. As part of that campaign, national managers encouraged regional managers to meet specific sales goals. To achieve these national sales goals, four regions each held prohibited sales contests.

In one case, the Southeast Region sponsored a contest in which the top-producing branch managers could win a trip to New York City. This contest, which was held on a monthly basis, set a goal of $100,000 per financial advisor in sales of Morgan Stanley mutual funds.

In June 2002, Morgan Stanley conducted a national sales campaign focusing on one of its new mutual funds, the Morgan Stanley Small-Mid Special Value Fund. As part of that campaign, national management set a sales goal of $500 million within the first month of the campaign. The national managers also required 100 percent participation in the campaign by all regions and branches of the firm. The firm offered rewards including dinner hosted by senior national management in New York City or travel and entertainment expense reimbursements to the managers of the top producing regions.

Regional managers held contests to meet the sales goals. For instance, the Regional Director of the Southeast Region set a sales target of $75 million in total sales of the Small-Mid Special Value Fund, consisting of $50,000 for each financial advisor in each branch office in the region. To help achieve that sales target, the Southeast Regional Director offered the top three branch managers a trip to Sea Island, Georgia, for dinner and golf school. In another contest, the Southern California Regional Director offered tickets to a 2002 NBA finals game involving the Los Angeles Lakers, and attendance at a due diligence meeting at a Four Seasons resort.

The branch managers, in turn, created their own contests in order to meet their offices' sales goals. They provided rewards to the top-producing financial advisors in their branches. The branch manager of the Alexandria, Virginia, office offered all-expenses paid vacations to Hawaii and the Caribbean. However, these rewards ultimately were cancelled. The branch manager of the Santa Ana, California, office offered Britney Spears concert tickets, retail gift certificates, and travel and entertainment expense reimbursements.

Morgan Stanley paid regional and branch managers a significant portion of their compensation as bonuses, consisting of "Management Incentive Compensation" and "Challenge Goal" bonuses. These were based, in part, on regional and branch

managers' ability to promote sales of Morgan Stanley mutual funds and meet their sales goals, as set by senior management, including Alonso.

Branch managers' compensation was tied directly to the profitability of their branches. Branches retained a significantly greater percentage of revenue on sales of Morgan Stanley mutual funds than other funds.

Morgan Stanley apparently attempted to shield this focus on sales of its own mutual funds from the public as much as possible to avoid public relations ramifications. This is evidenced from electronic mail messages by a regional manager directing branch managers and other employees to refrain from putting in writing details regarding contests promoting Morgan Stanley mutual funds. Former branch managers corroborated this policy.

In settling these charges, Morgan Stanley and Alonso neither admitted nor denied the charges.

NASD Sanctions Wells Investment Securities and its President For Non-Cash Compensation Rule Violations

NASD has sanctioned Wells Investment Securities, Inc., a sponsor of real estate investment trusts (REITs), for rewarding broker/dealer representatives who sell their REITs with lavish entertainment and travel perquisites, in violation of NASD rules. NASD censured Wells Investment and its President, Leo Wells, and fined them $150,000. NASD also suspended Leo Wells from acting in a principal capacity for one year.

NASD prohibits REIT sponsors from rewarding broker/dealer representatives from other firms with entertainment, gifts or other non-cash compensation. These practices create point-of-sale incentives that may undermine a representative's ability to objectively recommend suitable investments to customers. These payments directly from the REIT sponsor also could interfere with the ability of the representatives' own firms to supervise their sales activities.

"Our non-cash compensation rules help ensure that members and their representatives make recommendations that are in the best interest of their customers," said Mary Schapiro, Vice Chairman of NASD. "This case makes clear that NASD will not tolerate any payment of non-cash compensation that runs afoul of those rules."

Wells Investment, based in Norcross, Georgia, is affiliated with Wells Real Estate Funds, Inc., which is primarily involved in the acquisition and management of office buildings and other commercial properties. These projects are funded through the sale of REIT and direct participation program (DPP) offerings managed by Wells Investment and sold through other broker/dealers. To date, Wells Investment has managed four REIT offerings, which have raised investor proceeds in excess of $3 billion, and 13 DPPs, which have raised investor proceeds in excess of $300 million.

In 2001 and 2002, Wells Investment sponsored conferences in Scottsdale, Arizona, and Amelia Island, Florida, which were attended by broker/dealer representatives from other firms who sold its REIT products. Although Wells Investment represented to NASD that these conferences were "strictly educational," they actually constituted lavish affairs that did not meet the standards of NASD rules. For example, Wells Investment provided broker/dealer representatives with a Friday night "sock hop," a "beach bash," and dinner at a Civil War fort with costumed Civil War heroes, fireworks, fife and drum players, skydivers, and a cannon reenactment. Wells Investment also invited the representatives' guests to many of these events, and paid for the guests' food, transportation, lodging, and golf fees. Wells Investment provided less than 13 hours of training and education during the three full days of each conference.

In settling this matter, Wells Investment and Wells neither admitted nor denied the allegations, but consented to the entry of findings and imposition of sanctions.

NASD Charges Long Island Firm, its President, and Two Former Managers as a Result of Fraudulent "Boiler Room" Sales Practices; Eleven Others Barred in Related Conduct

NASD has filed a complaint charging Yankee Financial Group, Inc., of Melville, NY, its President, and a former branch manager with engaging in high-pressure, boiler-room type sales practices that defrauded investors of $8 million. NASD also permanently barred 11 other individuals, who worked for Yankee Financial and two other firms, for related fraudulent conduct.

NASD charged that, in the fall of 2001, Richard F. Kresge, Yankee Financial's President and majority owner, opened offices in Brooklyn and Staten Island. Brokers in these offices used high-pressure sales tactics, including misrepresentations, baseless price predictions, and omissions of material facts, to persuade investors to purchase shares of three highly speculative Over-the-Counter Bulletin Board (OTCBB) securities: Silver Star Foods, Inc.; Western Media Group Corp.; and Golden Chief Resources, Inc. In many instances, Yankee Financial brokers targeted sales of these stocks to the elderly and others for whom they were patently unsuitable.

NASD charged Yankee Financial and Kresge with fraudulent sales practices and unsuitable recommendations of these securities, as well as failing to supervise these branch offices and to establish any written supervisory procedures.

Gary Giordano, former Yankee Financial branch office manager, was charged with fraud for making unsuitable recommendations and for failing to supervise brokers in the Brooklyn and Staten Island offices. Charges against Joseph C. Korwasky, Yankee

Financial's former compliance officer, included failing to report customer complaints to NASD as required and charges related to the firm's written supervisory procedures he agreed to produce.

NASD surveillance of the OTCBB and subsequent investigation of the market activity in the three securities identified a number of other individuals, some affiliated with Yankee Financial and others with Sierra Brokerage Services and Argus Securities, who improperly pressured customers to purchase shares or otherwise participated in this scheme. As a result of NASD's investigation, 11 individuals were permanently barred, including:

- Kenneth Gliwa, Yankee Financial's former Vice President, who settled charges that he failed to supervise the firm's branch offices, allowed two unregistered persons to hire brokers and operate the Brooklyn and Staten Island branch offices, failed to conduct any meaningful review of the three securities to determine whether they were suitable investments for the firm's customers, and allowed the firm to operate without any written supervisory procedures;
- Jeffrey Richardson, Sierra's President and head trader, settled charges that he participated in an unlawful distribution of unregistered shares, which generated millions of dollars for offshore entities controlled by the two individuals who owned and operated Yankee Financial's Brooklyn and Staten Island branch offices;
- Lawrence Dugo, a Yankee Financial broker, and Samuel Barmapov, an Argus broker, settled charges that they used fraudulent sales practices in recommending shares to investors; and
- Joseph Ferragamo, one of the owners of the Yankee Financial branch offices; Yankee Financial brokers David Anderson (a.k.a. Vasily Kouznetsov), Eric Cenname, and Adam Klein; John Cook, Argus' former President; John Klukewycz, a former Argus branch manager; and Ilan Shteinberg, a former Argus broker were charged with failing to appear and testify in connection with NASD's investigation.

Under NASD rules, a firm or individual named in a complaint can file a response and request a hearing before an NASD disciplinary panel. Possible remedies include a fine, censure, suspension, or bar from the securities industry, disgorgement of gains associated with the violations, and payment of restitution.

NASD Charges Continental Broker-Dealer Corp. and its Executives with Sales Practice and Supervision Violations

NASD has filed a complaint against Continental Broker-Dealer Corp. of Carle Place, NY, for widespread violations of securities laws, including allowing Gregory M. Hasho to be its "de facto" owner and operator despite his previous SEC bar that prevented him from holding a supervisory and proprietary position in any securities firm. The NASD complaint also charged a former Continental registered representative, Rahman Rose, with executing numerous unsuitable, excessive, and fraudulent securities transactions involving high levels of margin and failing to appear for NASD testimony.

NASD also announced it had settled disciplinary actions with ten former employees of Continental.

NASD's investigation revealed Continental, at Hasho's direction, devised an unsuitable options trading strategy designed to generate commissions from customers. The promotion of this strategy, along with the lapse in proper supervision by the firm, resulted in widespread and egregious sales practice abuses by Rose and several other Continental registered representatives. The sales practice violations included unsuitable and excessive trading in customer accounts and the excessive use of margin. As a result of this violative conduct, many customers lost most or all of their principal investments, resulting in approximately $5 million in losses, while the firm and its registered representatives reaped commissions in excess of $5.3 million.

Continental had no enforced supervisory structure in place and therefore failed to ensure that designated principals performed their supervisory duties, NASD charged in the complaint. This lack of supervision and compliance with NASD rules and federal securities laws pervaded the firm and enabled Hasho to run Continental from 2000 to 2003 even though the SEC had barred him from acting as a supervisor in 1995. NASD's investigation revealed that Hasho actively managed and supervised Continental by participating in firm management decisions, directing substantial payments from Continental's bank accounts to third parties and by reviewing customer accounts.

Continental also failed to have its 2001 and 2002 annual audits performed by an independent public accountant, as required by NASD rules. The auditing firm's accountant was not independent because he had an outstanding $500,000 personal

loan from Continental. In addition, to conceal the existence of that loan, Continental employees posted false entries in its general ledger and filed false financial reports with the SEC and NASD.

NASD also settled five disciplinary actions against Continental's former President, Thomas Tiernan; Chief Compliance Officer, Dominick Bianco; Chief Financial Officer, Leon Fintz; Registered Options Principal, Regan Tegge; and the New Jersey Office Branch Manager, Thomas Francis.

Tiernan, Bianco, Tegge, and Francis were charged with failing to supervise registered representatives in connection with unsuitable and excessive trading in customer accounts. Fintz was charged as a result of his involvement with the improper loan to Continental's outside auditor, and his participation in the posting of false accounting entries in the firm's books and records and in reports filed with the SEC and NASD. Tiernan, Francis, and Fintz were barred from the securities industry in all capacities; Bianco was barred from acting in a principal capacity and fined $30,000; and Tegge was suspended in a principal capacity for one year, fined $20,000, and ordered to requalify prior to returning to the securities industry.

NASD has also settled disciplinary actions with five former Continental registered representatives and received a default decision against a sixth registered representative after filing a complaint. All six were charged with engaging in unsuitable recommendations, excessive trading in customer accounts and excessive use of margin:

- Joseph Mucci, George Difuilo, and Daren Deluca each received a six-month suspension.
- Mario Forte received a five-month suspension.
- Leonardo Balzano received a ten-month suspension.
- Kenneth Rodgers was barred from association with a member firm in any capacity.

Under NASD rules, an individual or firm charged in a complaint can file a response and request a hearing before an NASD disciplinary panel. Possible sanctions include a fine, censure, suspension, expulsion, or bar from the securities industry, in addition to the request made by NASD in the complaint that the respondents give up any ill-gotten gains and pay restitution.

All individuals involved in settlements relating to this case agreed to the sanctions while neither admitting nor denying the allegations.